

# [Part One]

B A C K G R O U N D



## [INTRODUCTION]

The Micro-economic Development Strategy (MEDS) for the Western Cape was first initiated in 2004 by the Provincial Government. Consequently, over the subsequent 18 months a large community of researchers were commissioned to investigate a number of sectors in the Western Cape as areas of potential growth and development, complemented by an examination of some key crosscutting themes. In 2005 the MEDS Oversight Committee reflected on the available evidence and analysis, and in July published the First MEDS Synthesis Report. This was not, however, the end of the exercise, for the MEDS was always intended to be an ongoing iterative process – undertaking new research initiatives in order to identify new possibilities to achieve its aims and reassessing and learning from past activities so as to revise previous strategies. In 2006 a further seven sectors were identified as warranting investigation, and the research was commissioned to investigate their development potential. This MEDS 2006 Synthesis Report is hence the most recent step in this continuing process of developing a growth and development path for the Western Cape.

As a living document the 2006 Synthesis Report builds on and updates the previous report. It maintains the same structure and content, but it adds new ideas, new directions and research on new sectors. For those readers approaching the MEDS 2006 Synthesis Report for the first time all the significant content from the previous Report has been incorporated and the 2006 Synthesis Report can be read as a stand-alone document. However, those who have read the previous report are advised to note that some chapters have only been slightly modified with the addition of new information and data, whilst others have entirely new sections added. In addition the MEDS 2006 Synthesis Report contains wholly new chapters.

This Introduction provides a synopsis and framework for the rest of the Report. Chapter 1 on The Western Cape Economy has been updated with minor amendments and additions. Chapter 2 has a new title, Knowledge in Regional Economic Development: The Role of the Province and has substantially new material outlining the importance of knowledge to the Province. Chapter 3 on the Policy Environment has been updated and incorporates new sections on national and provincial policy initiatives. Chapter 4, presenting an Evaluation of the MEDS Research, has been updated to include summary evaluations of the research on seven new sectors commissioned in 2006. Chapter 5 on Prioritisation and Selection includes changes and incorporates the seven new sectors

researched in 2006. We have added a new Chapter 6, New Directions for the MEDS, which discusses four issues that arise from the research and the further deliberations of the MEDS Oversight Committee. Chapter 7 on Monitoring and Evaluation is updated with suggestions for performance indicators, which would allow us to assess the progress of the knowledge economy in the Province. The report concludes with suggestions for further research and proposes A Way Forward.

A significant omission in the MEDS 2005 Synthesis Report, pointed out to the Oversight Committee members on a number of occasions, was an explanation of the rationale and assumptions that underlay the MEDS process. Hence this Introduction sets out an explanation of the Oversight Committee's thinking in this respect. Before moving into the Synthesis Report proper, a short summary of the conclusions of the MEDS 2005 Synthesis Report is also included in the Introduction in order to assist and prepare the reader with the material necessary to proceed further.



### **The rationale underlying the MEDS**

In developing the MEDS the Synthesis Report based itself on the following rationale:

- Increasing growth, facilitating employment, and enhancing equity.
  - Basing strategies on the Province's current and emerging competitive strengths.
  - Identifying knowledge intensity as the Western Cape's fundamental characteristic.
- Requiring all policy proposals to be grounded in an empirical analysis of the structure of the particular industry so as to avoid wish lists.
  - Focusing strategic attention on priority sectors.
  - Maintaining a realistic grasp of the limited capacity of provincial government and hence devising appropriate policy and strategy levers for implementing the MEDS.
  - Building strategic institutional relationships between government and industry.
1. The first goal and task of the MEDS is to attempt to identify sectors where growth can be significantly enhanced through government assistance. But a singular focus on growth does not suffice. The MEDS was cognisant of inherited inequality

that characterises and shapes economic and social life in the Western Cape. Hence it sought to focus policy initiatives on the goal of spreading the gains of economic growth, more especially through employment growth. In addition, the MEDS sought policies that would facilitate the entry of new firms, and especially black and female owned firms. So where possible, the MEDS also prioritised equity considerations and especially employment creation in seeking to identify key sectors and strategies for sectoral development. In order to avoid setting unrealistic goals the MEDS did not attempt to achieve all of these objectives in each of the strategies or each of the sectors identified.

2. The major competitive strength of the Western Cape was identified as resting in its human resources. Of particular importance, is a significant segment of the population exhibiting a high proportion of knowledge intensive skills and activities. This accords with current global trends wherein knowledge is a key foundation for growth in this new era of globalisation. Many of these inhabitants have high disposable incomes and are attracted to living in the Province for lifestyle reasons.
3. A significant and rising share of economic activity in the Western Cape rests on this knowledge base and underlies the comparative advantage of a number of sectors. However, this resource is also very limited and still racially constrained. A major theme that was reported in all of the MEDS research undertaken was emerging skills shortages. These shortages are likely to increase given the forecast of higher growth. Skills shortage is a significant constraint on further growth and policy to address this issue is accordingly of high priority.
4. The MEDS has explicitly tried to avoid the trap of drawing up an all-encompassing wish list designed to satisfy all possible interests and parties. Firstly, sector researchers were required to produce an empirical analysis of the structure of the particular industry and then to ensure that their policy proposals were derived from this analysis. Secondly, based on the sector analysis, researchers had also to prioritise the policies being put forward in order to escape the trap of multiple wish lists.
5. The Synthesis Report itself maintained overall focus and avoidance of all encompassing wish lists through the prioritisation of a few selected growth sectors based on the Province's current comparative advantages and the potential to develop future comparative advantages. In prioritising sectors the Synthesis

Report did not focus simply on the existing strong sectors, but rather those sectors where specific government interventions could have the greatest impact in terms of the goals of growth, job creation, and equity. In other words, the fact that a specific sector was not selected did not mean it was unimportant in the provincial economy but rather whether the strategy devised could achieve the highest return on the expenditure of public monies. For example, the fact that the financial sector is not listed as a priority sector does not mean it is not a very important priority sector in the provincial economy but rather that the levers available to the provincial government to enhance sectoral development are very limited.

6. Many government industrial policies are devised in the abstract based on first principles, and conceptualised as if the capacity issues to implement them were someone else's problem. Rather than adopting this approach, the Synthesis Report started from the principle that in formulating a policy or strategy one has to take into account the existing and likely institutional arrangements available to implement it. There is no point in devising an elegant, academically advanced industrial policy / strategy, which requires an unattainable level of expertise and / or large numbers of civil servants in government to make it operational. Provincial government has a limited budget, a defined civil service salary budget that makes it hard to attract skilled staff particularly from the business sector, and exhibits high staff turnover. Hence in reality it often operates with severe skills shortages and insufficient capacity. The MEDS therefore tailored its government interventions in line with the capacity of government to implement its proposals.
7. The Synthesis Report was cognisant that without industry buy-in industrial policy / strategy is unlikely to work. Furthermore, the process of implementation is an iterative one, involving an ongoing process of learning as the MEDS unfolds. Rather than assuming a priori answers to all issues, the MEDS has explicitly attempted to avoid producing a comprehensive directory of possible policies, which eager civil servants can thumb through, like the Yellow Pages, to find this or that detailed intervention. The MEDS has avoided creating such unrealistic expectations. Instead the foundation of the MEDS implementation mechanism was creating public-private institutions – either as 'sector forums' or independent 'special purpose vehicles' to bring together government and industry. These institutional arrangements were intended to ensure learning and transfer of knowledge about the needs of the stakeholders in the specific sectors identified for support, maintain continuous buy-in from the key

stakeholders as the process unfolded, allow for flexibility in the identification of key areas of intervention as conditions altered, and finally avoid the funding bottlenecks associated with overly bureaucratic government procedures. Provincial governments are particularly well positioned to manage and address the issues that are of a local nature and that require rapid action. This, in turn, gives investors an assurance that concerns will be addressed effectively and timeously.

#### **A summary outline of the MEDS**

The 2005 MEDS selected the following as priority flagship sectors or areas:

- Call Centres, Business Process Outsourcing
- Tourism
- ICT
- Oil and Gas Services
- SMEs.

Based upon the MEDS 2006 research, we have added the Informal Economy.

These sectors all have very considerable potential for output and employment growth and for the entry of new businesses. The provincial government can be effective in enhancing this potential and an initial suite of policies is proposed for each sector. However mindful of the limited capacities currently within government and the dangers of drawing up policy wish lists, which are not implementable, the MEDS has strongly recommended that policy attention should be focussed and not fragmented, and

that resource commitments should be of a scale where they can have a genuine impact. Hence the number of priority sectors was kept to a manageable minimum, and a limited number of policy initiatives identified for implementation. Cognisant that the active engagement of business in sector forums is critical to the success of these interventions, the MEDS recommended an ongoing dialogue and partnerships, through forums and Special Purpose Vehicles (SPVs), between government and the business sector. A number of these are already well established. Finally, proposals are made with regard to funding and the monitoring and evaluation of programmes and policies so as to mitigate the risks of wasteful expenditures.

For implementing the suite of interventions to bolster the priority flagship sectors the MEDS recommended that dedicated provincial government personnel will occupy priority sector “desks” in order to maintain constant touch with developments. They should also be ensured high-level access for interventions, and hence the ability to get the appropriate response from other government departments. Although non-priority sectors have less potential to grow output, employment and new business entry, the MEDS recommended more limited, individually discrete, policies to assist each of these sectors. In the clothing sector, for example, the MEDS has recommended that PGWC actively support the operations of a benchmarking and efficiency enhancement programme through the entire industry. Typically, however, the non-priority sectors have fewer support programmes and resources and will not have a dedicated “desk”. An important task for government is to keep a watching brief and to be in a position to identify new opportunities and constraints. Thus, the priorities identified are not forever set in stone, but will rather be periodically revisited.