economic development

Economic Development Department
REPUBLIC OF SOUTH AFRICA

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Economic Development Budget Vote, 2017

A note to accompany the Budget Speech

Overview

2016 was a challenging year for economic development globally and domestically but significant progress was also registered in South Africa. The economy avoided going into a recession in part through the collective action of business, labour and communities working with government, though growth remained very modest.

It was a year when rating agencies were focussing on South Africa, with a downgrade in April 2017 – after the end of the financial year.

The Economic Development Department played a major role in ensuring a co-ordinated infrastructure investment programme and in expanding the levels of development finance in the economy, rallying stakeholders around certain policy and programmes that will have major impact on our economy, as well as ensuring that government responds in an informed and more aligned manner across the three spheres to the challenges of the economy.

A mid-term review of the New Growth Path jobs drivers was completed for Parliament's Portfolio Committee on Economic Development, and the latest data shows that more than 2,4 million new jobs had been created in the period since the adoption of the NGP in 2010.

Key highlights in the work of the Ministry included:

- the innovative and extensive public interest conditions attached to a number of mergers including AB InBev's takeover of SAB Miller, Coca-Cola and Edcon (Part 1)
- the actions in the steel industry including the tough competition settlement with Arcelor Mittal and the reparation agreement with the seven largest construction companies (Part 2)
- the expansion of investment by the Industrial Development Corporation and the agreement to co-invest in a new auto plant in Nelson Mandela Bay (Part 3) and
- the increased investment in the National Infrastructure Plan, projected at R987 billion over the next three years (Part 4)

Details of these are found in attached specific short briefing notes.

Economic transformation was a key theme in 2016 and we made significant strides in opening the economy to new black-owned companies and expanding levels of youth entrepreneurship.

The Ministry of Economic Development is responsible for the work of the Economic Development Department (EDD), the Industrial Development Corporation (IDC), the International Trade Administration Commission (ITAC), the Competition Commission, the Competition Tribunal and the work of the Secretariat and Technical Unit of the Presidential Infrastructure Coordinating Commission (PICC). Highlights of the work of the Ministry and its agencies are reported below.

Impact of the work of economic development

87 187 positive jobs impact

A total of **61 250 jobs** were covered by job-protection commitments or investments directed at saving jobs and an additional **25 937 jobs** (minimum) are expected to be created as a result of the transactions involving the IDC, Competition Commission, ITAC and EDD.

Development funding and fines: R4.8 billion

R4.8 billion was committed by the companies listed below in development spending or major penalties (excluding the value of the BEE commitments):

- Coca-Cola: R800 million commitment
- AB Inbev: R1 billion commitment
- Construction Cartel: R1.5 billion payment (excluding the previous fine of R1.4 billion)
- AMSA: R1.5 billion fine

BEE transaction value facilitated: R19 billion

- IDC approvals to BEE empowered-companies: R10.1 billion
- BEE component of Coca-Cola merger: R2 billion
- Construction industry: value of transaction over seven years in ownership equity: R5 billion
- AMSA BEE partnership: R1.8 billion

Opening the market

More than 120 000 small spaza shops and taverns will be given the right to stock and display products from competitor brewers and soft-drink bottlers, opening the market for beverages in the boldest way yet in SA retail history

Part 1

Briefing note on competition interventions and settlements

During 2016, the Ministry of Economic Development concluded settlements with AB InBev, CCBA (Coca-Cola Bottling Africa), Edcon, Clicks, Arcelor Mittal and seven construction companies. These are major transactions that introduced either new public interest obligations on mergers, provided for funding for developmental projects or supported actions by the competition authorities against collusion in specific industries.

In addition, the Ministry facilitated the introduction from 1 May 2016, of new criminalisation provisions against collusion and cartel conduct in the economy, with stiff jail sentences of up to 10 years.

Some of the key transactions and settlements concluded in 2016 included:

AB InBev's purchase of SAB Miller, which had the following, public interest commitments:

- R1 billion to promote new employment outside its core operations, including
  - R610 million facility to support small, emerging farmers through which 800 new farmers will be developed, with total employment gain of 2 600 workers
  - Support for entrepreneurship and social programmes in South Africa - turning SA from a net importer to a net exporter of beer inputs
- Retention of the current 6 000 jobs of the workforce for at least five years and providing protection against retrenchment
- Opening up competition by craft brewers through granting them access to 10% of fridge space in taverns
- Developing low-alcohol and no-alcohol choices for the SA market
- Committing to the location of the African headquarters in South Africa.

Locations for three model farm programmes have been established and at least one model farm will be completed in 2017. A programme for supplier development is being established targeting micro-enterprises, small/medium enterprises as well as black industrialists. A dedicated incubation centre will also be established in Bryanston. The company is also introducing new learnerships and scholarships in engineering and agriculture in order to contribute to sustainable livelihoods in South Africa.

Coca-Cola merged three bottling operations, and after's EDD's engagement included commitments to:

- Retain the current 7 500 jobs for a three year period and provide for protection against retrenchments for specified categories of staff
- Provide R800 million funding to create new jobs in its value-chains, of which a R400 million facility will support small, emerging farmers as well as packaging companies, and a further R400 million is available to support the opening of new spaza shops and retail outlets
- Set aside 20% of the equity in Appetizer and 20% equity in Coca-Cola Beverages Africa for black South Africans
- Open up 10% of the fridge-space in coolers and display cabinets owned or financed by Coca-Cola in 117 000 spaza-shops and small retail outlets, to facilitate access for smaller and rival soft-drink bottlers
- Deepen localisation of its local supply-chain including commitments to retain the production base of Appetizer in South Africa.

Black Economic Empowerment

Since the merger, 17.5% of Appetizer has been sold to African Pioneer Group (APG) and a black entrepreneur will take up 4% shares to realise a total BEE share of 21.5%.

Localisation

In 2015 Coca-Cola Beverages South Africa (CCBSA) was sourcing all fruit locally except for grape juice concentrate. Through implementing the agreement to further develop and support local farmers in the Upington Region, and partnering with Orange Rive Cellars, CCBSA has increased its local sourcing of grape juice concentrate from 9% to 43%.

CCBSA is in the process of identifying additional local farmers to develop, in order to meet the target of 80% local sourcing by 2020. This is equivalent, in today's terms, to sourcing approximately 1.8 million litres of Grape Juice Concentrate, which requires 530 ha of planted grapes. Every 2 ha planted has the potential to employ 1 person.

The Edcon Group notified the Competition Commission of a merger, to address amongst others, conversion of debt to equity and a transfer of ownership of the company to its creditors. After Ministry engaged the Edcon Group, the company included commitments to:

- Support the local clothing, footwear and textile industry
- Retain 43 630 current jobs in the company subject to market conditions
- Grow the number of new jobs in its retail and manufacturing operations by 2 000 workers.

EDD has monitored the implementation of commitments. To date Edcon has:

- Employed an additional 2 226 people (Edgars 800; Jet 1 232 and Speciality 194)
- Replaced imports with the following locally manufactured items:
    - Footwear - 930 000 units
    - Hosiery - 278 000 units
    - Intimate wear - 109 000 units

Part 2

Seven construction companies (Murray & Roberts, Aveng, WBHO, Group Five, Steffanutti Stocks, Raubex and Basil Read) committed to promote transformation in the construction sector, when they signed an agreement with government in October 2016. This Settlement Agreement has 3 components:

- Financial contributions by the companies of R1.5 billion to development projects in addition to a R1,4 billion penalty for past collusion
- Deep transformation through the sale of equity or providing support for the development of black construction companies that will place many billions of rands in share-value or contracts in the hands of black South Africans
- Integrity commitments by the company CEOs to take all steps to avoid collusion and corruption in their dealings with the state, their competitors and their customers and to partner with government in exposing all forms of corruption and tender irregularities.

This agreement will help to turn a new page of partnership between major players in the industry found guilty of collusion on the one hand, and government and the society at large on the other. Details of the transformation plans have been publicly announced by all of the companies.

Four of the companies have opted to sell equity to black South Africans and three are in discussion or have concluded agreements with emerging construction partner-companies to increase the turnover of these black-owned companies within seven years.

The companies have paid their first tranche of R117 million in terms of the Settlement Agreement into the National Revenue Fund. These monies will be appropriated each year to a Trust to support bursaries for black students studying engineering, quantity surveying and building science; bursaries for black artisans; maths and science education in public schools; social development projects such as rural bridges and schools; building capacity in the state towards public infrastructure; and enterprise development programmes for small, black owned construction firms.

ArcelorMittal, which was fined R1.5 billion by the Competition Tribunal during 2016, was required to:

- Commit to fresh capital spending of R4.6 billion to upgrade its plant and equipment in South Africa
- Curb price increases through limiting its earnings before profit and tax to 10%
- Limit retrenchments in its operations.

Progress since this agreement: ArcelorMittal reported that R1 billion has been invested in capital upgrades.

Support to the steel sector

During 2016 the Ministry and EDD-agencies focussed on a range of measures to retain steel manufacturing in South Africa. A **Steel Task-team** developed a coordinated set of measures to address the impact of the global glut of steel on the local industry, the past collusive practices and the need to have a secure supply of steel. These included trade, competition and investment measures. A **Pricing Committee** was also set up with representatives across the value-chain to monitor steel pricing and Arcelor Mittal's adherence to a range of reciprocal commitments it made in relation to tariff support including increased investment, retention of jobs and pricing commitments.

In reality, the sector is quite diverse consisting of a number of sub-sectors such as foundries, fabricators and component manufacturers each with their own sub-industries and market environments. Structural factors such as a lack of fixed investment in modern plant and equipment, under-investment in skills and R&D appear to be common elements in the industry's decline across sub-sectors. The current cyclical downturn characterised by weak export demand and stiff import competition in a domestic environment of rising costs has only served to accelerate the sector's troubles.

To address this, EDD has established a **Downstream Steel Industry Competitiveness Fund** to assist qualifying enterprises in the downstream steel sectors to improve their competitiveness. The Fund will be applied to finance the following initiatives, which directly address competitiveness issues:

- Modernisation of plant machinery and equipment;
- Upgrade of plant machinery and equipment to meet quality assurance requirements;
- Capacity expansion of existing plants;
- Process improvements for cost efficiencies and productivity and to assist with plant optimisation;
- Working capital requirements or revolving facility;
- Assist firms to achieve appropriate industry quality certification and standards including environmental standards;
- Establishment of start-up enterprises; and

- Development and testing of prototypes, as well as the testing and certification of new products (for example by SABS or international certification where appropriate).

The IDC will leverage the total R95 million allocation from EDD over 3 years, to create a R1.5 billion Fund, **in the form of an interest rate subsidy to normal IDC risk pricing,** aimed at improving downstream competitiveness for qualifying firms in the Metals and Engineering sub-sectors.

The Fund will selectively target manufacturing firms in the steel-intensive downstream sectors:

- Foundry industries;
- Fabrication sectors (focused on pressure vessels, pipes and pipe fittings sub-sectors; structural steel and any fabrication work in support of steel intensive designated sectors/products);
- Parts and component manufacturers of steel-intensive products;
- Valve and pump manufacturers;
- Machining plants;
- Capital equipment industries particularly steel intensive rail and rolling stock components; and
- Any other steel-intensive business.

The Fund will **exclude** the following upstream steel sub-sectors, as well as sub-sectors where there are already substantial government support / incentive programmes in place:

- Integrated steel mills
- Component manufacturers that qualify for other incentives
- Large multinational OEMs and assemblers and their subsidiaries already benefiting from a government support programme, e.g. APDP.

Part 3

Industrial development and funding

The Industrial Development Corporation last year approved **R15.3 billion** in new investment, the largest sum in its 76-year history and 6% higher than the preceding year.

This included **R4.7 billion in transactions involving 77 black industrialists**, so that we broaden participation in the economy.

A sum of **R2.3 billion was approved for youth-empowered enterprises**, having at least 25% youth ownership, representing 142% increase from the previous year, as part of implementing the Youth Employment Accord.

A sum of **R3.2 billion was approved for women-owned enterprises**, which is an increase of 178% on the previous year, to tap the enterprise of women to help build the economy.

The IDC is driving new investment and commitments to improve the competitiveness of South African companies, with its initiatives in the past financial year **saving and creating 20 877 jobs**.

In addition to these outcomes, during 2016, the IDC partnered with the Beijing Automotive Industrial Corporation (BAIC) to set up a new **R4.3 billion auto-plant in Nelson Mandela Bay** that in the first phase will produce up to 50 000 vehicles for the domestic and African market, with planned employment of 2 500 workers during the construction phase and 800 permanent production workers in the plant.

Part 4

Infrastructure development

The Ministry and Department provided the technical backbone for the work of the PICC during 2016. Some of the highlights of this work include the following:

- Supporting the expansion of new infrastructure projects and funding, which is expected to rise by more than R1 trillion over the next three years, from R865 billion in the past MTEF to the new R947 billion announced by the Minister of Finance during the National Budget in February 2017
- Working with National Treasury to develop a financing instrument for all public infrastructure which will require fiscal support
- Technical work to support the development of a new multi-year budgeting and appropriations framework for infrastructure that would allow for better long-term planning, smoother phasing of construction works in a project, and better value-for-money through infrastructure spending
- Currently investing more than R1.2 billion per day in infrastructure which was used for:

  Education-build completed in the past year includes:
    - 82 new and refurbished schools
    - 3 693 student beds at universities (excluding private sector)
    - 2 new TVET campuses and 2 new universities under construction

  Energy-build completed in the past year includes:
    - 4 562MW completed which includes a further unit of Medupi providing 794MW, by 3 April 2017, resulting in 2 100MW usable energy, enough to supply electricity to a metro, equivalent to twice the size of Joburg which includes Alexandra and Soweto.
    - 585 km of new transmission lines were laid
    - 1 957 solar water heaters were installed by Joburg, bringing the total installed SWH to 504 060
    - 318 898 households connected to the grid. According to StatsSA's 2016-Community Survey more than 15 million households now have access to electricity

  Transport logistics and related rolling stock, completed in the past year includes:
    - 29 360km of roads across the country were maintenance and 332km of new road capacity was added
    - 46km of new bus way lanes was completed in Johannesburg, eThekwini and Cape Town to support the Bus Rapid Transport systems
    - 205 new buses were locally manufactured using 80% local content, bringing the total number of buses manufactured to 612 since 2009
    - 13 330 new taxis were locally manufactured, bringing the total number of manufactured taxis to 57 910 since 2011
    - 100 new wagons were locally manufactured, bringing the total number of manufactured wagons to 16 507 since 2009

- 185 new locomotives were assembled this year bringing the total number of locally assembled locomotives to 770 since 2009
- 303km of rail was refurbished and we are currently completing 68km of new rail between Ermelo and Majuba power station

Human settlements-build completed in the past year includes:

- 89 009 new houses were built bringing the total built since 1994 to 2.6 million

Health-build completed in the past year includes:

- 35 new clinics were built while 13 clinic and 41 hospitals were upgraded and revitalised

Water and sanitation-build completed in the past year includes:

- 15 km of new water pipelines was completed which can deliver 60 million cubic litres of water per annum
- 9 700 toilets were built, contributing towards eradicating the bucket system in formal settlements

Communication-build completed in the past year includes:

- additional "on-air" WiFi spots bringing the total to almost 12 000 across the country
- Increasing smart phone penetration to about 50%
- 24 new MeerKAT antennae were completed bringing the total to 45

- Identifying new sources of funding for infrastructure, including technical work on the approval of the $180 million loan by the BRICS New Development Bank for transmission lines
- Setting up a new Infrastructure Project Management Technical Unit, with funding secured from 1 April 2017
- Address to the Executive Council of NEDLAC on the National Infrastructure Plan and the need for stronger partnership between government, business and labour.