3

Sectoral Growth and Employment Prospects

1. Introduction

Formulating a realistic, forward-looking global, national or regional economic outlook requires robust insight into the key factors that drive economic performance, how these factors are likely to change and how they may be influenced by government action.

An important dimension of any national or regional development path is its sectoral nature. How much economic activity is concentrated in, for example, agriculture and related activities? This has important implications for the nature of employment, and the links to the livelihoods of local communities.

The Western Cape presents a mixed picture in this regard. While overall performance in the Province has been unsatisfactory, it has outperformed South Africa as a whole in recent years in value-added terms – largely due to the contribution of service sectors. But, these sectors have not been creating jobs. This means that workers, and their families and communities have not benefited from higher growth of the Province in recent years.

While tourism is undoubtedly an 'engine' for the Provincial economy, and there are opportunities in areas such as call centres, the Province has important strengths that need to be developed in industry and agriculture with broad-based employment potential. This in turn will stimulate activity in transport, communications, finance and construction.

Building productive capabilities across economic sectors is a key theme of this chapter. This requires upgrading skills across the labour force through the Province's Human Resource Development Strategy (HRDS) and the National Skills Development Framework. It means improving the technological capabilities of firms through the national technology and research and development (R&D) strategies. It calls the Province to draw on its strengths in tertiary institutions and apply knowledge, learning and technical excellence to the practical tasks of upgrading firms' capabilities, innovating and expanding new economic activity.

As mentioned in chapter 2, the Western Cape is open in respect of its marked integration into the international economy. This presents both opportunities and challenges. Trade flows reveal many industries are taking advantage of the possibilities through increased exports. Riding the globalisation wave requires that we preen our competitive advantage in international markets by developing strategic relations in areas such as design, R&D, technology and production operations.

This is the high road that will place Western Cape firms and industries in a stronger position to compete in the global marketplace. But it also means that the Province should move away from focused competition in respect of labour costs. Low-wage economies such as India and China are able to export labour-intensive products, such as low value-added clothing, at low prices, undercutting domestic producers, as their main input cost – wages – is much lower.

More particularly, the Province does not advocate wage reductions to match the input costs of such competitors. Instead, a strategic repositioning a restructuring of the Western Cape economy requires that the Province's firms ensure improved competitiveness in the new global sector.

Lessons from industrialising countries and regions indicate that government plays a crucial role in strategic repositioning by anticipating future developments together with local economic stakeholders, and co-ordinating the actions of local institutions to meet the dynamic needs of the global customer.

Yet economic development roles and responsibilities are not yet clarified in South Africa's evolving intergovernmental system. This chapter rises the debate on *provincial or regional developmental responsibilities,* identifying provincial economic sector opportunities and challenges, and going some way to opening the debate in respect of intergovernmental engagement on economic growth and development.

Offering an initial definition of provincial development responsibilities, the chapter moves on to outline sectoral growth and employment trends, opportunities and challenges for the Western Cape, drawing from research commissioned in respect of the Province's Microeconomic Development Strategy (MEDS) and additional data analysis of cross-sectoral trends in output, value-added contribution, trade and employment.

The following section then draws on a range of recent MEDS research to analyse the performance of key sectors in more detail. Using this analysis enables us to identify the main drivers of provincial economic performance. This provides a foundation for identifying the key policy challenges facing Provincial Government, the response to which is discussed in greater detail in chapter 6.

2. A Provincial Role in Economic Development

Sector development goes straight to the heart of contested terrain in respect of economic development. Yet, what is sector or economic development facilitation and why is it contested at all, given the immensity of the broader social and economic development challenges that face South Africa?

Interestingly, looking to the international stage, economic development facilitation finds itself at the centre of intergovernmental debate in developing and developed countries across the world. What is the interplay between national, provincial (regional) and local government in this respect? Does each sphere have a unique, distinctive role? Do the different spheres engage, co-ordinate their actions and lever synergies in a single drive towards shared growth and development?

A broader perspective of economic development challenges the very interaction, cohesion and performance within any co-operative intergovernmental system. Most importantly, delivery depends on the whole rather than on the sum of the parts.

Closer to home, South Africa's first decade of democracy has seen the intergovernmental landscape slowly changing, maturing noticeably along the way. Introducing a unitary state with a decentralised flavour – nine provinces and 284 local municipalities – the first 10 years saw significant political consolidation. More specifically, overarching macroeconomic imbalances and concerns led national government to centralise economic development responsibilities, focusing singularly on macroeconomic reform, in particular prioritising the strengthening of fiscal discipline and market liberalisation.

For the most part, Provincial and Local Government were new or revamped entities that faced enormous challenges, first and foremost of which included structural and administrative redesign to respond to the social and basic service needs of democratic South Africa.

Economic development was therefore not yet within their viewfinder. At the time, their vision, capacities and energies focused most appropriately on social and basic service delivery.

Ten years on, South Africa's democratic governance gains are many and well documented. Looking ahead, the time is right now to advance debate on co-operative response to economic development challenges so that we may maximise future development gains in a shared and equitable way.

In a snapshot, macroeconomic stability has been achieved, and social and basic service delivery is on its way to a measure of cohesiveness. But at the intergovernmental level economic development is not quite streamlined or seamless, given limited debate and engagement on roles and responsibilities.

After 2000 it was clear that macroeconomic reform alone was not sufficient to mobilise higher levels of investment and spur economic growth and development in line with national policy objectives. In his 2002 State of the Nation Address, President Thabo Mbeki proposed a new direction to economic policy – an integrated action plan that, using macroeconomic stability as its foundation and springboard, was directed towards overcoming microeconomic constraints to growth.

Broadly, the Microeconomic Reform Strategy aims to enhance economic growth and job creation, reduce income inequality and promote a more even spread of economic activity. Its focus is three-fold:

- Targeting growth sectors in collaboration with other key players, including parastatals, provincial and local governments;
- Addressing cross-cutting areas of concern, including technology development and transfer, infrastructure development, improved access to finance and human resource development; and
- Improving the performance of key input sectors – transport, telecommunication and energy – which are key drivers in themselves of accelerated development.

Initially, national government identified five key growth sectors – exports, tourism, agriculture, ICT and cultural industries – on the basis of their potential for increased output, exports and employment.

These sectors were detailed further in the national Department of Trade and Industry's (**the dti**'s) Integrated Manufacturing Strategy (IMS) released in 2002. The latter identified eight priority sectors for targeted facilitation and support – automotive & transport, clothing & textiles, agro-processing, metals & minerals, tourism, crafts, chemicals & biotechnology, and knowledge-intensive services. Since then three industries – aerospace, call centres and back-office operations – have been added.

The IMS is a broad, overarching industrial and sector policy strategy. It draws attention to the dwindling of South Africa's natural competitiveness in respect of cheap raw materials and energy. It highlights that protected markets are of the past. It focuses on building value-chains of related activities that cross sector boundaries. It stresses the importance of knowledge-intensive activities in enhancing a competitive edge in a rapidly globalising marketplace. It does not yet go as far as providing a detailed map for each sector, although a few sectors, notably auto and auto components, are significantly advanced in this regard.

While there is considerable movement at a national level in developing these sector strategies and developing sector-specific incentives, there is little discussion on roles and responsibilities of collaborative players, in particular, provincial and local government (DEDAT, 2005: 28-32).

National strategies are exactly that – national, overarching development frameworks. Positioned at a higher, more aggregated level, their implementation on the ground needs to take into account regional differences, local implementation capacities, and provincial and local economic development strategies. The latter are necessary for effective implementation, but they too are not sufficient on their own.

Equally, provincial and local strategies should be developed under the broad rubric of national frameworks, ensuring cohesiveness, direction and co-ordination. This means that provinces need to ensure that national sector policies are appropriately adapted, generally known to local players, and effectively implemented at the local level.

An effective economic development strategy therefore demands government actions along a continuum within the co-operative intergovernmental system.

So a first play at economic development positioning places National Government at the macroeconomic level, providing overarching economic development guidance, incentives and support that defines broad parameters for cohesive engagement.

On the ground, Local Government is the 'mover', the 'shaker', and the 'implementer'. Economic development happens at the local level, engaging people in economic activity in a real sense. Local Government therefore has a key role in economic development implementation.

National and local are drawn together through the actions of a 'weaver' that, at a *meso-economic level*, focuses on *connectivity and integration* and less on provision or implementation. Provinces occupy this dynamic meso-space, linking macro frameworks, institutions and interventions to local economic development.

A key element that is under-emphasised is the role of provinces in collecting *local knowledge* and in *representing* local needs.

A unique and stimulating responsibility, it spans activities that draw dissonant or fragmented pieces and/or players together. It catalyses, energises and synergises. It enhances and leverages. It lobbies key players at all levels. Most importantly, it facilitates economic development at the regional level, taking account of regional dimensions, peculiarities and preferences, and enhancing provincial economic growth and development over the medium to long term. Where necessary, provinces should design appropriate provincial interventions that stimulate broad-based economic activity and raise levels of economic participation.

Focusing at the industry and sector level, this is the realm of the Western Cape's MEDS, the overall goal of which is to guide the Province's actions to enhance, guide and support private sector activity in the Western Cape. This requires that the Province identify and respond to global and nation economy-wide as well as sector and industry-specific opportunities and challenges.

Many shifts in the sector make-up of the Provincial economy happened in response to global events or movements over which neither National nor Provincial Government has any leverage. Economic change, however, does not benefit all in equal proportions. There are winners and there are losers. The key challenge of the Province's MEDS is therefore to encourage, guide and support priority sectors to facilitate a better fit between what the Provincial economy has to offer and what global and domestic markets demand.

In the main, support should be targeted at industries or sectors that are likely to benefit from future global economic movements. This means identifying key growth sectors in the Province on the basis of employment as well as growth considerations. More detailed sector analysis allows the Province to identify useful 'meso-level' interventions in growth sectors that take account of global trends, technology transfer, and changes in exports and imports. The aim is to enhance the level of private sector activity and job creation in the Province, thereby stimulating shared growth and development over the medium to long term (DEDAT, 2005: 2).

3. A Broad Overview of Sector Development

Chapter 2 provides a succinct and robust review of the Western Cape's sector economic performance in its backdrop to the Province's economic outlook for 2005/06 to 2007/08, the detail of which is not repeated here.

This chapter takes a different tack, using sector trends analysis over the eight-year period 1995 to 2003 to develop strategic insight into sector trends and movements. Chapter 2 uses data in respect of a snapshot picture of the Provincial economy in 2003 and analyses trends in respect of the five-year period 1999 to 2003. The longer-term trends give a better picture of inter-sectoral shifts and industry restructuring.

Taking a broad sector sweep, the most important characteristic of the Western Cape economy is its broad base and diversity of base sectors as well as up-and-coming or promising sub-sectors, industries or 'niches'. The Province's four core sectors – agriculture, manufacturing, trade and financial & business services – are each well diversified, reducing the risk of over-dependence on any single industry or sub-sector.

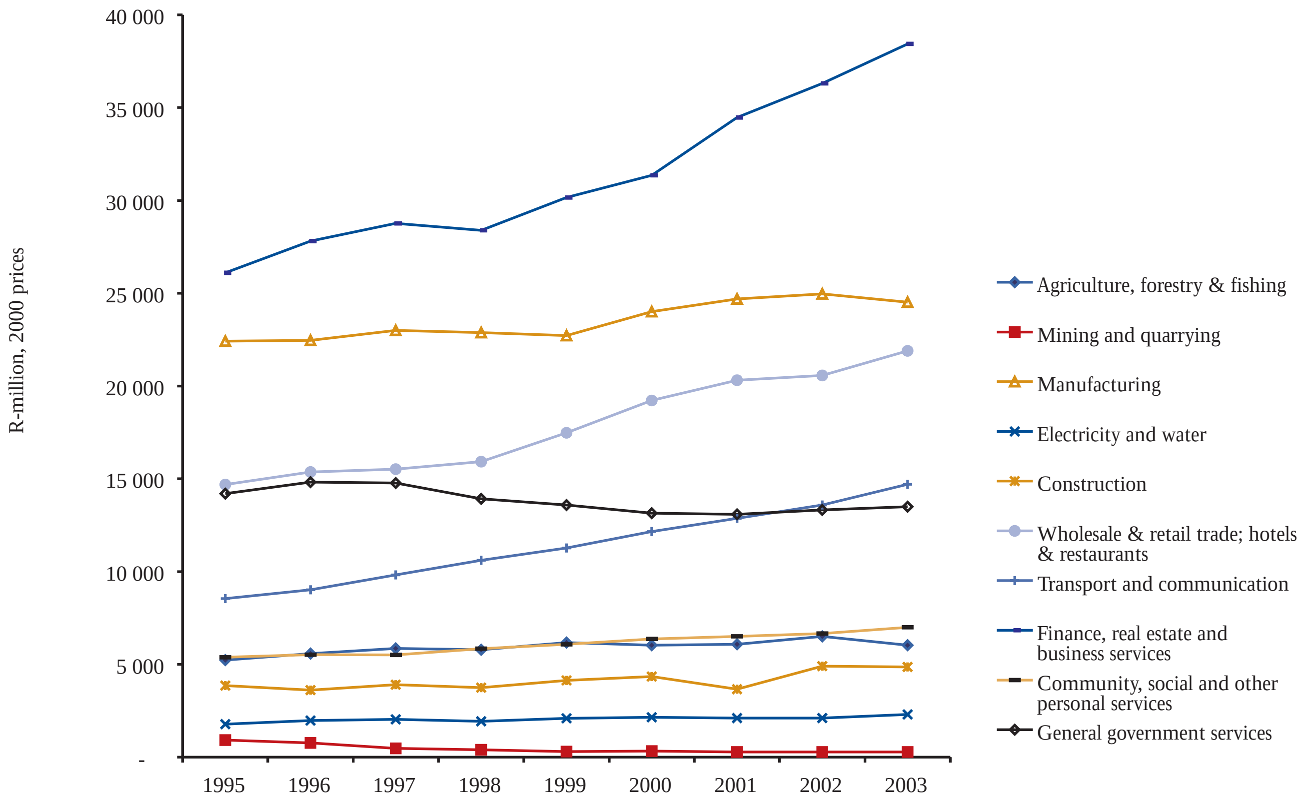
In addition, the region has a well-developed tourism sector, and reasonably strong and dynamic construction, fishing, professional services, higher education and transport sectors. A small mining base is mitigated by Saldanha's emergence as a major export harbour for minerals as well as a key base for the iron and steel industry.

Apart from Saldanha and Namakwa Sands, there is limited mining activity and capital-intensive mineral processing, as well as attendant heavy industry. This accentuates the dominance of small and medium-sized enterprises in the Western Cape economy, and is likely also to contribute towards the shift to a service economy (DEDAT, 2005).

This means that Western Cape sector patterns are quite different from those at national level, although overall output and employment trends over time have been similar. Between 1995 and 2003, the strongest average annual output growth rates in the Province have been recorded in transport & communications (7,0%), wholesale & retail trade and hotels (5,2%), and financial & business services (5,0%). These are detailed graphically in Figure 1.

In the first two of these sectors, Provincial performance has outstripped national performance. This suggests the increased importance of *tertiary services*, as might be expected from a relatively developed economy. However, the employment performance is much poorer, and the disaggregated picture shows very different patterns across different sub-sectors of services.

Figure 1 Western Cape sector contribution to GDPR, 1995 – 2003



[Source: Quantec Research]

In the *secondary sector*, the performance of *manufacturing* has been very disappointing, with an average growth of just half the national performance of 2,2 per cent per annum since 1995.

Trade liberalisation and increased integration into the international economy would be expected to favour coastal locations such as the Western Cape. But the potential gains from these developments do not appear to have been realised in the Province. This suggests that a careful evaluation is needed of constraints to firms' performance and competitiveness.

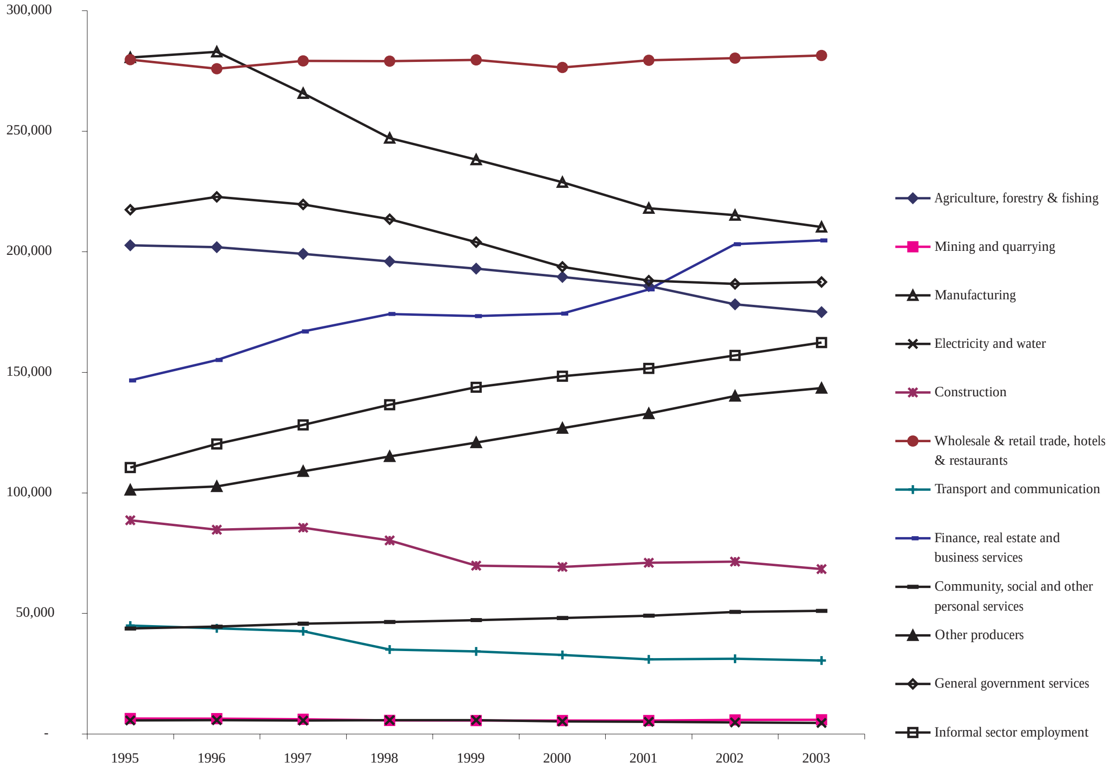
Similarly, in the *primary sector* the performance of *agriculture, forestry & fishing* in the Western Cape, with an average annual growth rate of 1,9 per cent since 1995, is also much poorer than the national growth rate of 3,5 per cent. Closer evaluation of sub-sectors reveals that the data do not reflect recent developments in the Province and that a generally low average performance hides significant growth and development in a number of areas.

More specifically, there has been increased activity across a diverse range of agricultural activity, as well as increased output and employment in fishing and mariculture.

As noted in chapter 2, the picture in terms of *employment* is much more worrying. The most dramatic development has been the decline in manufacturing employment from 1996 (-3,5% average annual growth between 1995 to 2003), while employment has increased rapidly in financial & business services (4,3%), the informal sector (4,9%) and 'other producers' (including domestic workers) (4,5%).

Comprising 18 per cent of total Provincial employment, the broad wholesale & retail trade, hotels & restaurants sector is now by far the largest employer, but it is surprising that this sector has not registered significant net employment creation (only 0,1% per annum over the period) given the output growth of this sector (5,2%). The decline in employment in transport & communication (-4,6%) is also quite out of line with the output performance. An increase in atypical forms of employment and the contracting out of service provision are possible factors here.

Figure 2 Western Cape sector employment, 1995 – 2003



[Source: Quantec Research]

The Western Cape differs markedly from the national picture in employment. Nationally, informal employment has been the largest grouping throughout the period, with a share of 27,9 per cent in 2003 compared to a share of just 11,1 per cent in the Western Cape.

While manufacturing employment has declined in South Africa as a whole (at -1,6% per annum on average), it is at a much lower rate than the decline in the Province (of -3,5% per annum). These comparisons show a shift in emphasis to the areas of services in which the Western Cape has led the country, and away from manufacturing. As will be explored in more detail below, different sub-sectors of manufacturing perform quite differently, and generalisations can be misleading.

Of perhaps even greater concern is that there is little indication of increased *employment* resulting from tourism and transport & telecommunications, either in the Province or nationally. Financial & business services have recorded strong employment growth at both the Provincial (4,3%) and national level (5,6%, due mainly to business services).

Data problems, and needs

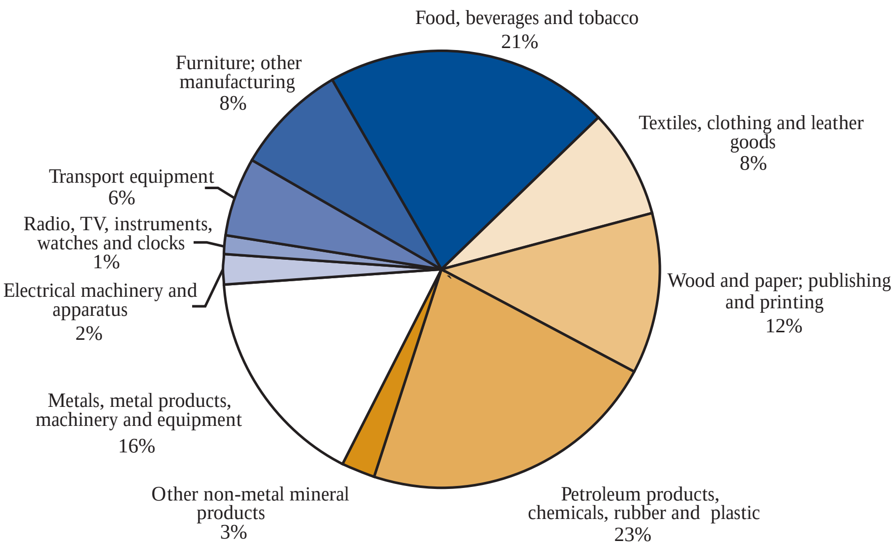
Critical to economic policy and implementation is the ability to collect information and undertake analysis. Such analysis enables Government to understand the Provincial economy and to anticipate economic outcomes under different scenarios and policy choices. This relies on economic data at a provincial level. Unfortunately, the available data is not always reliable when examined at the provincial level, due to considerations such as the size of the samples used and changes occuring in the economy, for example, the increasing importance of ICT which is not picked up, as well as the more traditional industries.

This increases the importance of local research and information gathering to ensure that Provincial Government has a well-founded basis from which to make decisions. It also increases the importance of being responsive to stakeholders, in particular, those who do not have the loudest voices.

3.1. Manufacturing

Focusing on the performance of manufacturing in the Western Cape reveals that, in comparison with the national economy, industry in the Province is oriented towards food & beverages (a 21% share), clothing & textiles (8%), and wood, paper & publishing (12%), which together account for 41 per cent of output (measured as value-added). By comparison, metals & machinery and transport equipment are much less important in the Province (16%) than they are nationally (21%) (*see Figure 3*).

Figure 3a Shares of sectors in manufacturing value-added, 2003: Western Cape



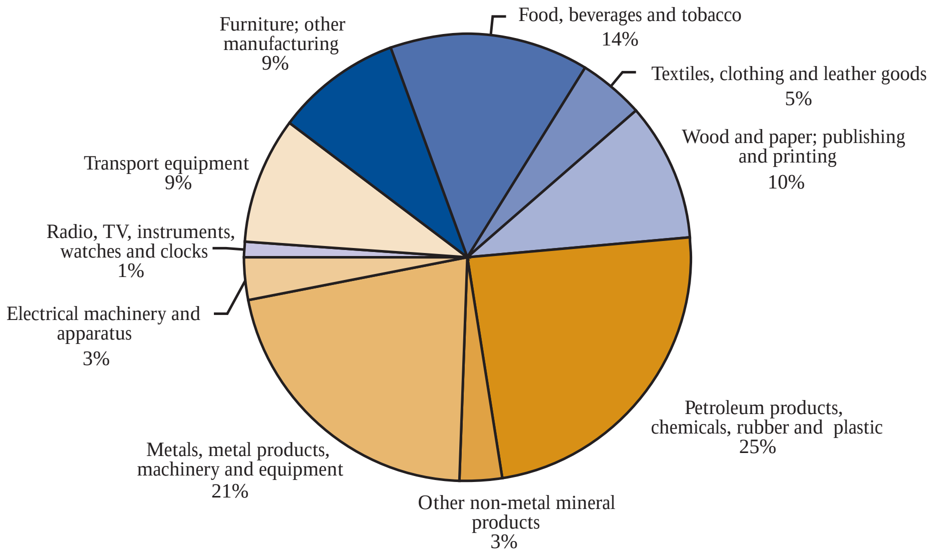
Source: Quantec Research]

However, the sectors in which the Province is relatively under-represented have been performing better. Figure 4 shows that over the eight-year period 1995 to 2003, relatively strong average annual growth of output was recorded for transport equipment (7,4%); petroleum, chemicals & plastics (4,3%); electrical machinery (3,7%); and metals & machinery (3,3%). And in transport equipment and electrical machinery ,the Province has far out-performed the national economy, which recorded output growth of 3,2 per cent for transport equipment and 2,4 per cent for electrical machinery.

But food & beverages (at -0,4% per annum); non-metallic minerals (-5,9%); radio & TV (-4,6%); clothing & textiles (0,2%); and wood, paper & publishing (-1,4%) have either stagnated or recorded contractions in output, and have generally performed more poorly than the national economy over the period.

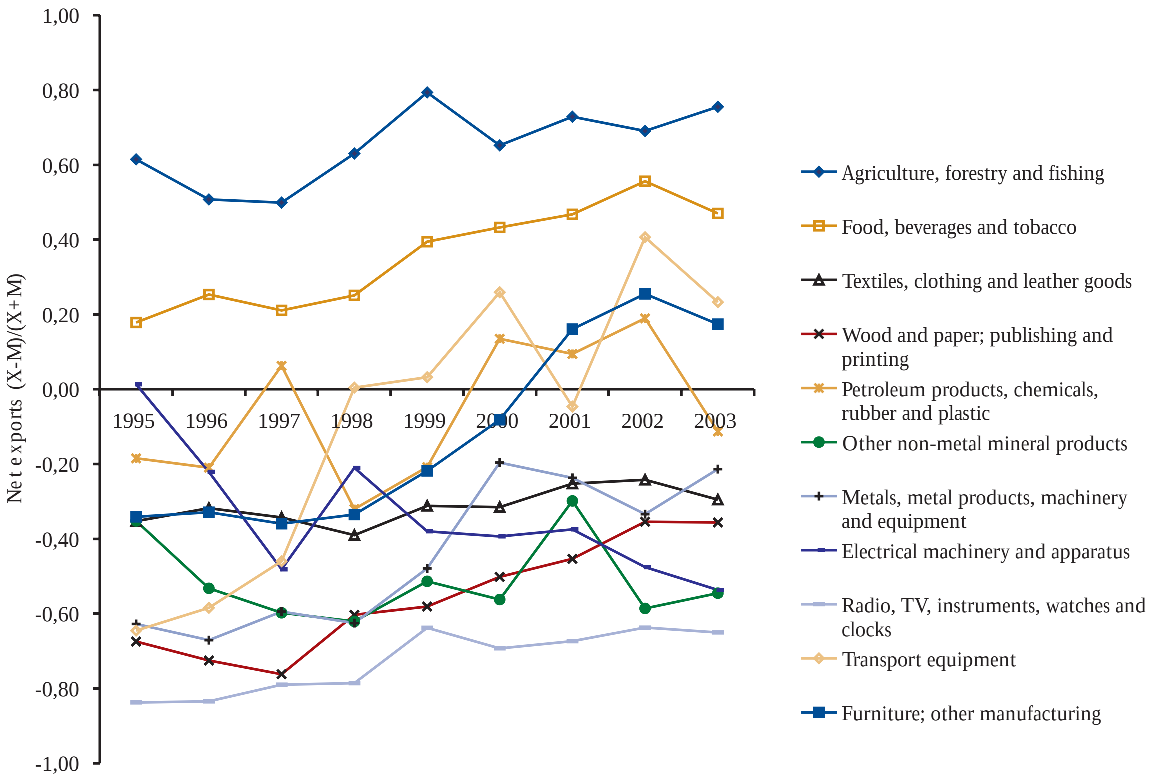
Figure 5 shows that all manufacturing sectors in the Province had lower employment in 2003 than in 1995, except for transport equipment (3,2% average annual growth) (which has grown from a very small base, and furniture & other manufacturing (1,1%). The biggest proportionate declines were in electrical machinery (-11,9% per annum) and other non-metallic minerals (which includes cement and brick-making) (-10,3%). The biggest absolute job losses were in the largest sector of clothing, textiles & leather (23 737 net jobs), closely followed by food, beverages & tobacco (18 321 net jobs).

Figure 3b Shares of sectors in manufacturing value-added, 2003: South Africa



[Source: Quantech Research]

Figure 4 Western Cape manufacturing value-added, 1995 – 2003



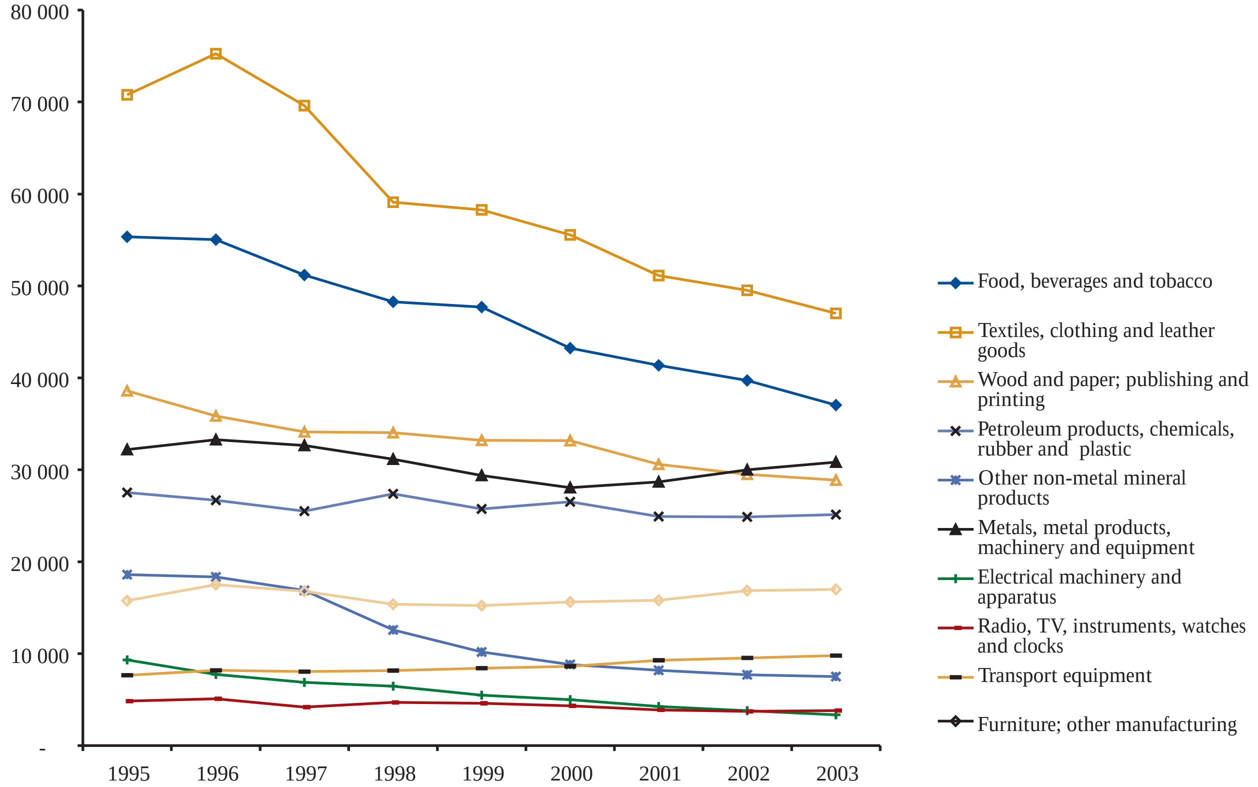
[Source: Quantec Research]

In the last three years, the metals and machinery sector has shown signs of growth (3,2% growth per annum from 2000). This sector is linked to important areas of potential. Similarly, positive growth in employment in transport equipment in the Province reflects capabilities in auto components and in yacht- & ship-building.

Of more concern is that the Province's performance is generally much poorer than that of the country as a whole. In addition, while nationally the wood, paper & publishing and the petroleum & chemicals sectors have recorded employment growth from 2001 to 2003 of 0,7 per cent and 1,5 per cent per annum respectively, employment in the Province overall has continued to stagnate.

Growth at national level in these broad groupings relates to the narrower sub-groupings of wood products (due mainly to increased processing of forestry products) and plastic products. Plastic product manufacture is both labour intensive and experiencing higher than average employment growth (of 2,1% per annum) at the national level, as plastic products increasingly replace other materials. The Western Cape needs to ensure that it benefits from these developments.

Figure 5 Western Cape manufacturing employment, 1995 – 2003

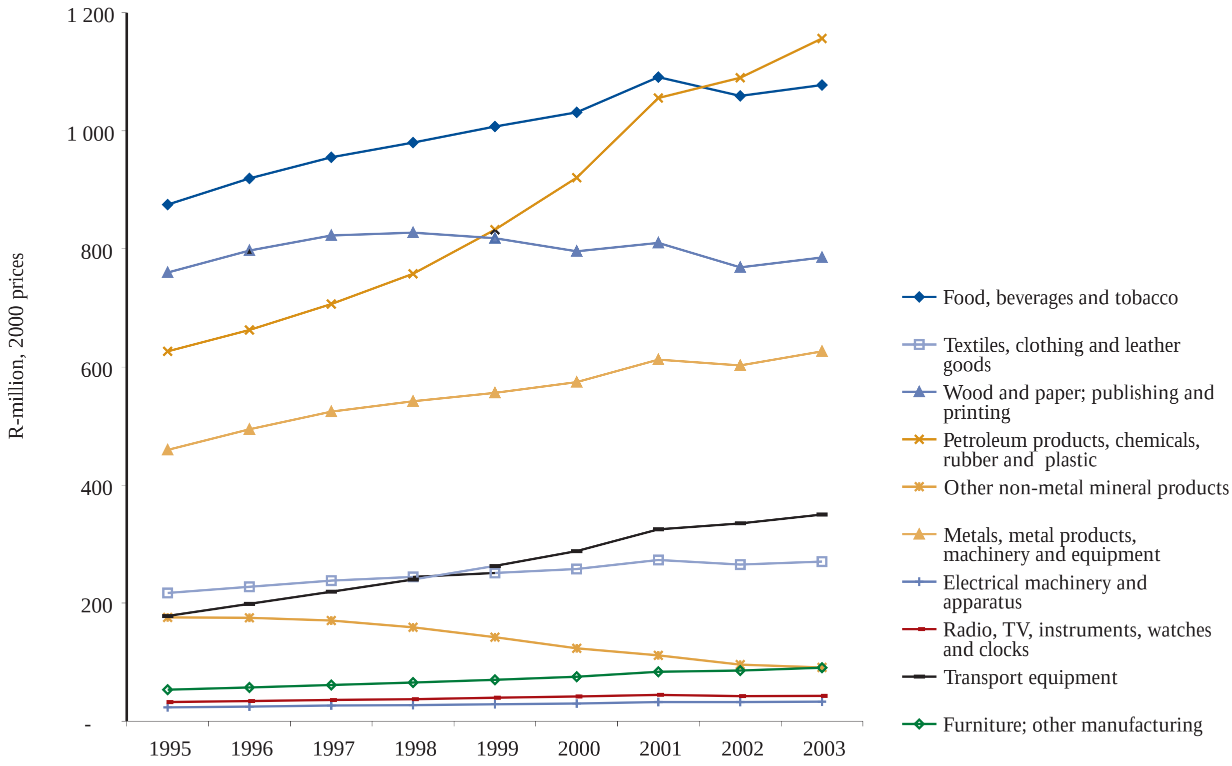


[Source: Quantec Research]

Figure 6 indicates that while manufacturing firms have not increased employment, they have increased investment. Particularly strong increases in investment in the Province have occurred in petroleum, chemicals, rubber & plastic products (8,0% per annum), as well as in transport equipment (8,9% per annum).

For firms to be able to compete internationally and to expand and grow employment, it is important that they increase their productive capacity and upgrade equipment. Recent performance suggests that this is especially the case for employment growth in more labour-intensive sectors. But in very capital-intensive sectors, such as basic chemicals and basic iron & steel, increased investment has coincided with large reductions in employment.

Figure 6 Western Cape gross manufacturing domestic fixed investment, 1995 – 2003



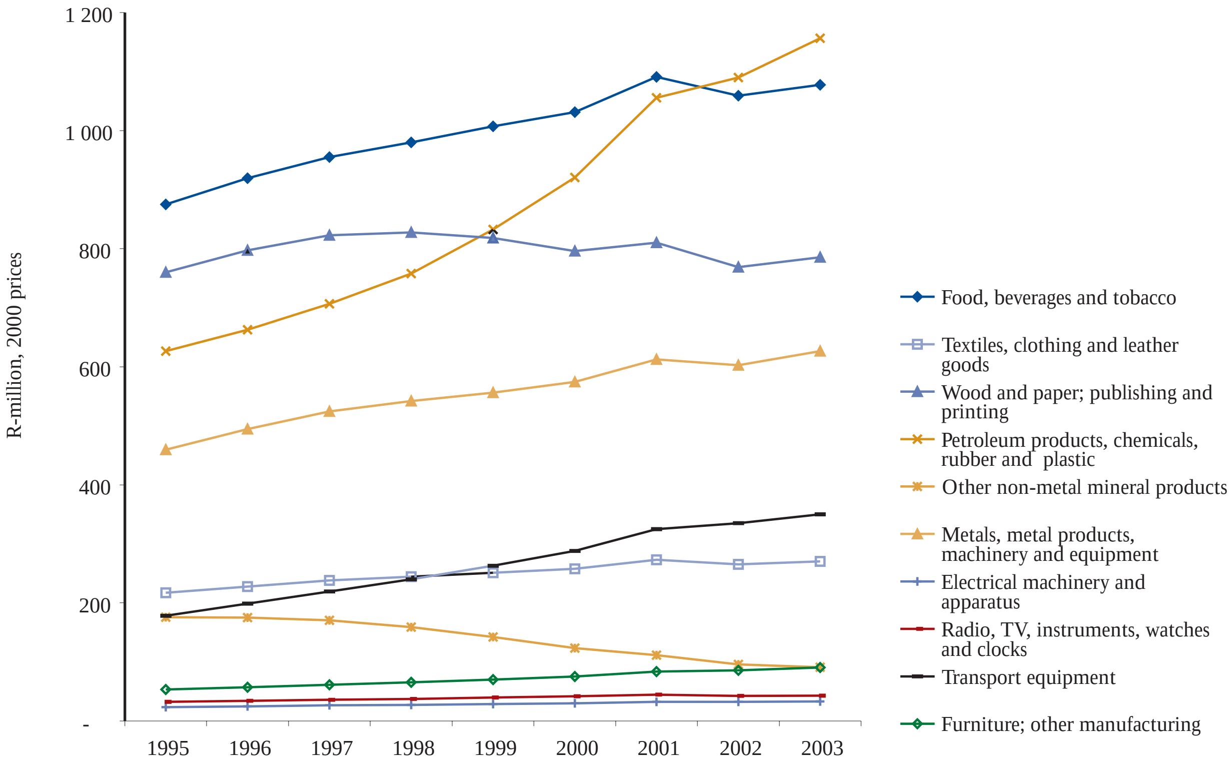
[Source: Quantec Research]

The trade data provides a more accurate indication of changing patterns of competitiveness. Figure 7 shows that Western Cape firms have increased competitiveness strongly in almost all sectors, with the largest growth recorded in petroleum, chemicals, rubber & plastics (24,5% per annum). The exports of this industry are dominated by petroleum products (76,4% of the total), which are mainly exported to other African countries. However, exports of other chemicals, fibres & plastics have all increased too. Strong growth has also been recorded in exports of agriculture, food & beverages (14,6%) and in metals & machinery (14,6%).

A more disaggregated analysis in Table 1 reveals the importance of agricultural products, fishing, and food and beverage products in the Province's exports. These account for four of the top five exports categories in 2003. Iron & steel is in fourth place, due largely to exports of steel from Saldanha, while the Western Cape's strengths in metals and machinery is reflected by the sixth-place export category, as well as exports of electrical machinery (12th), vehicles & parts (17th) and ships & boats (18th).

The strengthening of the rand had a major impact on the value of exports in rand terms in 2003. The total value of exports from the Province declined by 6,3 per cent. But, if one considers the longer-term period of 2001 to 2003, high rates of increase are recorded

Figure 7 Western Cape Sector Exports, 1995 – 2003



[Source: Quantec Research]

across most categories. Reduced trade barriers in the domestic market and the impact of trade agreements such as the EU-South Africa Trade and Development Agreement (EU-SA TDA) and the AGOA are key contributing factors to the Province's export success.

Of further interest is that the top four exports – fruit, wine, fish and iron & steel – make up 54 per cent of exports. All are based on 'local' raw materials that are subject to fluctuations in global markets and in supply, as a result of weather or other natural factors. Further detailed time series analysis is threrfore required to see whether the Western Cape is export performance is subject to a high degree of volatility in comparison to national trends.

Table 1 Top 20 Western Cape exports and growth (HS2), 2001 – 2003

Products	Value, 2003 (R-million)	% of Total Exports	% Increase 2002 – 2003	% Increase 2001 – 2003
1. Fruit	5 168,0	19,4	17,6	75,0
2. Wine, beer & spirits	3 333,0	12,5	4,6	58,0
3. Fish, crustaceans & molluscs	2 311,9	8,7	-4,4	28,5
4. Iron & Steel	1 777,8	6,7	-13,3	50,5
5. Processed food	1 684,0	6,3	-16,8	-2,4
6. Machinery, boilers & appliances	1 090,3	4,1	38,7	79,4
7. Precious & semi-precious stones	943,8	3,6	-19,3	74,5
8. Ores, slag, ash	857,7	3,2	-22,0	19,1
9. Clothing	768,2	2,9	1,65	50,8
10. Man-made filaments	614,3	2,3	-12,4	8,2
11. Plastic products	576,2	2,2	-15,6	14,6
12. Elec & telecom. Mach & equipmt	564,3	2,1	-5,1	40,8
13. Railway equipment & stock	559,4	2,1	-5,0	12,9
14. Wood and wood products	429,7	1,6	4,7	75,5
15. Raw hides, skins & leather	371,3	1,4	-42,0	-15,7
16. Furniture, lamps, soft furnishings	356,6	1,3	-24,5	21,5
17. Vehicles, parts & accessories	346,7	1,3	-8,5	23,1
18. Ships & boats	268,9	1,0	-52,8	23,9
19. Other chemical products	262,0	1,0	-36,5	136,5
20. Meat	227,7	0,9	-26,5	-12,5
Total Top 20 Exports	**22 512,8**	**84,5**	**-3,5**	**43,6**
Other Exports	**4 126,1**	**15,5**	**-19,0**	**18,9**
Total Exports	**26 638,9**	**100,0**	**-6,3**	**39,1**

[Source: Customs and Excise]

Note: Excludes mineral oils and arms

African Growth and Opportunity Act

AGOA is an arrangement between the US and Sub-Saharan African (SSA) countries that was entered into in 2000 and will be in operation until September 2008. AGOA liberalises access to the US for 37 SSA countries.

AGOA builds on existing US trade programmes by expanding the (duty-free) benefits previously available only under the Generalised System of Preferences (GSP) programme. Duty-free access to the US market under the combined AGOA/GSP programme now stands at approximately 7 000 product tariff lines, including the roughly 1 800 product tariff lines that were added to the GSP by the AGOA legislation.

Items such as apparel, footwear, wine, motor vehicle components, a variety of agricultural products, chemicals, steel etc. can be exported to the US duty free. (www.tralac.org)

European Union-South Africa Trade and Development Agreement

The EU-SA trade agreement has been in operation since 2000. South Africa is supposed to open its market to 86 per cent of EU goods over a 12-year period, while EU will open 15 of its economies to 95 per cent of South African goods over a 10-year period.

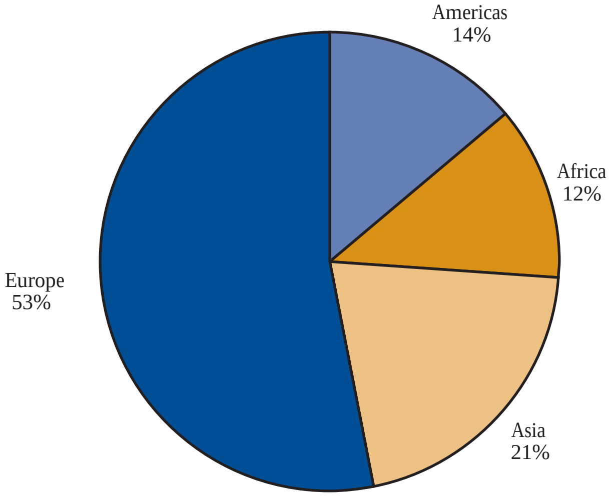
The EU has always been a market destination for South Africa and this agreement will help domestic exporters to supply more to this market if they can compete with EU firms. The EU pledged to drop average duties on South African goods from 2,7 per cent to 1,5 per cent while South Africa agreed to cut average duties on EU goods from 10 percent to 4,3 percent (UN Department of Public Information 1999: 1)

The EU-SA agreement is notable because it includes agriculture in a bilateral free trade. South Africa is granted a sizeable zero-tariff quota, which allows the country to export volumes of goods in agriculture duty free. South Africa, in contrast, is obliged to scrap tariffs on 95 per cent of agricultural imports from the EU over a 10-year period.

Complementary analysis in respect of export products focuses on trade partners, in particularly export destinations.

Figure 8 shows that Europe is that the main destination for Western Cape exports, with 54 per cent of the total in 2003. This is followed by Asia (21%) and the Americas (14%).

Figure 8 Western Cape exports by region, 2003

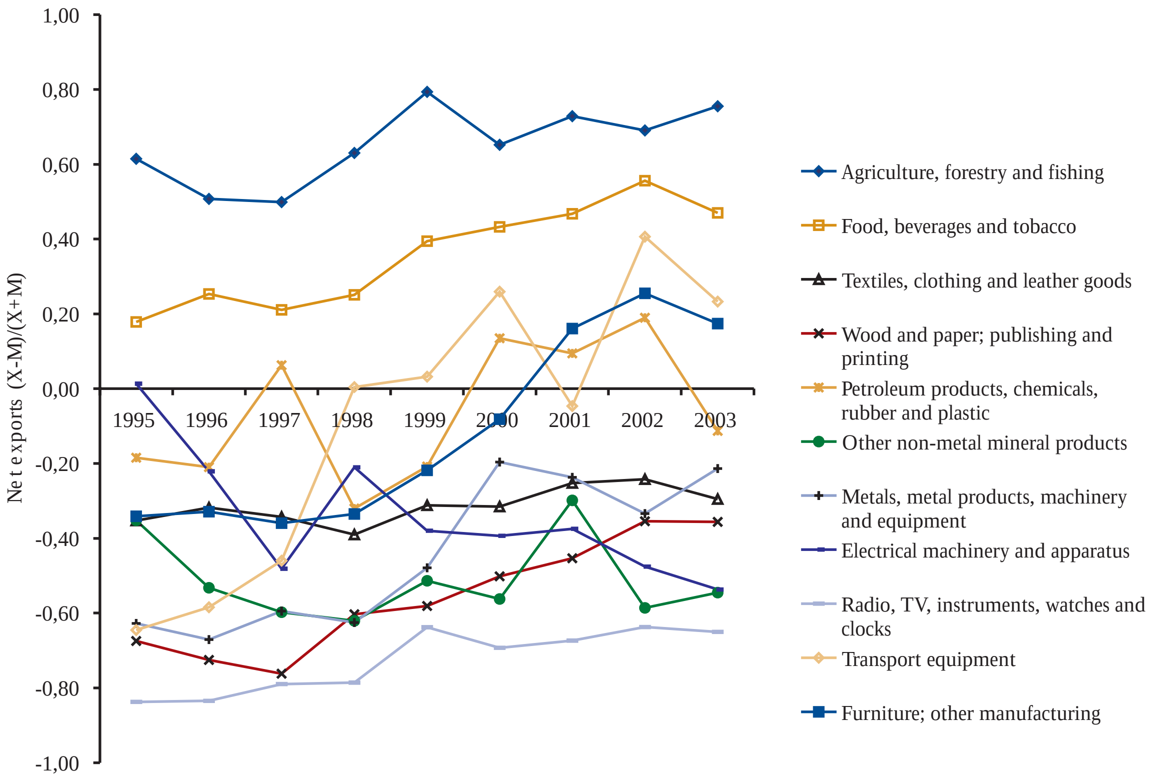


[Source: Customs and Excise]

The *net trade ratio* expresses the trade balance of exports relative to imports as a ratio of total trade flows. This indicates that competitiveness has improved greatly across industries. A positive value indicates a trade surplus, while a negative value reflects a trade deficit. A positive change over time reflects improved trade performance, either because the ratio becoming less negative means the trade deficit has narrowed, or because the ratio has an increasing positive value, reflecting an increased surplus.

Figure 9 illustrates the growing trade surplus in agriculture & fishing, food & beverages, transport equipment, and furniture & other manufacturing. Moreover, the trade deficits in most other industries have been declining over the past eight years, with the notable exception of electrical machinery. Of concern is the poorer performance in many groupings in 2003, reflecting the effects of the stronger currency.

Figure 9 Net export ratio, Western Cape, 1995 – 2003



[Source: Quantec Research]

Note: Excludes mining, electricity & gas and unspecified

The improved trade performance over the longer term strongly suggests that, while a process of restructuring has taken place, Western Cape industries have gained from increased exports in particular. The coastal nature of the Province has enabled it to take advantage of opportunities offered by greater international integrationto a certain degree. The latter offers significant potential for further expansion.

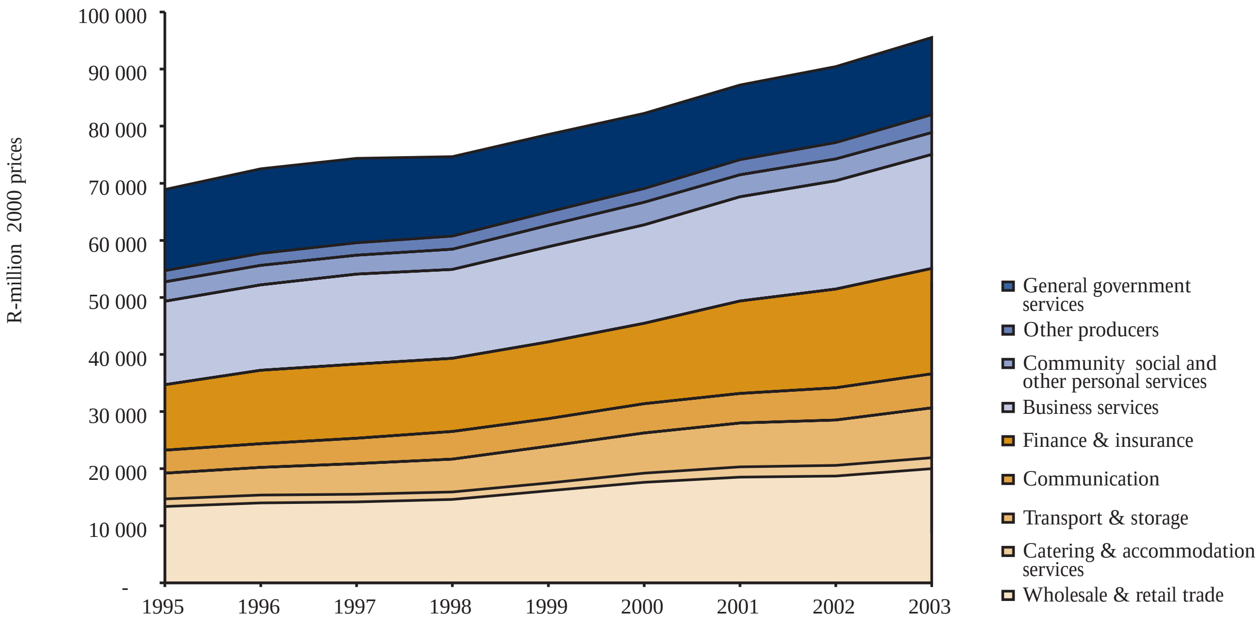
3.2. Services

Services together account for over more than two-thirds of Provincial GDP, higher than the national average. Financial & insurance and business services, in particular, stand out, with a share of 13,8 per cent and 15,0 per cent of GDPR respectively in 2003, compared to 9,7 per cent and 10,6 per cent of national GDP.

There has been strong growth across services, led by transport (8,6%), finance & insurance (6,2%) and wholesale & retail trade (5,2%), which all recorded average annual growth rates from 1995 to 2003 in excess of five per cent per annum (*see Figure 10*). This is similar to national patterns of growth.

The Province has recorded higher growth than the national average in catering & accommodation (4,9%), transport & storage (8,6%), business services (4,0%) and other producers (5,9%). This reflects strengths in tourism and call centres, as well as having the advantage of a major port.

Figure 10 Value-added in services, Western Cape, 1995 – 2003

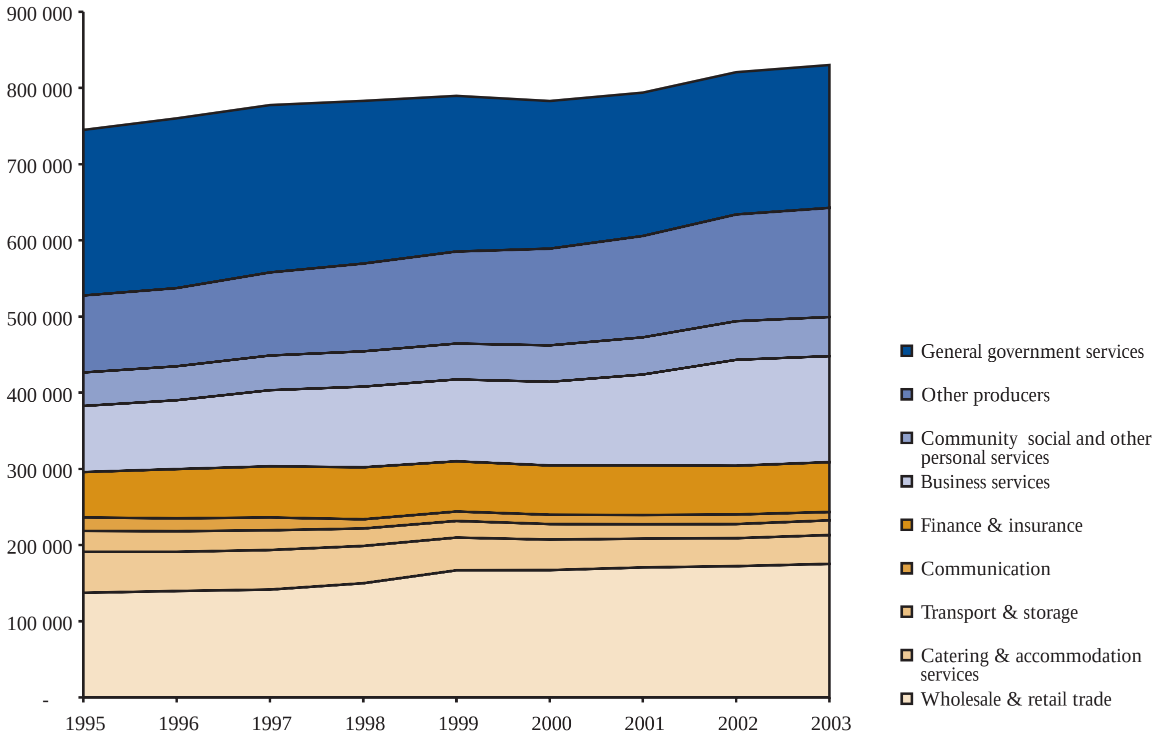


[Source: Quantec Research]

A major concern is that the strong growth in services value-added is not reflected in employment patterns. Indeed, as seen in Figure 11, contractions in employment have occured in many service sectors. The largest contractions have been in communications (-4,8% per annum), transport (-4,3%) and catering & accommodation services (-4,2%).

It is surprising not to see the substantial growth in tourism reflected in employment in catering & accommodation and transport. The communications sector shed almost 5 000 jobs between 1997 and 1998, probably reflecting major retrenchments by Telkom following its commercialisation and move to privatisation. Almost 4 000 jobs were also shed in transport between 1996 and 1998, reflecting retrenchments by Transnet across their operations as part of broad restructuring of the corporation.

Figure 11 Formal employment in services, Western Cape, 1995 – 2003



[Source: Quantec Research]

By comparison there have been high rates of employment growth in business services (average annual growth of 6,2%), wholesale & retail trade (3,2% growth) and other producers (4,5% growth). Business services reflect employment creation in call centres, while other producers may capture some of the effects of tourism. However, it is quite surprising that the Western Cape has not recorded as rapid increases in employment in business services as in the country as a whole.

The fluctuations in employment in the financial & insurance sector, alongside rapid growth in value-added, reflect the increased use of information technology, which entails increased capital intensity. The Province has also seen the expansion of international banks such as Citibank and Barclays, as well as niche financial services aimed at the wealthy, which are not significant generators of employment. In contrast, the roll out of retail banking services to low- and middle-income consumers do create significant employment opportunities.

4 Demands of Provincial/Regional Economic Development

Despite international trends towards liberalisation and increased international flows of goods and capital, industrial activity remains highly concentrated in local regions or districts. The main reasons for this are:

- The importance of local *agglomeration effects* in skills, specialist services and inputs, and knowledge and information flows, which entail the benefits firms reap from locating where skills, inputs and services are available, and the ongoing development of such services where the demand for them exists.
- *Collective learning* by firms to develop competencies within and across groups of firms.
- The development of common services, effective business associations and industrial policy frameworks all require *effective governance* at the local and regional level. This is one of the key reasons underpinning the growth of successful industrial clusters.

The potential gains from shared learning, a wide skills pool and sharing of appropriate institutions supporting research, training and development are important in explaining why production is increasingly concentrated in specific locations. For example, while firms in the auto industry sell into international production chains, their competitiveness depends on the existence of design capabilities, skilled labour and effective logistics in the local region. The presence of these conditions will attract other auto component firms, which in turn will enhance the pool of services provided, and local skills and knowledge. These factors mean that there is a strong path-dependency driving agglomeration effects (*see, for example, Helmsing, 2001 and Dunning, 2000*).

Locations and countries that were first-movers derive an initial advantage, which is compounded over time. For late-industrialisers the clear implication is that co-ordinated and purposive action is very important in the development of more sophisticated industrial activities. Analyses of the East Asian experience of industrialisation have highlighted the importance of co-ordination across R&D, investment, training and product-development activities within selected sectors.

Technological capabilities are a central element of firms' overall capabilities. Indeed, a major body of literature argues that how enterprises manage the process of mastering, adapting and improving upon existing technologies – better known as 'innovation' – is the single most important determinant of industrial development. This in turn is an outcome of firms' decisions and wider strategic orientation. It reflects deliberate actions and the evolution of firms in the context of their environment and incentives.

R&D activities and firms' development of production capabilities more broadly are areas in which collective action by government and firms has an important role. Such action can establish institutions that provide services and training, so enabling positive externality effects (or 'spill-overs') on which to build. For example, there may be common elements in the development of a process technology by two firms in different sectors. And investment in training by firms contributes to a pool of skilled labour from which all may draw. This role for the public sector is an important feature of developing production systems and more dynamic business models.

International experience of the development of industrial districts and local industrial clusters demonstrates the importance of the public sector in creating appropriate institutions. These institutions may be developed in conjunction with business associations and represent collective action responses to market failure.

In the celebrated case of Emilia-Romagna in Italy, the regional development agency established a network of general, sector-specific and function-specific centres to provide services to targeted industries. The centres were jointly managed with business associations. Important areas for institutional actions are education and training, and support for research and development. The institutional framework is, however, broader than this. Taken as a whole, it is effectively the means through which information and integration are achieved.

Value-chain frameworks (such as those that underpin **the dti's** *IMS)* highlight the importance of linkages and raise questions of governance by firms at different levels in the chain. Governance also relates to the organisation of inter-firm relations and which firms ultimately drive the value chain. If the role-players driving the value chain are only interested in maximising their returns in the short-term through optional extraction of economic rents, it is unlikely that firms will develop their capabilities and co-operate to improve products. Business and industry associations may be effective groups to address the challenges of upgrading production capabilities, but they may also be ineffective social clubs.

4.1. Industrial and technology policy in South Africa

Historically, industrial and technology policies both focused on the strategic concerns of the *apartheid* government, such as defence and liquid fuels, and the needs of resource extraction and processing industries. By comparison, recent industrial and technology policy frameworks aim to encourage downstream value-addition and employment creation. In 2003, the Department of Science and Technology, through the National Council on Innovation, released its *Advanced Manufacturing Technology Strategy* (AMTS). The *AMTS* and **the dti**'s *IMS* complement each other and emphasise the need to develop production capabilities, the need for firms and public institutions to work together effectively, and that knowledge and technology should be the foundation for growth of output and employment. Many of these areas require action at the local level.

The *IMS* places increased value-addition downstream and the strengthening of vertical and horizontal linkages at its centre. The strategy identifies a range of broad issues to be taken forward through specific policy measures. These issues include the pricing of inputs, and improving skills and technological capabilities.

The *AMTS* also establishes a framework for government action to support industrial development, specifically as it relates to research, technology and productive capacities. This strategy is to be given effect in specific programmes, such as a *National Tooling Initiative* launched by the Council for Science and Industrial Research's (CSIR's) National Product Development Centre. This was initially driven by the auto industry but has now grown to be much broader. The *Advanced Metals Initiative* (AMI) has also grown out of the AMTS, and is aimed specifically at light metals. A key target area is the application of technologies to aerospace.

Much of the actual programmes, such as technical centres or innovation networks, envisaged under the AMTS have concrete locations as part of growth clusters. This is evident in the Automotive Industry Development Centre, which is linked to a supplier park in Rosslyn, Tshwane, and a chair in automotive engineering at the University of Pretoria. In these initiatives champions are needed from the different stakeholders, and particularly from government and business.

5. Key Sector Performance 1995 – 2003

Understanding the performance of different economic activities requires assessment of the factors influencing firms' decisions – from developments in input costs, through employment and investment decisions, to demand patterns and growth of markets. Producers' ability to grow output depends on their competitiveness in existing and new markets. This relates to the positioning of firms in terms of the types of products they supply and their strategies in product development.

The broad sectors are far from homogeneous, which makes it necessary to examine the composition of economic activity and developments at a disaggregated level. From this we can identify the impacts on employment and the key challenges in the reorientation and growth of the economy.

Our review of development in key sectors draws heavily on the base sector research reports completed as part of the first phase of the Province's MEDS. Looking ahead, this enables us to identify major cross-cutting issues in respect of the drivers of Provincial economic performance.

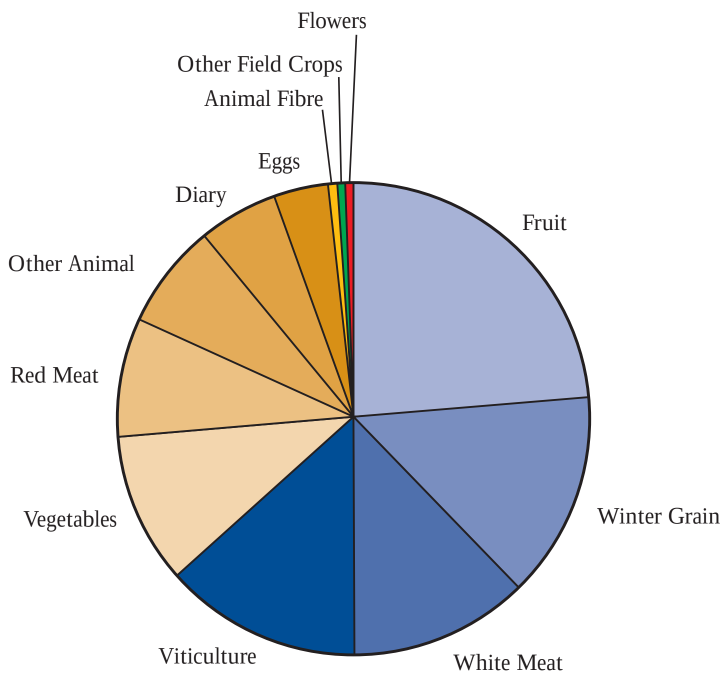
5.1. Agriculture and food & beverages

Agriculture, together with food and beverages production, is one of the main pillars of the Western Cape economy. And, while the share of agriculture in the economy overall is declining from 5,1 per cent of GDPR in 1995 to 4,5 per cent in 2003, the sector continues to grow in absolute size and offers many opportunities for further growth, especially around higher-value exports.

Agriculture is a significant exporter and has been a primary contributor to the export boom of recent years. The two largest categories of exports of the Province are agricultural – fresh, dried and processed fruit (19,4% of total Provincial exports) and wine, beer & spirits (12,5%) – both of which have strong growth potential.

There is also growth potential in a whole range of diverse *fynbos* products, ranging from flowers through *rooibos* and a variety of herbal teas. A distinctive feature of these products is that their production is often associated with poor communities living in distant rural areas.

Figure 12 Agricultural production in the Western Cape, 2002



[Source: Wesgro]

The diversity of agricultural production reflects the mix of conditions in the Province's sub-regions. Figure 12 illustrates that major products include deciduous and citrus fruit (20%), vegetables (12%), viticulture (12%), white meat (14%) and winter grain (15%). As is well known, South Africa is the world's sixth-largest wine producer, due to the Western Cape, and is also a major exporter of canned fruit. There are thus strong linkages from agriculture into processed exports.

Agriculture is an important employer in the Western Cape, providing jobs to 13 to 14 per cent of total Provincial employed as opposed to eight per cent nationally. Production processes are also more labour-intensive than is the case nationally, and worker remuneration is higher (farm workers in the Province earn 24 per cent of all farm wages yet account for only 18 per cent of all farm workers in South Africa). Farmers' incomes are also higher.

Within the total employment picture, key trends are the substitution of labour by technology (in line with global shifts), replacement of permanent labour by seasonal or part-time labour, increased use of contract labour and an increase in the number of women employed as farm workers (DEDAT, 2005:84).

While the strong currency has impacted on the sector, especially on the fruit and wine producers, there have also been indications of improved capabilities. For example, in viticulture (wine), the technology and production systems mean the industry is very competitive. There have also been new entrants to the industry and a number of joint ventures have been established with farm workers. The advancement of black farmers requires Government to play a role in advisory services, and in ensuring effective and appropriate institutions that are open to all.

Continuing to grow agricultural exports requires ongoing development of research and standards, including in food safety and in organic production. It also requires training for farmers. In addition, the development of a mix of agricultural production – for the local market and for export – necessitates that decisions be taken with a view to scarce resources, including water.

The rapid growth of China, in particular, means greatly increased demand for the agricultural products of the Western Cape. This represents the greatest possible gains for South Africa from the proposed Southern African Customs Union (SACU)-China trade agreement.

Biotechnology

The Western Cape has important advantages in the establishment of a biotechnology hub. These include a strong research community and institutions, long-established firms in the fields of agricultural, medical and industrial biotechnology, and an ecosystem (or biome) with the richest plant diversity on earth.

It is estimated that more than a third of South Africa's biotechnology companies are in the Western Cape. However, the transfer of technology from research institutions to commercial applications is slow, with only two start-up companies being created for every 100 patents granted in South Africa, compared to a global norm of 10 to15 start-ups.

A special-purpose vehicle, Cape Biotech, was established in 2003 and is tasked with developing and promoting biotechnology capacity in the Western Cape, including through investing in promising projects and creating capacity and support networks in the industry. Cape Biotech is also responsible for running one of three national Biotechnology Regional Innovation Centres. As a relatively new industry, the initiative represents an investment in the future.

Looking forward, there are a number of constraints that could impact negatively on the sector. First and foremost is resource availability, particularly in respect of water. Here both reduced rainfall patterns arising from climatic change and increased competition for irrigation water from the Province's continued urban growth should be taken into account.

Second, there has been slow progress in land reform and overall transformation in the Province's agricultural sector. Only 0,8 per cent of available agricultural land was transferred in the period between 1997 and 2002. Given national and Provincial targets, it is critical that the pace of transfer accelerates over the medium term. Concern, however, has been raised that most land transferred is used for settlement rather than agricultural purposes. And when land is used for the latter, there is limited capacity to advise and support new farmers effectively.

Finally, there is increased competition in agricultural exports from southern-hemisphere producers, mainly Chile, Brazil, Argentina and New Zealand. Exchange rate competitiveness is key here, but equally important is product quality control, supply-chain logistics and marketing.

Looking beyond these constraints, there is undoubtedly potential for growth of the sector, although the latter requires further strategic repositioning and diversification in response to climatic and global competitive trends (DEDAT, 2005: 85-86).

Rooibos tea

The export-oriented growth of *rooibos* tea is one of the agricultural success stories of the Province. It is cultivated almost exclusively in the Clanwilliam-Cederberg region and now sells more than three-million kilogrammes per year.

Competition initially meant lower margins, but it has also brought more vigorous exploration of new markets and variations on the product and its use. In 2000, more than 4 500 tons of *rooibos* was exported to 31 countries, up on 1 800 tons in 1999. Currently, Germany imports as much *rooibos* as is consumed in the whole of South Africa. Other importers include Switzerland, Israel, US, Holland, the UK and Japan.

Together with similar herbal products such as honey bush tea, there is significant employment opportunities have been created by the *rooibos* industry, particularly in historically poorer rural areas of the Province. Export and marketing also provides employment in packaging and processing. According to Wesgro (2000: 2), in 2000 the rooibos industry in the Western Cape employed 4 000 people and earned an annual income of between R60-million and R70-million a year.

Maximising the potential from natural herbal products, such as essential oils, requires attention to the organisation of production, harvesting, processing and marketing to ensure that both effective market entry and positive effects for communities, including employment, are attained.

In this respect, a number of institutions – the Agricultural Research Council, the Medical Research Council, and the Universities of Stellenbosch and the Free State – assist in *rooibos* research that focuses on production, cultivation and health properties.

Certification is crucial to food products, and includes certification as organic produce. However, the costs of certification are potentially a barrier to small farmers.
[Source: Wesgro, 2000]

5.2. Fishing and aquaculture/mariculture

5.2.1. Fishing

The fishing industry is a major employer and income generator in the Western Cape. The Province accounts for 70 per cent of national employment and 71 per cent of income earned from fishing in South Africa. In total, approximately 27 000 people are employed in the industry in the Western Cape, predominantly from historically disadvantaged groups and in jobs of a semi-skilled nature.

As with agriculture, the importance of the industry extends to the processing, packaging and export of the product. For example, the pilchard and anchovy catch supports eight fish-meal plants, six canning factories and more than 40 bait-packing facilities. Employment in secondary and tertiary activities is roughly equivalent to primary activities (on vessels and on-shore support).

The key market for fishing is exports, and the industry is the third-largest exporter in the Province after fruit and wine, representing 8,5 per cent of total Western Cape exports. Exports have been growing in both mass and value terms in recent years. The most important products are frozen fish and fish fillets and cutlets. The main export destinations are Europe, Asia, Canada and Australia, and several African countries such as Angola.

The two main dynamics in recent years have been the transformation of the industry and the need to manage fish stocks in a sustainable way. Transformation is primarily the result of a change in the number and size of fishing rights allocated. Some 2 625 rights (or quotas) were allocated in 2001, of which at least 2 000 qualify as SMMEs. Historically disadvantaged persons now own approximately 60 per cent of quotas, enhancing income generation in poor fishing communities. Despite such progress, there is still much to be done in respect of employment, income generation, skills development and distribution, as well as livelihoods in these communities.

Looking ahead, the fishing industry faces a number of key constraints. These include natural resources limitations with increased demand for resource access, the continued marginalisation of small fishers, limited access to capital for new entrants and poor fishers, destabilising livelihoods in a seasonal industry, and skills composition among traditional fishers and small operators. Poaching and corrupt behaviour in certain sub-sectors and poor resource conditions in line fish and abalone also pose risks.

There are, however, equally important opportunities for future growth. These include local beneficiation and value addition, improving the infrastructure and enhancing the status of women in the industry (DEDAT, 2005: 89).

5.2.2. Aquaculture and mariculture

Aquaculture (freshwater cultivation of trout, crocodiles, ornamental fish, catfish and tilapia) and mariculture (marine cultivation of abalone, prawns, oysters, seaweed and mussels) are small but have been growing rapidly, with growth rates of up to 25 per cent per annum in the late 1990s. Mariculture, in particular, has shown great potential, with the majority of activities taking place in the Western Cape.

Mariculture encompasses abalone of which South Africa is a net exporter with 15 commercial farms, as well as mussels and oysters in which the country is a net importer. Cultivation has increased in each of these, with potential for further expansion. In addition, there is potential for growing the kelp and seaweed industries, with expanded employment opportunities.

While prospects for the sub-sector are extremely promising, a critical concern is the location of suitable sites along the south and west coast for farming purposes. Furthermore, the industry is capital intensive and involves imported technology and expertise. There is therefore need for technological adaptations towards smaller-scale models that are technologically more effective, hold lower risk and could have on enhanced impact on poverty alleviation in poor communities (DEDAT, 2005: 91).

5.3. Tourism

Tourism has been identified as a major growth impetus for the Province, with ambitious targets set for 2010 in the Provincial White Paper of 2001. However, the lack of good statistics means it is difficult to evaluate performance. Information on overseas tourist arrivals indicates there was an increase of 30 per cent in 2002 following the rand's depreciation. While this growth was not maintained in 2003 as the rand strengthened, it is encouraging that numbers did not decline.

Recent reports suggest that tourism-related revenues are increasing once more in 2004. Of concern is that the foreign visitor's average length of stay in the Province appears to have declined. Moreover, the affordability of Cape Town in particular has come under increasing scrutiny.

Even less is known about local tourism and visitors from other African countries. Encouraging these visitors to the Province is also an important goal. Cheaper domestic air-fares with increased competition has undoubtedly made it much more affordable to travel to Cape Town from destinations such as Johannesburg, and increased flights suggest the numbers of visitors has increased, but assessing the impact is difficult.

South Africa Tourism has identified local tourism as a high-potential growth area, further development of which requires greater local promotion as well as products suited to local tourism consumers. These include packages linked to local events, off-season specials, and cost-effective group travel packages.

Of critical importance is the management of tourism as a system, with infrastructure provision, marketing, skill development and improved service all part of the package. In addition, there has been relatively little integration of tourism to link the City of Cape Town to regional centres elsewhere in the Province. The vast majority of tourists stay in the City of Cape Town with day trips outside, but do not extend their stay with longer excursions throughout the Province.

A further priority identified by the Province is to increase the involvement of previously disadvantaged individuals through their role in providing services and through increased township tourism. Low barriers to entry into tourism-related activities mean there are great opportunities, but without clear strategies these will not be realised. The developing policy framework sets out an integrated approach; the challenge is to design and implement concrete actions.

Two new transformation initiatives are also proposed – the facilitation of the set-up of craft, jewellery and cabinet-making co-operatives in the Province, and initiating research into extended beach tourism. The latter would explore the costs, benefits and feasibility of the Province positioning itself as an international destination for beach tourism. Of necessity, this would have to explore the environmental implications as well as attitudes of local residents to extended beach tourism initiatives (DEDAT, 2005: 117).

Co-operatives development in South Africa

Government has recognized the value that co-operatives development may play in promoting entrepreneurship and SMMEs, and contribute to enhanced employment, black economic empowerment and reduced inequality in South Africa over time.

In brief, a co-operative is a type of ownership that members form to combine skill or capital to achieve a specific objective, such as profit. Co-operatives differ from other forms of ownership due to few formalities required to register the enterprise, as well as its independence from its founders. Furthermore, there is no limit to the number of people who may join a co-operative.

At present, co-operatives in South Africa do not have legal capacity to perform juristic acts, making it difficult for them to acquire financial assistance. Government is now introducing enabling legislation – the Co-operatives Bill – that enables co-operatives to operative as legal entities, facilitating their development and sustainability.

The dti is leading the formulation of government policy to incorporate co-operatives in the mainstream economy, and is currently designing a grant that will enable co-operative members to access finance with fewer legal requirements. National Treasury is also involved in the process by developing tax incentives and other enabling regulations, such as the Co-operatives Banks Bill, which will enable financial services co-operatives to operate as banks and offer their services to unbanked communities. These co-operatives will be exempted from the requirements of the Bank Act, and fewer legal requirements will apply to institutions.

[Source: Shabalala, 2005]

5.4. Clothing and textiles

The clothing & textiles industries account for the single largest share of manufacturing employment in the Western Cape. However, in line with national trends, employment levels have been falling sharply. There have been huge job losses – in the 18 months from January 2003 to June 2004 it is estimated that 27 000 jobs have been lost nationally.

The clothing & textile industries are driven by the demands of the main international retailers. The latter expect low prices, high quality and rapid delivery on designs. Retailers such as Walmart in the US govern the clothing and textile ‘value chain’ around the world, dictating standards of design, delivery, quality and price to the different levels of production, from yarn through to fabric and the making-up of the garments. Their control ensures delivery to their specifications and enables the retailer to capture the largest share of the value that is created.

Value in the clothing industries derives less from the production capabilities than from the branding and distribution of the product to consumers in industrialised markets. It is very difficult for South African firms to have any influence over major brands; instead they are made to compete against other manufacturers for the same customer located in different countries around the world. There are, however, product niches where firms can develop their own brand identities. South Africa has also been more successful in non-clothing parts of textiles.

The biggest development in the last five years has been China's ability to compete on the delivery, design and quality criteria at very large volumes, which means they are highly price competitive. To compete entails investing in up-to-date machinery and having very efficient work organisation. China does not have the lowest clothing labour costs but has been investing heavily in machinery and equipment for its textile and clothing industries.

The South African industry has not, in most cases, made the changes necessary to lay the foundation for sustained improvements in competitiveness. There has been some investment in new machinery and equipment, but on average the machinery being used is quite old.

Of greater importance appears to be a very slow adjustment to new ways of working – to improve throughput time, ensure quality at every level of production and broadly be able to respond to the demands of international, and increasingly also of local, buyers. Recent benchmarking of Western Cape firms against best practice internationally and locally reveals great room for efficiency improvements.

The removal of quota restrictions under the Multi-Fibre Agreement (MFA) as of 1 January 2005 further threatens the South African industry. The MFA meant that countries were subject to maximum limits on their exports of clothing and textiles. This originally protected the clothing industries in countries such as the UK, but recently the biggest effect has been to limit South Africa'a exposure to competition from countries such as China for these markets.

Asian firms in particular have a long history of 'quota hopping': moving production facilities to developing countries with low labour costs that have not fulfilled their quotas. With the ending of restrictions, there is likely to be greatly increased concentration of clothing and textiles production in countries such as China, India and Pakistan.

An advantage for clothing and textiles in African countries has been the AGOA, which provided for duty-free access to the US market – a significant advantage given that US tariffs average 17 per cent on apparel imports. South Africa (along with Mauritius) is at a disadvantage, however, as it is required to use local fabric and yarn (or to import from the US). Other countries, such as Lesotho, are not subject to this triple-stage transformation requirement and have rapidly increased exports to the US of garments, generally of low-price basic items. Recently, investments have also been made in textiles factories in Lesotho, which entails more stages of processing.

Multi Fibre Agreement (MFA

Clothing & textiles were excluded in 1947 under the General Agreement on Tariffs and Trade (GATT), which was the forerunner of the World Trade Organisation (WTO). In 1974, the MFA was signed, ratifying countries' rights to impose tariffs on clothing and textile imports. The MFA's objective was to allow developed countries time to restructure their clothing & textile industries before opening up to competition from developing countries. Although meant to be temporary, the MFA was frequently renewed. In 1994, the GATT signatories signed the Agreement on Textiles and Clothing (ATC), committing to phasing out the MFA by 1 January 2005.

One of the major concerns is how countries such as China and India, which have become major threats to clothing and textile-producing countries across the developed and developing world, will behave now that quotas have been removed.

Experts predict that in a quota-free world, China's share of world clothing exports will double in less than five years and that more than 80 per cent of clothing production may move to China.

Low wages are often attributed to China's success. However, while wages in China are competitive, they are not the lowest in the world. There are other reasons for China's export success. The most noted is China's maintenance of at least a 15 per cent under-valuation of its currency as it pegs the Yuan to the US dollar. This currency under-valuation has the effect of acting as an export subsidy to the industry.

Second, the Chinese government has a 52 per cent ownership interest in textiles and 25 per cent in clothing. It subsidises output by providing these industries with access to cheap capital, thereby allowing firms to undercut the prices of their competitors and increase their market share.

Clothing and textiles are important industries and export earners for both developed and developing countries. China's increasing dominance is therefore a concern – not only for the US and the EU but also for Mexico, the Caribbean and SSA.

Despite risks to the global outlook, there is substantial scope for export growth in the sector, particularly to growing middle-income countries. This may require repositioning and restructuring of domestic industry to ensure improved competitiveness in the new global order.

[Source: Morris, Barnes and Esselaar, 2004: 7]

The Western Cape clothing & textiles industries are strongest in niche areas where there is a quality or design advantage, such as in worsted woollen suits to the UK market primarily. There are also firms making high-quality household textiles, again targeted to the EU market.

Following international trends, local retailers have also become much more demanding in terms of price, quality, flexibility and variety. As a result, Western Cape firms have become more design-oriented and focused on serving the upper end of the market, which has also led to formal factory downsizing and increasing outsourcing of garment manufacturing to cut-make-trim operations.

Future performance of the industry requires going further to build firms' competitive capabilities in high quality and design niches. In this regard, high-quality fabrics are very important. This requires co-operation between firms in the industry, and the development of appropriate local institutions oriented to technological development and design.

The strategies at a Provincial level need to link with a coherent national industrial policy for the sector. Important revisions include changes to the workings of the duty credit certificate scheme (DCCS). At present, retailers use the DCCS credits from clothing exports to import duty-free products rather than clothing firms using them to import inputs at internationally competitive prices.

Duty Credit Certificate Scheme

The DCCS is an export incentive programme for the clothing & textile industries in South Africa and is aimed at encouraging the outward orientation of the two related industries.

Set to expire on 31 March 2005, the DCCS permits firms to claim a remission of duty for proven exports. Alternatively, rebates may be sold to any other importer of clothing and textiles. The level of support depends on the product exported. Relief granted ranges from a minimum of eight per cent of the export sales value for yarn exporters whose export sales represent 15 per cent of total sales, to 35 per cent for clothing exporters whose sales represent more than 15 per cent of total sales.

As a result of restrictions on the use of the DCCS as well as its tradeability, the majority of the DCCS is sold, benefiting major retailers. The latter pay as much as a 30 per cent to 40 per cent discount on the DCCS which they then use to import clothing and textiles, thereby decompressing local industry.

The dti has indicated that the DCCS would not be extended past 31 March 2005. In response, the industries submitted a joint proposal requesting that a two-year Interim Development Programme be implemented for both industries, allowing them time to restructure before phasing the programme out completely. The DCCS has now been extended and made more powerful. Smaller firms that used to get 15 per cent now get the full allowance. There are further possible changes in the pipeline.

[Source: Morris, Barnes and Esselaar, 2004:7]

5.5. Metals and machinery

The metals and machinery industry grouping is at the heart of the manufacturing industry. It encompasses the basic manufacture of metals through to the working of metal to make machinery and equipment – the capital equipment which is used across industries to transform materials into manufactured products through successive stages of processing. The Western Cape has the advantages of availability of basic metals, a relatively good skills base, developed infrastructure and a coastal location.

While the industries in the Province have suffered from the same slump as the country as a whole, there has been growth of output and employment over the last three years. Employment in 2003 was nine per cent higher than in 2000.
The better performance of the sector in the Western Cape is reflected in its trade performance. There have been big improvements of exports from the Province relative to imports in most product categories, except for electrical machinery & appliances. Increasing international integration means that the Western Cape has the opportunity to benefit from improved opportunities to export – if the appropriate environment is in place.

In addition, there are three key recent developments which point to much-improved performance in the next decade:

- The expansion of basic steel production in the Province at Saldanha and the negotiation of a developmental pricing arrangement to ensure that local buyers of steel benefit from competitive steel prices holds a huge opportunity to increase local beneficiation for export.
- The growth of cast components for the auto sector. These are strongly export-oriented and have developed without the presence of a major auto assembly operation in the Western Cape, reflecting the competitiveness of the Western Cape industry.
- Increased investment spending by National Government on infrastructure. This will have important demand effects for metals and machinery industries.

The key challenge for broad-based employment creation is to grow downstream industries. Fabrication of metal products is a relatively labour-intensive operation and requires mainly low-skilled labour. While labour-intensive, firm competitiveness also requires competitively priced material inputs and investment in up-to-date machinery to be able to ensure quality and reliable on-time delivery, and the necessary skills in areas such as design and tool-making. For example, 37 per cent of direct material inputs for fabricated metal products are basic iron & steel and even for the more sophisticated general machinery products, iron & steel accounts for one-quarter of all material inputs when the iron & steel content of components is taken into account. Competitively priced steel inputs (as opposed to the import-parity pricing charged by Ispat-Iscor and other metals producers) will fundamentally alter the competitiveness of downstream labour-intensive industry in the Province.

Metal fabrication industries are well-established in the Western Cape, with specific links into markets for marine equipment, tank containers and food packaging (ship-building and repair is addressed separately below). Internationally, industry growth is characterised by clusters of firms developing niche capabilities and drawing on shared services, including technical and design services, skills development and R&D facilities.

The importance of quality, design and delivery has been emphasised by recent studies of the sector. This points to the importance of ongoing upgrading of skills, and the increasing use of computer-aided design and computer numerically-controlled machining, which enables greater precision. A sustainable growth strategy therefore requires attention to the network of shared facilities, in addition to vertical linkages from material inputs through to markets. The Western Cape is fortunate in this regard in having well-established tertiary education institutions.

The Western Cape foundry industry has undergone something of a renaissance with the growth of small and medium firms supplying a range of diverse markets. The auto industry has been the main source of growth, however, firms also supply castings for the general engineering and machinery, electrical machinery, railway equipment, medical equipment, ICT, defence and shipbuilding industries.

The ability of transnational corporations to source castings from anywhere in the world means that continued improvements in technological capabilities are crucial alongside cost-competitiveness. The majority of foundries in the Western Cape have introduced technologically improved castings, with both incremental improvements and radical developments in the production process.

Crucially, the industry has started to reap the economic gains that derive from agglomeration and clustering. Firms in the Province share knowledge and expertise and have devised a common training programme, even before this has been done at the national level.

Two important national initiatives are directly relevant to metals and machinery – the AMI and the National Tooling Initiative. The AMI's light-metals focus is particularly relevant for firms supplying the aerospace and automobile industries. The National Tooling Initiative has been launched by the CSIR's National Product Development Centre and is initially being driven by the auto sector. However, improved tooling capabilities are important for many industries, including plastics. Without good local tool-making firms, South African manufacturers often have to source their tooling and moulds from overseas countries, such as Italy.

Steel pricing developments and beneficiation

The Western Cape is a major producer of primary steel at Saldanha. From originally being orientated 100 per cent towards export, it is the intention of both National Government and of Ispat-Iscor that there is increased local beneficiation. To an extent this has already occurred, although local beneficiation in the Western Cape has largely been limited to galvanising and re-rolling. Ispat-Iscor's intention is also to double the production of Saldanha Steel in the very near future.

The main obstacle to local beneficiation is the current import parity pricing practised by Ispat-Iscor. This means charging prices equal to those that a local buyer would have to pay to import the product, including the notional costs of shipping, tariffs, wharfage and port charges.

However, in the case of steel there is a very large trade surplus, reflecting South Africa's competitive and comparative advantage in steel, and there is no need to import. In such conditions, additional local consumption means exporting less. But, while South Africa has low production costs for steel – certainly below the international average – it has much higher than average local prices for steel, placing steel using industries at an immediate competitive disadvantage. The prices charged to local buyers of steel are between 30 per cent and 50 per cent higher than the prices received for exported steel.

Indeed, the size of the notional costs added in depends on geographical accident, as the price mark-up is due partly to the distance of the local market from the sources of imports. In flat-steel products, the market power of the main producers is such that they maintain their prices just at the level at which it is not worth it for a local buyer actually to import.

Current negotiations of a developmental pricing framework to replace the import parity pricing being practised by Ispar-Iscor pose a major opportunity for growth of industries around Saldanha.

The establishment of a service centre already means that steel can be cut and slit for use by fabricators, and there are several firms engaged in manufacture of products, such as palisade fencing, for export. It should be emphasised that there are very large employment creation opportunities of a mainly low-skilled nature in metal fabrication.

A Saldanha steel beneficiation cluster requires:

- Provincial Government to facilitate beneficial pricing for local firms as part of the wider pricing framework.
- An industrial development plan for the area, the current lack of which apparently is holding up further industrial growth (despite the location of heavy industries in the area).
- Provision of infrastructure for firms making 'greenfield' investments (that is, establishing new factories or production sites).
- A commitment to provide the appropriate training support – essentially to ensure that firms can use the skills development framework.
- Support for small firms, for example in accessing export markets and financing investments in new capital, to name a few.

5.5.1. Motor vehicles

The South African motor vehicle sector has recorded one of the highest rates of output growth over the past decade. This has been largely due to the Motor Industry Development Programme (MIDP) which provides a structured plan to encourage the local production and export of motor vehicles and components. This allows the main auto firms to obtain duty-free import licences for car models not made in South Africa. Although the Western Cape does not have a major motor vehicle assembler, there has been growth in auto components in the Province.

Catalytic converters is by far the largest single category of auto components exports, with exports of R8,1-billion in 2003 (a share in total components exports of 38%), followed by seat leather with exports of R2,9-billion and tyre exports of R1,3-billion. Of importance for the Western Cape is the increasing diversification of components exports, and particularly the increased exports of engine parts, which rose to fourth place in 2003, with exports of R0,8 billion, with exports of engines and auto tooling not far behind.

Exports of motor vehicles and components from the Western Cape are still relatively small at R347-million in 2003, but have increased strongly. For example, in 1998 they totalled just R99-million. However, the stronger rand in 2003 impacted negatively on the local currency value of exports, and has placed increased pressure on firms to improve their international competitiveness.

5.6. Ship- and yacht-building

The Western Cape has long been a base of ship-building and repair, and has recently developed into a major boat-building location for yachts. While all related to water-born craft, these industries operate on quite different bases. Ship-building and repair have an engineering base, and are predominantly concerned with metal-working – mainly steel. Making yachts is a very sophisticated activity, with a range of materials.

The international ship-building industry is currently booming as increased freight drives global demand. The major players are Asian countries and, in particular, Japan, South Korea and China. After a major slump in ship-building in the Western Cape, with only one major ship-building firm left, there is now potential for growth, particularly in small and medium vessels in which the Western Cape has a geographical advantage over the big Asian producers in the African market.

Ship-building potential

There is a major opportunity for the Western Cape to develop a ship-building industry focused on smaller vessels, such as tugs and harbour craft, targeted at the west coast of Africa. The only current producer is performing well, and there is interest from new entrants. A key obstacle is the financing provided by European countries for exports of ships. A competitive financing package is therefore required, and would be consistent with the New Economic Plan for African Development objectives, where South Africa becomes a major supplier of ships to the other African countries.

Local ship-building essentially requires steel and labour. The important design activities and engine components are sourced internationally and this would continue in the early stages. Partnerships with international ship-builders are important for design and technology. Ship engines are sourced from a small number of manufacturers globally and provision should be made for their duty-free importation.

A Western Cape ship-building initiative requires:

- Identification of sites for major new ship-builders and appropriate infrastructure provision.
- Identification of potential investors – foreign and local. (Reportedly, major foreign concerns have already shown interest.)
- Development of a 'package'; including export financing in conjunction with national agencies such as the Industrial Development Corporation (IDC). In the medium term, the package would include development of local design and research capacities ,with universities building on what already exists.
- A steel pricing deal for ship-building firms (such as the current auto industry currently deal).
- An industry development body (again, the Auto Industry Development Council provides one possible model).

Ship repair is labour-intensive and provides between 1 700 to 2 000 direct jobs nationally, with 1 000 being in the Western Cape. Moreover, the employment in related activities is also significant.

The Province has always been the main repair location in South Africa, benefiting from well-developed facilities and its ideal location. The development of offshore oil and gas fields off the west coast of Africa have added to the demand for services, while foreign fishing fleets also use the Port of Cape Town's facilities.

The main bottleneck to the expansion of the sector is the available port infrastructure and its management. The facilities in Cape Town include two dry docks and a shiplift facility; however, these are sometimes fully utilised, which means ships move elsewhere, to East London or to other countries altogether. It is estimated that the Western Cape loses an average of R14-million annually for vessels turned away due to lack of quay and repair space. A new shiplift facility is planned, which will increase repair capacity considerably; however, the huge increases in international shipping traffic suggests that demand for repair services will continue to rise.

Oil & gas

The oil & gas supply sector in the Western Cape is extremely diverse, and includes ship and rig maintenance and repair, logistics, marine construction and engineering, sea and air freight, and personnel transport. It is a specific niche within the broader activities in ship-building and repair, benefiting from the Western Cape's unique position and infrastructure.

The industry initially took off to meet the need of exploration and production by companies off the South African coast, but now the major opportunities lie with offshore exploration and production up the west coast of Africa. In 2003, 80 wells were drilled off the west African coast, with exploration and production spending of over US$10-billion. It is estimated that despite South African firms supplying less than one per cent of the needs in this market, the activity in 2003 supported 5 000 jobs in South Africa.

The Cape Oil and Gas Supply Initiative aims to position the Western Cape as the preferred oil and gas service and supply hub for exploration and production off the African west coast. To do this requires addressing a range of obstacles, including:

- Price and availability of specialist steel products;
- Infrastructure and port inefficiencies;
- Skills and training needs;
- Technology transfer and the attraction of foreign players to the Western Cape; and
- Improved visibility and marketing.

It has already succeeded in facilitating several large deals bringing business to the Western Cape, but much needs to be done to address the core issues impeding broad-based growth of the sector.

5.6.1. Yacht manufacture

Boat-building, which accounts for approximately 70 per cent of activity in South Africa, has been long-established in the Western Cape. The manufacture of yachts for cruising and racing has recently underpinned a rapid expansion of the industry in the Province, notwithstanding the poor performance in 2003 with the strengthening of the rand (when export earnings in rand terms fell 50%).

Exports of ships and boats from the Western Cape increased from just R45-million in 1997 to R569-million in 2002, before falling back to R269-million in 2003. The indications are that, after some painful adjustment, the industry is growing once more.

The Western Cape has the important pre-requisites for boat-building, namely a network of the various suppliers required (including sail-makers, composites and metal fabricators), a tradition of boat-building and the skills base that accompanies it, as well as a relatively good business environment for manufacture and export.

The competencies required for boat-building can be broken-down into:

- Boat construction;
- Supply industries of related products and services, such as sail-making, mast builders and riggers, and naval architecture;
- Outsourced manufacturing of component parts; and
- Post-production services.

Some firms specialise in making products and systems for one boat-builder, while others make components for many firms, including those outside boat-building, for example, in making stainless steel fittings. The competitiveness of the whole depends on the performance of each of the parts, as high-specification boats are reliant on all the parts working together. The Western Cape has also tended to make small numbers of boats, often custom designed, which differs from the trajectory followed in, for example, New Zealand, which has firms engaged in mass production.

Of critical importance for ongoing growth of the industry is attention to the pricing of material inputs, improved training and skills development, support for product development and research, and appropriate support for exporters. Together this suggests a framework for collective action by the industry, which has recently led to the launch of the Cape Town Boat-building and Technology initiative (CTBi).

Cape Town Boat-building and Technology initiative

Following studies commissioned by Wesgro and **the dti**, which identified key constraints in the future growth of the industry in the Western Cape, the CTBi was launched in mid-2004 with the following objectives:

- To identify the key industry bottlenecks restricting further growth and development;
- To develop a three- to five-year strategic business plan with programmes to unlock this potential; and
- To implement and manage the strategic business plan.

Initiatives are underway to address issues of skills training, suitable financial products for boat-building, increased international exposure, improved co-operation within the industry and regulatory and legislative issues. A generic one-year boat-building qualification is currently being designed for introduction in 2005.

5.7. Information and communication technology

The ICT sector provides a range of goods and services that support electronic display, processing, storage and transmission of information. With ongoing developments in technology, this sector is growing strongly. One key area of employment is in the business process outsourcing and contact centre sector – this is reviewed separately below due to its importance.

Total information technology spending nationally was estimated to reach R37,8-billion by the end of 2002 and to grow by 10,9 per cent per annum to R57,1-billion by 2006. The majority of the turnover is estimated to be in software design and development, and IT services. Gauteng has the largest shares of the 6 400 firms and 212 000 employees nationally. The Western Cape is in second place with 16 per cent of firms and an estimated 27 000 employees (13%).

The main strengths of the Western Cape are in the good skills, infrastructure, communications network, and the Cape IT initiative. These have underpinned the growth of the foreign client base.

The main challenges are, however, the small local market and an effective response to BEE. Much of the software development is for local clients, which entails that growth depends on the developments of sectors such as financial services which demand ICT solutions.

5.7.1. Contact centre and business process outsourcing industry (BPO)

The BPO and contact centre industry was identified in 2003 as one of five key growth sectors to drive employment in the Province, and the government has targeted it to create 5 000 new jobs by 2008. The industry is well developed in the Western Cape, with a broad base of management and service provider expertise.

There are now more than 105 active operations in Cape Town, with over 11 000 employees. Offshore outsourcing is a key area, and the main driver of industry growth. Approximately 55 per cent of the revenue of BPO operators came from international clients in 2004, with seven foreign languages offered.

Key strengths of the Western Cape industry include the depth of financial services expertise, particularly in insurance, mortgage and loan processing. Financial services operations account for more than half of the employees in the industry. Coupled with this are the excellent skills base, good technology and infrastructure, and the sophistication of the local industry. Productivity measures such as first-call resolution are high by international comparisons, and the attrition rates of employees are low. Wages are not high by international comparisons and are around one-third of those in the UK.

With the fall in telecommunications costs, expected competition from a second national operator and liberalisation in February 2005 allowing voice services to be carried over the Internet, there is great potential for growth.

To meet the potential demand, the industry is working together with government to grow and develop the skills pool. A non-profit organisation, CallingtheCape was established in 2001 as a partnership between industry and Local and Provincial Government to promote and develop the industry.

Small Enterprises

In many industries, small enterprises are at the heart of growth and dynamism. In South Africa, recent survey research has estimated that there are 4,9-million people in the 'small business sector' (in firms with 10 or fewer employees). Often small enterprises dominate in the more labour-intensive downstream sectors, as well as in industries based on design and craft skills such as boat-building. The level of entrepreneurial activity is thus clearly important for the growth of provincial and local economies.

The Global Entrepreneurship Monitor (GEM) is an international research project which examines new business formation in more than 30 countries. Its findings indicate that entrepreneurial activity in South Africa is generally low by international comparisons. However, the Western Cape, along with Gauteng, has significantly higher levels of activity than the rest of the country.

Importantly, the survey distinguishes between entrepreneurial activity driven by 'opportunity' (where an attractive opportunity stimulates the entrepreneur to set up) rather than 'necessity' (where the entrepreneurial activity is because of the lack of alternative income-generating activities). The Western Cape scores higher on opportunity than any other province. The Western Cape (and Gauteng) also has a high rate of start-ups and new firms. (Start-ups are firms that have not paid wages or salaries for more than three months, while new firms are those that have paid wages or salaries for between three months and three and a half years.)

In the Western Cape, all owner-managed businesses were estimated to employ approximately 542 000 people, excluding the owner-managers. Of these, 103 000 were in start-ups, 146 000 were in new firms, and 292 000 were in established firms. Opportunity-motivated owner-manager businesses employed 312 000 people, compared with 53 000 in necessity-based owner-manager enterprises. The main sector in which entrepreneurial activity occurs is the retail, restaurants and hotel industry. thirty nine per cent of established and new firms are in this sector, and 47 per cent of start-ups.

Perhaps surprisingly, firms in the Western Cape are not more export-oriented than those nationally, although entrepreneurial firms in South Africa are more export-oriented than in other countries.

While entrepreneurial activity is important for the growth of the Provincial economy, it is important to distinguish entrepreneurial drive (which may underpin the growth of established firms) from the establishment of new firms as such. While new firms have an important impact in creating new employment, increased employment still derives to a greater extent from the growth of established firms. The key challenge is the survival rates of firms once established. This depends on the entrepreneurs, but also on the environment in which entrepreneurs operate.

6. Drivers of Provincial Economic Performance

To a large extent, the drivers of provincial economic performance are national. The restructuring of industry in the past decade has been reflected in poor performance and employment losses in the Province. Similarly, the improved national growth in the past year and the move to a more expansionary macroeconomic stance means the Province should plan for growth – in addressing training, infrastructure and investment by firms. The stimulus for growth is, however, primarily domestic demand.

At the sectoral level, Provincial growth and employment need to rest on a broad foundation of agriculture, industrial regeneration, tourism and services, such as BPO. The pattern of higher growth in financial & business services and tourism, with agriculture remaining very important, does not negate the need to further develop the manufacturing base further.

The far-reaching economic restructuring brought about by policy reforms in the past 10 years means that now is a crucial time to plan for expansion – both regeneration of some of the more traditional industries and new growth. The liberalisation of the economy entailed tough adaptation to increased international competition and a tightening of macroeconomic policies, including high real interest rates. This period is over, or at least for the time being. The tariff reductions are essentially complete, and Government is expanding capital spending, while real interest rates are expected to decline gradually.

A crucial dimension in the Western Cape is its coastal location and the opportunities that arise from it. These opportunities are not only in exports, but also in deepening international links around investment, technology and production networks. The trade data reveals that some sectors have made major gains, led by agriculture, food & beverages and transport equipment. The challenge is to translate the opportunities into output growth and employment in relatively labour-intensive areas of manufacturing.

The way in which increased international integration impacts on the Provincial economy, and the impacts on different groups such as low-skilled and high-skilled workers and different economic sectors, depend to an important extent on actions by Government, in respect of integration and incetivising progammes and interventions.

Broad-based manufacturing growth depends on the patterns of competitiveness in the Provincial economy. Competitiveness in the context of being able to deliver on design, quality and delivery dimensions requires vibrant firm clusters and effective local institutions. For example, in the absence of an appropriate framework, the Province will continue with exports of unbeneficiated metals and in niches such as yacht-building, with relatively limited returns to the wider economy. Interventions around the pricing of steel and the needs of downstream metals products and machinery firms are areas of possible concrete action.

The broad approach here is in line with the thrust of National Government's industrial, trade, technology and skills policies. The challenge is to ensure *effective implementation*. This relates to building/developing effective local institutions and to information gathering, analysis and dissemination. Together this will mean that Provincial Government is able to play a crucial co-ordinating role – building linkages between different programmes, ensuring coherence and consistency, and identifying and removing bottlenecks. This is also very important if government attention is to be directed to less high-profile sectors and industries, which may have much greater potential to absorb low-skilled labour and thereby contribute to poverty alleviation.

From the sector analysis, the following main priorities in building competitive capabilities of producers emerge:

- Ongoing upgrading of agriculture, with emphasis on a broader base of higher value-added products, and support for the research and standards necessary for exporting. This needs to be complemented by support for smaller and historically disadvantaged farmers.
- Addressing cost competitiveness issues in industry (including steel prices); which are impeding the performance of labour-intensive, relatively basic products.
- Developing and implementing action-oriented plans to ensure that policies for skills and training are being implemented effectively. This requires addressing the use of the skills levy, the administration involved, and the provision of appropriate courses by local institutions. These measures will be employment generating in themselves, as increased training activities will lead to the growth of local educational and training institutions.
- Monitoring the various technology initiatives and identifying where Provincial and Local Government facilitation can ensure the potential gains are realised (including the National Tooling Initiative and the AMI). The Province needs to proactively identify areas to develop local technological competency in tertiary education and other research institutions.
- Facilitating of ongoing growth in industries already performing well, such as yacht-building and film-making, with particular emphasis on the quality and quantity of employment.
- Selection of a small number of target areas where Government action can facilitate significant expansion. These include:
    - Ship-building in medium and small vessels;
    - Herbal and natural products such as essential oils;
    - Furniture; and
    - BPO.
- Mechanisms to build inter-firm communication and co-operation, such as benchmarking (which is specifically proposed for foundries and clothing).

Government support should be linked to clear performance criteria and expectations within specified time frames. In this way, the interventions influence firm behaviour, and firms are provided certainty as to what government will provide.

The prospects are good for sustained employment generation as part of a dynamic and diversified growth path.

Benchmarking and cluster development

The development of local clusters is premised on the collective gains from shared services, suppliers and skills development in localised areas, as discussed above. However, collections of firms do not necessarily become clusters. *Benchmarking* relates to a process of inter-firm learning and upgrading to improve operational performance.

Initially, benchmarking – exemplified in South Africa by those in the auto industry – compares firm performance across a range of criteria related to cost control, quality, flexibility and capacity to change. This enables firms to see clearly how far they are from best performance amongst their peers, and naturally leads to a desire to improve and to learn from other firms.

Improved relationships between firms can then graduate to a process of continuous improvement and the development of clusters where firms co-operate to improve competitiveness. Firms may be reluctant to participate together with those they regard as their competitors; however, it is important to distinguish the dynamic development of competitive capabilities from the static competition between firms for a given market. Increased international integration means it is important to view competitiveness in international terms, and related to the development of new markets and product niches.

Benchmarking initiatives are particularly useful where a need for upgrading of firms' competitiveness in terms of quality and delivery has been identified, which points to the importance of examining the organisation of production within firms.

This is relevant for many manufacturing sectors in South Africa, given the environment of a typically ageing management locked into 'ways of working' developed in a relatively protected local market. To achieve firm commitment to an initiative, however, requires analysis to demonstrate to firms the basis of their poor performance and to highlight the future development path in the absence of purposive action.