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Spending Review on the Special Economic Zones: 2020/21

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Summary

In the early 2000s, government launched the industrial development zones (IDZ) programme aimed at attracting foreign investment and export of value added commodities. A review of the programme in 2007 revealed that the programme had a number of challenges which included: lack of coordinated planning arrangements; insufficient guidance in relation to governance arrangements; dependence on government funding; lack of targeted investment promotion measures; and insufficient marketing and inadequate coordination across government agencies.

With these challenges, a case was therefore made to develop a new policy with a wider range of instruments. This culminated into the special economic zone (SEZ) policy. The SEZ policy sought to provide a clear framework on the development, operations, and management of SEZ. The programme's purpose was therefore to expand the strategic focus to cover different regional development needs; provide a clear, predictable and systemic planning framework for the development of a variety of SEZs to support industrial policy objectives; clarify and strengthen governance arrangements; expand the range and quality of support measures apart from infrastructure; and provide for predictable funding arrangements. As a result, the SEZ Act (16 of 2014) was enacted.

To date 11 SEZs[1] have been designated and government has spent approximately over R25 billion on the programme since the inception of IDZs. The bulk of funding was through the Department of Trade, Industry and Competition (DTIC) mainly towards infrastructure (top structures and bulk works). Provincial governments fund operational expenditure and capital expenditure in some cases.

Out of the 11 SEZs, Coega, East London and Dube Tradeport have the largest number of investors. Others such as Richards Bay and OR Tambo IDZ were designated in 2002 but have struggled to attract investors. Considering government spending on the programme to date, the spending review was undertaken to determine the effectiveness and efficiency of the SEZ programme in realising the Act's objectives.

Most SEZ operators are not able to generate sufficient revenue to be financially self-sustaining; they are loss-making and rely on fiscal support from the provinces for operational expenditure while most capital is funded through the SEZ Fund within the DTIC.

In general, SEZ performance reporting has been problematic. Zones are not reporting consistent information. Reports are not standardised. As a result, it is difficult to track key data. While the DTIC often argues that the 16 302 direct jobs and R17.2 billion worth of investment reported in 2018/19 Q4 could not have been realised without the SEZ programme, an argument is also advanced about the extent to which investment took place because of this programme. This especially in the context of concern expressed by many zones that government has not delivered on the promised SEZ incentives, which includes the 15 per cent corporate income tax. A key question to ask of a programme such as this is whether expenditure on subsidies and incentives generated economic activity that would not have happened anyway. This is a very hard question to answer, but it cannot be assumed that every activity that is located in an SEZ would not have happened if there were no SEZs. The DTIC, provinces and SEZs should demonstrate the extent of this causality to justify continuous

[1] The newly designated Tshwane Automotive SEZ is counted as standalone here. However, the DTIC designated it as part of the OR Tambo SEZ.

support. Therefore, there is a need for the DTIC to conduct a comprehensive evaluation of the programme to determine the return on investment.

Considering that only three SEZs have managed to attract a sizable number of investors while some have struggled and that most SEZs are loss making, government may need to reallocate resources. Government cannot afford to continue supporting SEZs that are failing to attract investors. Therefore, government should evaluate whether it is necessary to continue to support SEZs that have failed to attract investors or whether these should be closed. This should be coupled with suspension of designating new SEZs especially in areas that have no comparative advantages at all. These decisions need to take account of commitments to and the needs of existing investors.

Government should consider collaborating with the private sector in the management of SEZs under the PPP arrangement. It seems that current approach does not stimulate operators to be profit-minded and be financially self-sustaining. Alternatively, consideration should be given to privately managed SEZ in the same way that office parks or shopping malls are managed.

There is a need for the DTIC to implement a digital performance monitoring system for SEZs. This will ensure timely and consistent reporting. It seems that the current system is fragmented. The DTIC does not have some of the data that can assist in evaluating the programme extensively.

Due to lack of data, detailed expenditure analysis could not be conducted. Expenditure data is mainly at a high level on transfers to the respective SEZs without details of what the funds were used for. Similarly, the annual reports from the respective SEZs does not provide the details on how the funds allocated were utilised.

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1 Introduction

Special economic zones (SEZs) are specific geographical areas in a country where certain economic activities are promoted through a set of policy measures not generally applicable to the rest of the country. Using policies and programmes to create favourable conditions for foreign investment, the SEZ programme seeks to overcome obstacles to the development of a competitive, export-oriented and industrialised economy. The programme is identified as a key instrument to drive industrialisation, create employment opportunities and economic growth in South Africa.

The success of SEZs in East Asia, particularly China, led the South African government to pursue the development of such zones as part of its industrial policy. However, evidence presented to show that the SEZs have been successful is not convincing. The current economic crisis and job losses in major industries prompted scrutiny of industrial support instruments in the country, which include the SEZ programme. The SEZ programme was formalised in 2000 as an Industrial Development Zones (IDZ), and 11 SEZs have been designated to date, three of which perform better than the others: Coega, East London and Dube. Since inception, SEZs have cost government an estimated R25.7 billion.

The SEZs have been unable to attract sufficient tenant investors to be financially self-sustainable, and, consequently, rely on government funding to sustain operations and infrastructure. Some of the contributory factors identified include the lingering effects of the 2008 global economic crisis, exchange rate volatility, the small domestic market, long distances to other markets, rising labour costs, negative perceptions of South Africa, and a lack of supporting industries, skills and infrastructure. Other constraints identified by the DTIC include weak governance of the SEZs, inadequate incentives, deficient integrated planning, poor stakeholder coordination and poor marketing strategy. These concerns, along with the changing priorities articulated in the National Development Plan, prompted the DTIC to review and repackage its approach to industrial development in the new Re-imagined Industrial Policy, SEZ Policy and the new SEZ Strategic Framework.

The spending review, therefore, seeks to assess the effectiveness and efficiency of the SEZ programme, which will inform policy choices about the design, and funding of SEZs, to ensure that successes are replicated and shortcomings remedied.

2 Policy and Institutional Information

Policy and Legislation

There is no universally agreed definition of an SEZ. The definition of an SEZ is determined individually by each country. The SEZs are recognised as a special type of economic zone. Economic zones are geographic areas within a country where certain economic activities are promoted by a set of policy measures that are not generally applicable to the rest of the country (DTIC, 2004: vi). These zones are used as a tool to circumvent obstacles that inhibit the development of a competitive export-oriented economy by creating a favourable environment for foreign investment through some form of artificial comparative advantage (i.e. policies and programmes affecting conditions for foreign investment).

Internationally SEZs usually display the following characteristics:

- Geographically delimited area, usually physically secured (fenced-in);
- Single management/administration;
- Eligible for benefits based upon physical location within the zone; and
- Separate customs area (duty-free benefits) and streamlined procedures (World Bank, 2008:9).

SEZs operate in different guises such as export processing zones, free zones, free trading zones and foreign trade zones (Farole, 2011:17). The SEZs are meant to confer two types of benefit. These are:

- Static economic benefits (relatively short term) – as instruments of trade and investment policy. They are expected to contribute to employment creation, the generation of foreign exchange through exports, and the creation of economic value added.
- Dynamic economic benefits (long term) - Structural and developmental benefits that result from establishing the SEZs. These relate to the promotion of non-traditional economic activities, hard and soft technology transfers, facilitation of domestic entrepreneurialism, and the promotion of economic openness. Nationally, the SEZs stimulate the competitiveness of the country or a region (Farole, 2011:26).

In South Africa, these economic zones are referred to as SEZs. Following the review of the IDZ programme in 2007, the new SEZ programme was established through the Special Economic Zones Act (2014). In terms of the Act, the purpose of establishing SEZs include:

- facilitating the creation of an industrial complex, having strategic national economic advantage for targeted investments and industries in the manufacturing sector and tradable services;
- developing infrastructure required to support the development of targeted industrial activities;
- attracting foreign and domestic direct investment;
- providing the location for the establishment of targeted investments;
- enabling the beneficiation of mineral and natural resources;

- taking advantage of existing industrial and technological capacity, promoting integration with local industry and increasing value-added production;
- promoting regional development;
- creating decent work and other economic and social benefits in the region in which it is located, including the broadening of economic participation by promoting small, micro and medium enterprises and co-operatives, and promoting skills and technology transfer; and
- generation of new and innovative economic activities.

According to the DTIC, the SEZ programme is appropriately aligned with the Strategic Integrated Projects (SIPs). The new SEZ strategic framework emphases on aligning SEZ with trade agreements, in particular in the light of the new Africa Continental Free Trade Agreement (AfCFTA) (DTIC, 2019:45).

New developmental objectives of SEZs

The development objectives of zones have changed. The first zones were a product of trade-restricted and/or closed economies and were intended to promote exports, create jobs, and transfer technology. Globalisation and trade liberalisation have changed this. Zones are now viewed as an important mechanism to promote two-way trade and facilitate modernisation of the host economy with a strong emphasis on integrating zones into the domestic economy (DTIC, 2019:6). Key elements of the modern zone offering are:

- Provision of world class-infrastructure;
- Strong capacity of institutions appointed to develop and operate the zones;
- A stronger emphasis on import substitution and export led growth;
- Strong support from the state particularly with respect to the provision of reliable and discounted prices on rentals on land and top infrastructure, competitive tariffs on electricity, water, rail and ports;
- Collaborative and well-coordinated planning among key government agencies and the private sector; and
- A strong suite of tax-based incentives (DTIC, 2019:6).

This is underpinned by long term and collaborative planning that is comprehensive and well coordinated, grounded in diverse regional needs and contexts. Zones today are integrated largely with their host regions. They support and develop local communities, which become the source of labour and skills for the zone firms. This can result in more jobs on offer, a wider variety of skills required and higher earnings, which in turn reduce poverty and inequality. When they import specialised skills, this often results in a skills transfer to the host region. Small and medium enterprises are also integrated into the procurement chains of the zone firms.

Furthermore, SEZs are increasingly used to stimulate regional development, and can be the basis of modern urban development. Shenzhen in China was a fishing village and is now a modern city with 14 million people with a per capita GDP growth of 100 times since its designation in 1989. Today's SEZs combine residential and multiuse commercial and industrial activity (DTIC, 2019:6).

Programme benefits

The SEZs programme encompasses different benefits, which include ease of doing business and simplified access to resources. A few such benefits include:

- employment incentives that are mandated by Employment Tax Incentive Act, 2013 (Act No. 26 of 2013),
- the preferential 15 per cent Corporate Tax as mandated by Income Tax Act, 1962 (Act No. 58 of 1962.) together with section 24(4) of the SEZ Act. It is worth noting that the incentive has not been implemented yet,
- the building allowance as per Section 1 of the SEZ Act,
- the customs controlled area given right by the Customs and Excise Act, 1964 (Act No. 91 of 1964), the Customs Duty Act 2014 (Act No. 30 of 2014) and the Customs Control Act, 2014 (Act No.31 of 2014), and
- the 12I Tax Allowance benefit. However, it should be noted that this incentive is not limited to investors located in SEZs.

3 Programme Chain of Delivery

Programme elements

The SEZ Act (16 of 2014) guides the delivery of the SEZ programme. It identifies the different stakeholders and the roles they play. These include, the Minister of Trade and Industry, the Special Economic Zones Advisory Board (including its various committees and secretariat), Minister of Finance, SEZ applicants (this has been mostly provincial departments), SEZ entity, SEZ Board, and SEZ operators.

Although most programme elements are generic to all SEZs, there are some differences between the SEZs arising from their respective mandates and locations, the industries that they target, and the services that they provide. It is notable that all spheres of government are involved in the SEZ programme value chain. For this reason, it is important to demarcate the elements or outputs of these various stakeholders, namely, the national department, the provincial government, the local government, the operating entities and the South African Revenue Services (SARS).

National department

In South Africa, the DTIC, through Minister of Trade and Industry, is the custodian of the SEZ programme, which is part of its industrial development mandate. Responsibilities for Minister of Trade and Industry with respect to the SEZ programme are outlined in the SEZ Act. The department is responsible for formulating and drafting the SEZ policy and strategies. It has a dedicated unit that is responsible for all matters pertaining to SEZs, including, policy development, oversight, designation, monitoring and evaluation, supervising the national zone system and SEZs, approve investment, and report progress at national level. The unit resides within Sub-programme: Regional Industrial Development within Programme 3: Spatial Industrial Development and Economic Transformation.

Other units within the DTIC contribute directly or indirectly to the outcomes and outputs of the SEZ. Specifically, they provide services such as incentive schemes to companies investing in the SEZ as well as export promotion assistance and investment marketing services, which are not exclusive to the SEZ firms. These activities reside within Programme 6: Industrial Financing and Programme 7: Export Development, Promotion and Outward Investments.

An important function of the DTIC is to facilitate the designation of the SEZs. The prospective SEZ (applicant - e.g. province) registers an “intent‟ with the DTIC to establish an SEZ. A concept note is drafted and forwarded to the Minister of Trade and Industry. The Regional Industrial Development (RID) section within DTIC evaluates the concept note to determine if the potential SEZ is, among others, aligned with government polices namely the National Industrial Policy Framework (NIPF), Industrial Policy Action Plan (IPAP), now the Re-Imagined Industrial Strategy and liaises with the other stakeholders such as municipalities. If the DTIC is satisfied, the applicant goes ahead to conduct a business case and a subsequent feasibility study.

Once the business case is completed and submitted to the DTIC, the SEZ unit undertakes a due diligence evaluation on the viability of the SEZ. If it supports the proposal, it then makes a recommendation to the SEZ Advisory Board, which in turn recommends to the Minister of

Trade and Industry to designate an area as an SEZ. Another key component prior to issuing a permit is obtaining Cabinet approval to designate the SEZ. A permit is therefore only issued after Cabinet has approved the designation of the SEZ.

Another key role player at national government level is the National Treasury. In terms of the SEZ Act, the Minister of Trade and Industry should seek concurrence of the Minister of Finance before the designating an SEZ. The Minister of Finance, supported by units in the National Treasury (which include Public Finance, Economic Policy, Tax Policy, Intergovernmental Relations and Budget Office-Public Entities Governance Unit) evaluate the application to ascertain financial and tax implications. Minister of Finance either concurs or disagree with designation of proposed SEZ, provide reasons and propose suggestions to the Minister of Trade and Industry and Cabinet.

The National Treasury also plays a role in allocating funding for the SEZ through the Budget Process. The National Treasury through Tax Policy Unit also facilitates the gazetting of SEZs that can benefit from tax incentives. The Public Entities Governance Unit deals with scheduling of SEZ entities/operators. Intergovernmental Relations works closely with and assesses budgets for provincial departments who are the owners of most of the SEZs.

Provincial government

Provincial governments are the applicants/owners of individual SEZs and provide funding for SEZs' operations. The SEZs are usually located within the economic development department of the province and serve as an instrument to realise provincial economic objectives. These relate to developing infrastructure, promoting economic development and stimulating job creation. The revised SEZ strategic framework (DTIC 2019) provides for equal ownership of an SEZ by the different spheres of government, for example the Tshwane Automotive Special Economic Zones is equally owned by the Gauteng Department of Economic Development, Tshwane Metropolitan Municipality and the DTIC.

Local government

The municipalities provide a host of vital services that are necessary for the optimal operation of the SEZs. Firstly, in some cases, the municipalities donate land for the establishment of the SEZ or offer it at discounted municipal rates. Secondly, municipalities provide adequate and appropriate utility services such as water and electricity, which are sometimes also granted at lower rates. These preferential rates are negotiated on a case-by-case basis. The SEZ Act and strategy do not prescribe special rates for firms located within the zone as they are negotiated from municipality to municipality. Thirdly, municipalities are responsible for the construction, maintenance and upgrading of access roads to the SEZ. Fourthly municipalities provide specialist waste services.

South African Revenue Services

The SEZs are expected to provide a Custom Controlled Area (CCA), which in turn offers firms in these zones:

- relief from customs duties for equipment (e.g. machinery) imported into a CCA;
- simplified customs procedures (e.g. release of cargo);

- no import duties are payable on goods imported for use in the construction and maintenance of the infrastructure of a CCA; and
- an exemption from Value-Added Tax on the importation of goods to be used in exporting.

However, to date, no fully-fledged CCAs have been established within an SEZ. Presently, factories within an SEZ apply and register with SARS and the factory is subsequently designated a CCA. This procedure is no different to that which is already available to firms outside the SEZs.

SEZ Operating entities

The operating entities are the institutions that run the SEZ. Functions of the operating entities are multiple and can be summarised as follows:

- development and operation of an SEZ, including the provision and maintenance of all infrastructure, utilities, buildings, warehouses, factory shells and other facilities and improvements necessary for its operation;
- assisting investors with regards to registration, business permits and licences, environmental permits, accessing incentives, custom clearances processes, tax matters and government liaisons;
- marketing and brand development; and
- provision of specialised products and services such as training or incubation facilities.

SEZ Advisory Board

The role of the Advisory Board is critical and its functions are outlined in the SEZ act as to:

- advise the Minister on policy and strategy in order to promote, develop, operate and manage SEZs;
- monitor the implementation SEZs policy and strategy and report to the Minister of Trade and Industry on an annual basis on the implementation of such policy and strategy; consider an application for designation as an SEZ and recommend to the Minister of Trade and Industry whether or not to approve the application and grant an SEZ licence to the applicant; consider an application for an operator permit and recommend to the Minister of Trade and Industry whether or not to approve the application;
- consider an application for the transfer of an operator permit and recommend to the Minister whether or not to approve such application with or without any condition;
- liaise with a SEZ Board and an operator on the implementation of the SEZ strategic plans;
- report in the prescribed manner to the Minister of Trade and Industry on progress relating to the development of SEZs; advise the Minister on minimum norms and standards required for the provision of a one stop shop in an SEZ;
- advise the Minister on initiatives to market SEZs; and
- assess and review the success of SEZs in achieving the purpose.

The Advisory Board also conducts investigations on any matter arising out of the application of the SEZ Act and performs such other functions consistent with the objectives of the Act as determined by the Minister of Trade and Industry. The SEZ Advisory Board plays a critical role on the SEZ policy.

SEZ Board

The Special Economic Zone Board is the accounting authority of an SEZ and it plays oversight on the management of the individual SEZ entities. SEZs are listed in the Public Finance Management Act (PFMA) and they are business entities that are governed by Companies Act. Therefore, the SEZ Board is also expected to perform its oversight in line with provision of the Companies Act. In practice, the SEZ operators rely on funding from the fiscus and therefore, the reality is inconsistent with the Public Finance Management Act, which required the operators as business enterprises, to fund themselves from own generated revenue.

Funding Arrangements

The DTIC houses an SEZ Fund, which only provides for bulk infrastructure and top structures for the SEZ programme. In some cases, funds may also be used for feasibility studies for projects to be initiated within the zone. On the other hand, provincial government departments provide funding for operations to augment revenue collected from tenant firms located in the SEZ. Provincial governments also fund capital expenditure. In most cases, municipalities provide land parcels at discounted rates. In addition to this funding, investors may also apply for incentives that are provided by the DTIC.

SEZ Funding process

Through the budget process, the DTIC is allocated money for the SEZ under Programme 6: Industrial Finance. The money is not allocated per specific SEZ. Rather, each SEZ submits applications to the DTIC based on the investor space requirements it has. The application process is on a first come, first served basis.

The DTIC receives applications to fund bulk infrastructure from SEZs. Applications are reviewed by the technical committee in line with set guidelines and criteria, which then makes recommendations to the adjudication committee for approval. Once approved based on the set criteria, a funding agreement is drafted. The SEZ is then required to open a bank account dedicated for the approved project. Thereafter funds will be disbursed based on agreed milestones.

Requirements for an application for monies from the Special Economic Zones Fund

From time to time, the Minister of Trade and Industry sets the procedure to be followed when applying for monies from the Fund in terms of Regulations made in terms of section 41 of the SEZ Act published in Government Gazette 39667 published on 9 February 2016. The following steps are followed when applying for SEZ funding:

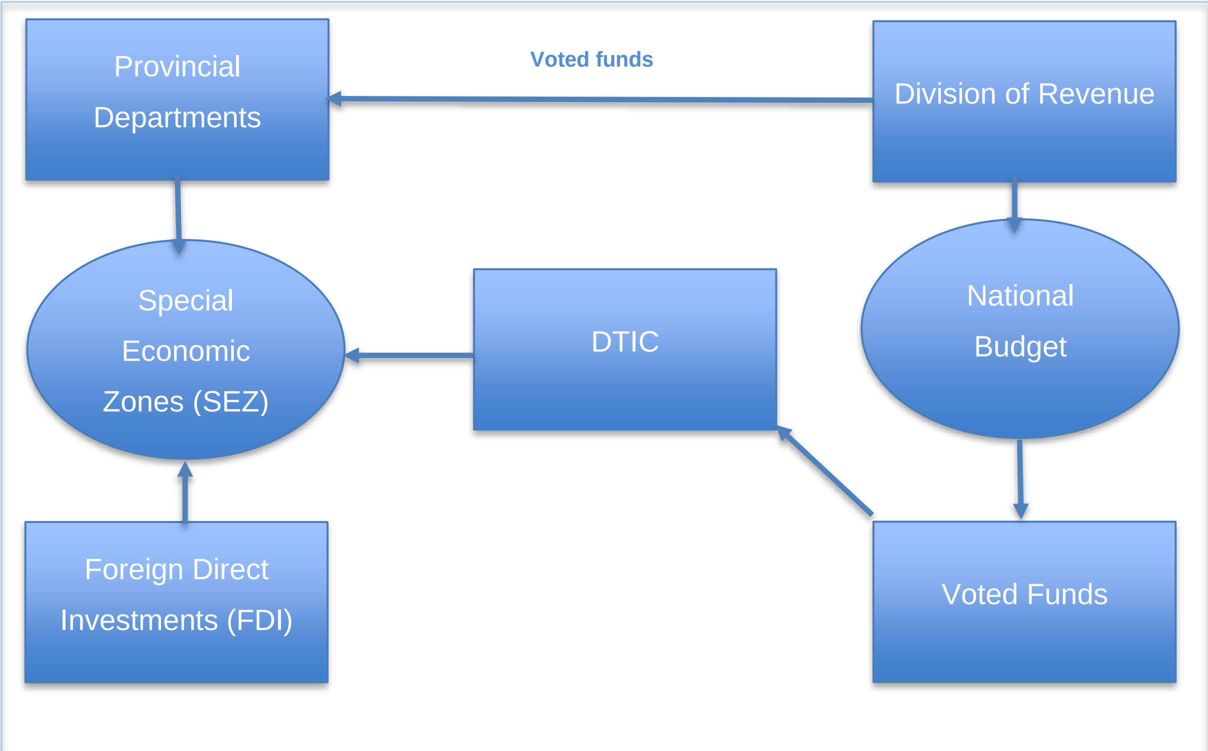
Step 1: An applicant must submit the application, which includes a project motivation, a detailed business plan, and budget for the project; and a feasibility study, unless the application is for funding for a feasibility study.

Step 2: The Adjudication Committee evaluates applications.

Step 3: The Adjudication Committee submits a recommendation to the Minister of Trade and Industry on whether or not to approve the application for funds.

Step 4: The Minister, after considering the recommendation of the Adjudication Committee, may approve or reject the application, with conditions; and must inform the applicant in writing of the decision.

Figure 1: SEZ funding process



Source: National Treasury

Designation Process

National government, a provincial government, a municipality, and a public entity a municipal entity or a public-private partnership may apply to the Minister of Trade and Industry for a specified area to be designated as an SEZ. An application for designation must be in writing and must comply with the requirements in section 23(2) and section 23(3) of the Act. In addition, the applicant must indicate:

- the manufacturing activity or internationally tradable service that the SEZ intends to engage in;
- whether the SEZ intends to target a local or export market; and
- where the SEZ intends to be located in the Republic of South Africa.

Steps followed for designation of SEZ:

- Step 1: An applicant must submit an application addressed to the Chairperson of the Advisory Board;

- Step 2: The Advisory Board must consider the application and recommend to the Minister of Trade and Industry whether or not an area must be designated as a SEZ within five months of receiving the complete application;
- Step 3: The Minister must, within two months of receiving the recommendation of the Advisory Board, decide whether or not to designate an area as an SEZ;
- Step 4: If the Minister decides not to grant the application to designate a specified area as an SEZ, the Minister must:
    - inform the applicant of the decision in writing; and
    - provide the applicant with reasons for the decision.
- Step 5: An unsuccessful applicant may submit a new application for a specified area to be designated as a Special Economic Zone, as provided for in the Act.

Figure 2: below summarizes the designation process.

Figure 2 SEZ Designation Process mapping

Chapter 5 of the SEZ Act outlines the SEZ designation process. Section 23(6) of the SEZ Act states that the Minister of Trade and Industry may, by notice in the Gazette, designate an area as an SEZ after considering the recommendation of the SEZ Advisory Board and after consultation with the Minister of Finance.

Similarly, section 24(4), the Minister of Trade and Industry may prescribe the type of service and business that may be located in an SEZ after consultation with the Minister of Finance. Prior to designation, the Minister of Trade and Industry is required to publish his/her intention to designate an area as an SEZ in the Gazette for public comments.

The team was not been able to obtain data on whether and under what circumstances applications for the designation of SEZs have been rejected.

Observations and conclusion: designation process

While the concurrence of the Minister of Finance has always been sought prior to designation of SEZs, National Treasury raised concern with the DTIC that public comments were sought prior to obtaining the concurrence of the Minister of Finance. DTIC argued that public comments could be concurrently sought while awaiting the concurrence of the Minister of Finance to avoid delays in the designation, which may result in loss of potential investors.

National Treasury argued that concurrence with the Minister of Finance should take place prior to seeking public comments to avoid a situation where the Minister of Finance raises fundamental issues that may affect designation process. If this happens, management of public expectation would be an issue as there would be perception of policy uncertainty.

In the previous applications to designate Nkomazi and Bojanala SEZs, Minister of Finance did not concur due to unclear financial implications and lack of commitment on funding availability. The Minister also raised concern on lack of a strong pipeline of investment.

The chain of delivery

The programme generates various outputs, which collectively contribute to government's main outcomes and subsequently impact on society. These outputs are derived via various activities, which require specific inputs. The link between the outputs and the outcomes and impact of the SEZ programme is shown in the table below.

Table 1: Logical framework model

<table>
<tr><th colspan="9">IMPACT</th></tr>
<tr><td>Impact statement</td><td colspan="8">Accelerated sustainable growth and poverty reduction</td></tr>
<tr><th colspan="9">OUTCOMES</th></tr>
<tr><td>Long term (> than 5 years)</td><td colspan="8">Economic transformation and job creation (Priority 2 of the 2019-2024 MTSF)</td></tr>
<tr><td>Medium term (3 - 5 years)</td><td colspan="2">Increased investment</td><td colspan="3">Increased value added exports</td><td colspan="3">Efficient, competitive and responsive special economic zones</td></tr>
<tr><th colspan="9">OUTPUTS</th></tr>
<tr><td colspan="9">National Government - DTIC</td></tr>
<tr><td colspan="2">SEZ Governing policy and legislation</td><td colspan="2">Designation of SEZ</td><td>Regulatory compliance and Monitoring & Evaluation</td><td colspan="2">Investment marketing services</td><td colspan="2">Export promotion schemes and assistance</td></tr>
<tr><td colspan="3">Provincial Government</td><td colspan="4">Local Government</td><td colspan="2">SARS</td></tr>
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<tr><td colspan="9">Operating Entities</td></tr>
<tr><td colspan="2">SEZ capital and operational plans</td><td>General economic Infrastructure</td><td>Specialist infrastructure and technology</td><td>Shared infrastructure</td><td>Investment marketing services</td><td>Export promotion facilitation</td><td>Compliance support and aftercare</td><td>Incubation programme</td></tr>
</table>

Impact

The SEZ programme is expected to contribute to an accelerated sustainable growth and poverty reduction, which is one of government's main strategic objectives.

Outcomes

The impact of the SEZ programme is dependent on both long term and medium term outcomes as denoted in Table 1 above. Specifically, the SEZ programme is aligned with Priority 2: Economic transformation and job creation of the 2019-2024 Medium Term Strategic Framework. These long-term outcomes are manifested through the realisation of the intermediate outcomes, namely, increased investment, increased value added export and efficient, competitive and responsive industrial zones.

Outputs, activities and inputs

In terms of the logical framework model, the outputs are generated by the various programme elements or stakeholders.

4 Performance Analysis

Monitoring and Evaluation methodology

The DTIC developed a Performance Monitoring and Evaluation Framework for the SEZ programme. The Framework details the manner in which SEZ monitoring and evaluation should be conducted; and how data will be collected, managed and disseminated. It also seeks to: clarify definitions and standards for performance information in support of regular audits of such information. It aims to improve integrated structures, systems and processes required to manage performance information; define roles and responsibilities for managing performance information; and promote accountability and transparency by providing the SEZ Advisory Board, Parliament and other relevant stakeholders with timely, accessible and accurate performance information.

Institutional arrangements

The effective management of performance information requires a clear understanding of the different responsibilities and structures involved in managing performance. The SEZ Advisory Board, through the Minister of Trade and Industry, is charged with the responsibility of providing oversight on the development and implementation of the SEZ programme and therefore has a duty to ensure that appropriate systems to collect, collate, verify and store performance information are in place in all SEZs. These systems must be integrated with the national SEZ performance monitoring and evaluation system. Annual reports on the SEZ programme are not produced consistently and performance information seem to be fragmented.

Data collection mechanisms

Methods used for data collection play an important role in the credibility of information. Quality data monitoring will lead to quality evaluation, and consistency is paramount in the supply of information from identified sources. The Framework acknowledges that a concerted effort should be made to build good relationships with all identified institutions to supply data. DTIC through the SEZ policy unit facilitates a CEOs' forum were reports on performance of SEZ are presented on quarterly basis. The shortcomings on the forum is that information is presented at a high level and in a fragmented manner, which inhibits quality monitoring.

Upon publishing the framework, following initiatives and processes were noted:

- at present, national centralized data system does not exist. The DTIC is in the process of developing an SEZ data collection system based on information technology (IT). This system will be linked with all SEZ data management systems. This integration of data systems will ensure the standardisation of data collected from all operational SEZs.
- The DTIC has signed a memorandum of understanding with StatsSA for SEZ data collection. The relationship is intended to ensure that SEZ performance data is of acceptable quality and is compliant with the guidelines of the national statistics system and prescripts of the South African Statistical Quality Assessment Framework. The relationship between to DTIC and StatsSA exists, however StatsSA has published only

two reports with performance information of SEZ (one in 2015 and other in 2018). The 2018 report only has information for Coega SEZ. This suggests that the relationship with StatsSA has not worked well.

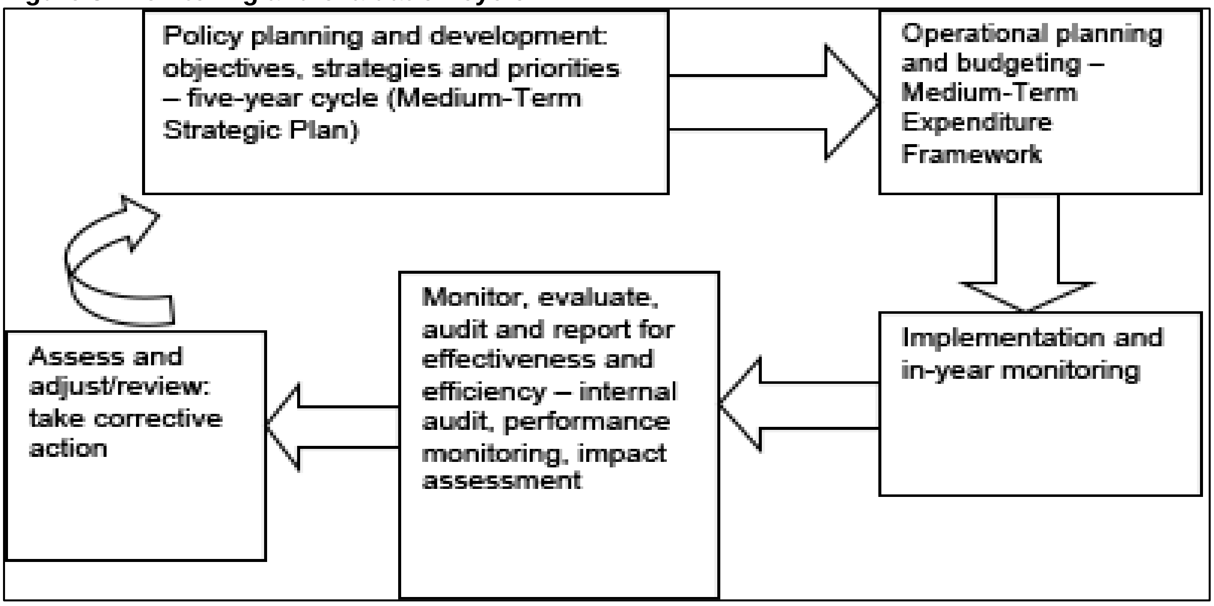
- SEZ operators are establishing a data management function with a direct link to the DTIC's SEZ monitoring and evaluation function. This function will be responsible for collecting, populating, and managing data in the respective SEZs. Each SEZ use their own financial and accounting systems. No direct link DTIC monitoring and evaluation function currently exists.

Key performance information concepts and KPIs

To clearly demonstrate effectiveness of SEZ programme in delivering on its mandate, performance information has been structured as demonstrated below. However, this is yet to materialise.

Monitoring and evaluation cycle: Linking policy, planning, budgeting and management

Figure 3: Monitoring and evaluation cycle



Organisational indicators

In terms of SEZ high-level management indicators, the SEZ Act creates four distinct structures, namely, the licensee, the SEZ entity with its board, the SEZ operator, and businesses located in SEZs. Each structure has its own roles and functions, and the SEZ Act provides a framework to ensure that the structures perform their functions and fulfil the SEZ Act's objectives. Each structure is required to be appropriately skilled to perform the functions provided for in the Act. Thus, government, by means of the Act, policy and strategy provides a strategic direction and intent for the SEZ programme. The licensee, the SEZ entity with its board, and the SEZ operator are responsible for operationalising the strategic objectives of the programme. Government, therefore, would measure the organisational efficiency of an SEZ through its contribution to the attainment of the overall programme's strategic intent.

Chapter 27 and the regulations emerging from SEZ Act require operators to supply the DTIC with the following information:

Table 2: SEZ Performance Management Indicators

Performance indicator	Description	Frequency
Business and financial Plan	Submit business and financial plan two months before the end of the financial year: - Projection of revenue - Projection of expenditure - Cover the affairs of SEZ entity for the following two financial years	Annually
Financial statements	Submit financial statements within three months after the end of the financial year to the Auditor-General	Annually
Annual report	Submit within five months of the end of the financial year to the Minister of Trade and Industry: - Annual report - Audited financial statements - Auditor-General's report on financial statements	Annually
Implementation of one-stop shop model	Submit progress report on the implementation of one-stop shop model	Biannually
Incubation programme/supplier development programme	Submit progress report on incubation programme/ supplier development programme support	Annually
Performance progress report	Submit performance report in line with the agreed-upon KPIs	Quarterly
Infrastructure progress report	Submit progress report in line with Section 3.5.2 on the implementation of the infrastructure projects supported by government	Monthly

While the process is properly outlined, operationalisation has been very slow and fragmented with the SEZs not reporting consistent information. The DTIC could not readily provide the information that the National Treasury requested even though some of the information should be collected regularly in terms of the outline above or based on the SEZ Fund Guidelines. The DTIC, the SEZ Advisory Board and the provinces should ensure that an efficient reporting system is implemented urgently.

Observations and conclusion: monitoring and evaluation methodology

Although the Monitoring and Evaluation Framework sets the right tone for proper monitoring and evaluation of the SEZ programme, effectiveness of the framework is questionable. For example, the national SEZ performance monitoring and evaluation system does not exist. Furthermore, the DTIC does not have system that test efficiency and accuracy of performance information submitted by SEZ operators. The zones have also not been reporting consistently and uniform performance indicators. It is critical to note that there is nothing in the framework that sets standards for the reporting of non-financial performance of the SEZs.

Performance of South African SEZs

To date, 11[2] SEZs have been designated and there is a pipeline of a further six. According to the progress report on implementation of SEZ in South Africa submitted to Cabinet in October 2019, the promulgation of the Special Economic Zones Act in 2016 brought many changes in the industrial development drive in South Africa. The new SEZ programme strengthened the value proposition and investment appetite. Before the introduction of the SEZ Act, the six designated IDZs had a total of 42 investors that were operational. The total value of the investments was R3 billion, with 5 169 jobs created. According to the DTIC, with the introduction of the SEZ Act and implementation of the SEZ Programme, the number of investors grew to 127 operational investors. There were 90 secured but non-operational investors). Private investment value of over R17.2 billion was leveraged from operational investors, creating 16 301 direct jobs. Similarly, secured but not operational investment was projected to create 8 563 jobs as demonstrated in the table below.

Table 3: Investment in Special Economic Zones – 2019/20FY (Q1)

SEZ Name	Year established	Operational Investors			Secured but not operational investors		
		Number	Value (R billion)	Total Direct Employment Created	Number	Value (R billion)	Expected number of jobs
Coega SEZ	2001	45	11.2	7 815	28	17.8	936
East London SEZ	2002	32	3.1	4 158	16	5.0	3 097
Richards Bay SEZ	2002	2	0.3	111	7	3.3	1 174
Gauteng IDZ/OR Tambo SEZ	2002	1	0.3	600	12	0.30	246
Saldanha Bay SEZ	2013	0			11	3.3	398
Maluti-A-Phofung	2014	1	0.3	126	5	0.7	360
Dube Tradeport SEZ	2014	42	1.3	3 167	9	3.2	2 342
Musina Makhado SEZ	2017						
Atlantis SEZ	2018	4	0.7	324	2	0.02	10
Nkomazi SEZ	2019						
Total		**127**	**17.2**	**16 301**	**90**	**33.7**	**8 563**

Source: DTIC report

National Treasury attempt to get reports from SEZ operators and firms to affirm the above performance numbers was not successful. However, key questions remain unanswered, how does the DTIC and firms count "direct jobs", what evidence do they have for the number of jobs reported, the nature of jobs reported (i.e. is it full-time or temporary/contract jobs), and it is also not clear how often jobs get counted (i.e. on a specific date in the year). Without such

[2] This figure includes Tshwane Automotive SEZ. However, the DTIC designated it as part of the ORT SEZ

critical details, it is highly likely that the DTIC is taking investors' word, as it is when it comes to report on number of jobs.

Operational SEZs

- ***Coega***

Coega was established in 1999 in the Eastern Cape. It was launched as an Industrial Development Zone (IDZ) in 2001, and was designated as an SEZ in 2017. It is the oldest spatial development zone in South Africa and the largest. The total number of investors attracted by the zone is 73 (45 operational and 28 secured but not yet operational), with a total investment value of R29.1 billion (R11.2 billion operational & R17.8 billion secured but non-operational) and employment creation of 7 815 jobs.

Coega has four investments under construction, which represents a total private sector investment of R11.2 billion. Recent investments include Beijing Automotive Industry Corporation (BAIC) SA (R11 billion in all phases and approximately R3.5 billion in the current phase), OSHO Cement (R600 million), Akacia Medical (R100 million) and HELLA (R50 million). The SEZ has estimated a 1 350 per cent growth in investment (R115 billion) by 2030, as well as a concomitant increase in job creation of 230 percent (18,000 new jobs). To put this into perspective, it is 10 times the erstwhile General Motors assembly plant.

- ***Dube Tradeport***

Dube SEZ is in KwaZulu Natal (KZN) in the same zone as King Shaka International Airport, and was designated in 2016. To date, Dube has attracted 51 investors (42 operational and 9 secured but not yet operational) with a value of R1,3 billion and 3 167 direct jobs created.

From an industrial perspective, Dube focuses on aviation (and related logistics), electronics, medical and pharmaceutical, clothing and textiles and automotive manufacturing and services. Approximately 18 per cent of available land has been taken up and there is a pipeline of 34 investors to an estimated value of R8 billion. An additional recently signed investment is MaraPhone15, a R1.3 billion investment which is estimated will employ 1 500 people by 2025.

- ***East London***

East London IDZ (ELIDZ) was established in 2002 as an IDZ. Since then, approximately 25 per cent of available land has been taken up. The SEZ has 48 investors (32 operational and 16 secured but not yet operational), with a total investment value of over R3.1 billion (and R5 billion secured but non-operational). To date, 4 158 jobs were created.

Recent growth in the ELIDZ has been enabled by significant investment into infrastructure by the DTIC. Four investments, valued at R680 million, are currently under construction. East London SEZ estimates that it will have grown investment by 214 percent (to R14.9 billion) by 2030, but with limited growth in operational jobs over the same period.

- ***Richards Bay***

The Richards Bay IDZ (RBIDZ) was designated in 2002, and is focused on the metals beneficiation, energy, agro-processing, marine and ICT/technopark sectors. The zone only has two operational investors to-date (one of which was at the location before the IDZ was declared), valued at R320 million, which created 111 direct jobs. An additional 17 investments were signed by mid-2019, which are at different stages of development. Ultimately, these are expected to deliver over 1 000 additional jobs, and new investment of approximately R3 billion. Richards Bay IDZ estimates an increase of over 4 000 per cent by 2030 in investment value (to R14 billion) and an increase in jobs of approximately 2 200 percent from the current 111 jobs to 2 118 jobs over the period.

- ***Atlantis***

The Atlantis SEZ was officially launched on 6th December 2018, and is the first SEZ to focus predominantly on green and renewable technologies. From 2014 to 2018 when it was finally designated, it has created 324 operational jobs, and has attracted R700 million from six private sector investments. The SEZ has estimated a growth in investment of approximately 2 000 per cent (to R14 billion) by 2030, and a 2 700 per cent growth in jobs (to 9 000) over the same period. However, some delays within the Western Cape Province have meant barriers to further development, including land release and the setting up of the SEZ entity. This is currently being addressed.

- ***Maluti- a Phofung (MAP)***

Maluti-a- Phofung was designated in 2016. The primary focus and value of the SEZ is to function as a logistics centre that will take advantage of its geographical location on the Gauteng – Durban corridor, and as a link to the Bloemfontein-Cape Town Corridor. The SEZ focuses on logistics, but also agro-processing, and has indicated it will also target pharmaceuticals and electronics. Negotiations are currently under way to set up a beverage processing plant in the SEZ.

The zone has signed six new lease agreements with agro-processing and chemical companies valued at R996 million. One of these investments, valued at R250 million, is currently operating in a temporary structure. However, there have been barriers and challenges arising from lack of clarity pertaining to roles and responsibilities between the operator and the SEZ entity, which have hampered growth activities for the SEZ. Once these have been resolved, the SEZ estimates it will double revenues by 2030 to at least R485 million, and will increase jobs to 548 operational jobs.

- ***Musina-Makhado***

The Musina-Makhado SEZ is a new development and was designated in 2017. Its establishment is driven by the South African Energy and Metallurgical Special Economic Zone (EMSEZ) bilateral agreement between China and South Africa. The SEZ anticipates investment of approximately R150 billion and 21 000 jobs by 2030. However, Environmental Impact Assessment (EIA), Bulk Infrastructure and Township Establishment issues remain to be addressed. The has been slow progress to operationalise the SEZ.

- ***Nkomazi***

The Nkomazi SEZ is a new development situated in Mpumalanga. The focus is food, and agro-processing for export, while adding value within the SEZ. The SEZ is not operational yet, but plans to create 9 000 operational jobs by 2030 and in early 2019, Letters of Intent (LOI) amounted to a value of approximately R14 billion.

However, Nkomazi is experiencing difficulties in implementation of the zone. There have been changes in administration in the province including the suspension of the CEO of Mpumalanga Growth Agency (MEGA), who was the project driver; the resignation of the board members of MEGA; and the appointment of a new MEC after the 2019 national elections. The provincial Department of Economic Development, Environment and Tourism (DEDET) does not have a full time Head of Department/ Accounting Officer. These changes have resulted in a new administration unfamiliar with the project and new working relationships between the DTIC and the province are in the process of being rebuilt, so that work can progress on the implementation of the zone.

- ***Gauteng /OR Tambo (ORT) IDZ***

The OR Tambo International Airport SEZ is being developed within and in proximity to the property boundaries of the OR Tambo International Airport. The first investor in the zone, In2Food Group, was launched in 2019, with an investment value of R257 million and 600 direct jobs created. A major development is the expansion of the SEZ to incorporate the Tshwane Auto Hub. The slow progress in this SEZ is also a concern.

- ***Saldanha Bay***

Saldanha Bay is South Africa’s first SEZ to include a commercial, operational port and is the first SEZ focused on the Oil and Gas Industry and Marine Repair and Fabrication sectors. The SEZ has a pipeline of 52 investors – eleven of which have signed lease agreements- at an investment value of R3.26 billion. The SEZ estimates it will grow investment to R23,2 billion by 2030, an increase of just under 500 percent, and will increase jobs to 1 200, an increase of approximately 300 percent.

Proposed SEZs

Table 4: Proposed SEZs (2019)

SEZ	Province	Focus/Targets	Current Status
Bojanala (Mogwase)	North West	PGM beneficiation and mining input supplier park; agro processing, renewable energy	Investor pipeline needs strengthening
Bronkhorstspruit	Gauteng	High technology and Science commercialization	Full business case and feasibility begins July 2019
Tubatse	Limpopo	Mineral beneficiation (PGMs/Chrome) Mining inputs supply; energy, general manufacturing	Business plan in development for license application
Upington/Namakwa	Northern Cape	Solar and renewable energy manufacturing; aeronautics (maintenance, repair & overhaul, MRO)	Phase one business plan for MRO submitted; business plan and strategy for solar and renewable energy submitted
Wild Coast (Mthatha)	Eastern Cape	Agro-processing and tourism hub	Feasibility and business plan complete

Observations and conclusion: performance of South African SEZs

Scope for measuring performance of SEZ mainly focuses on number of operational investors, jobs created and value of investment leveraged. This appears to be a narrow scope. Rather, the programme has to be assessed in line with the objects of the SEZ Act. Scholars have argued that jobs should not be used to assess performance of SEZs. Instead, focus should be on the increase in value added exports from SEZs. This is in line with the objectives of the SEZ Act as well as the SEZ Fund Guidelines. To date, it seems there is no meaningful tracking of exports from SEZs. It is difficult to determine if the SEZ programme has resulted in increased exports. This should be a good time to note that even the measurement of jobs is not standardised and the number of jobs reported should be treated cautiously whether they actually exist and whether they might have existed even in the absence of a SEZ.

In general, SEZ performance reporting has been problematic. Zones are not reporting consistent information. Reports are not standardised. As a result, it is difficult to track certain variables.

However, using narrow scope of performance measures, only three SEZs --~~,~~ Coega, East London and Dube Tradeport -- have attracted a sizable number of investors. The number of jobs and value of investment leveraged remains low. While the DTIC often argues that the number of jobs and investment could not have been realised without the SEZ programme, an argument is also advanced on the extent to which investment took place because of this programme. This is especially in the context of concern expressed by many zones that government has not delivered on the promised SEZ incentives, which includes the 15 per cent corporate income tax. It should however, be noted that, firms in SEZs receive other benefits through lower rent even though this is not the main attraction in the SEZ value chain. This, in turn, has implications for the sustainably of the SEZs themselves, which ought to fund themselves through rental income.

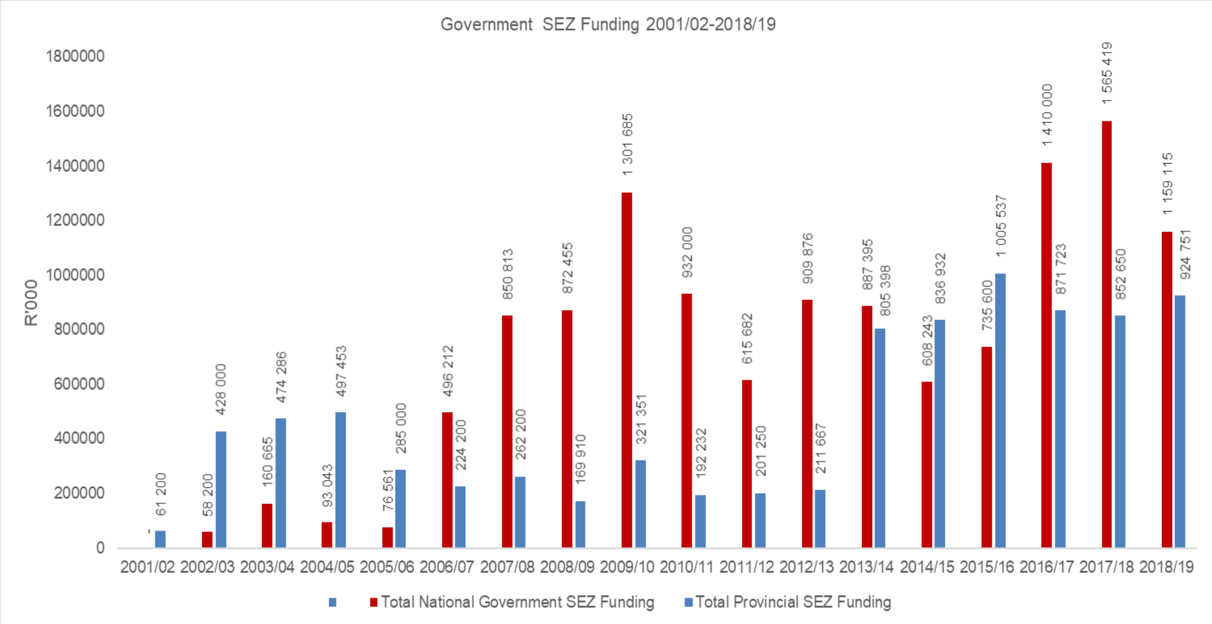
There is a need to expand the scope of what is measured to track progress and contribution of the SEZ programme to the country and to determine if the objectives of the SEZ Act are being attained. The DTIC, the SEZ Advisory Board and the SEZ licence holders must urgently implement the performance monitoring and evaluation framework.

5 Expenditure Observations

Government expenditure towards the SEZ programme

Total government expenditure towards the SEZ programme since inception to 2018/19 is estimated to be R25.7 billion. Annual spending was highest in 2017/18 at R2.4 billion as shown on the figure below. Total spending is distributed between national and provincial government as reflected on Figure 4 below.

Figure 4: government expenditure towards the SEZ programme



Source: National Treasury

From 2001/02 to 2005/06, provincial funding exceeded national government funding portion. Thereafter, national government funding provided most of the funding except in 2014/15, and 2015/16. The level of provincial government funding towards the SEZ programme increased substantially from 2013/14.

Observations and conclusion: expenditure observations

Through the SEZ Fund, national government contributes the largest proportion of SEZ funding. However, funding mainly provides for infrastructure (top structures and bulk works). In some circumstances, funds are also used to fund feasibility studies for projects in the SEZ or setting up of new SEZs.

The contribution of local government on the SEZ programme remains obscured. While it is known that municipalities are key stakeholders, their contribution is not well documented and is often not properly accounted for. As a result, total government funding towards the SEZ may not be accurately reported. Therefore, there is a need for a transparent system to record funding towards the programme. This can be incorporated into the online reporting system.

Financial self-sustainability of SEZs entities

In terms of the draft new SEZ strategy, SEZ operators are expected to be financially self-sustainable. They are expected to finance their operations from revenue collected from rentals, and any other revenue generated from operations. After designation and establishment of the SEZ operating entity, the DTIC provides start-up funding to the new operating entity. Funds are allocated and distributed through transfer line item: Industrial Development Zone – other which used to be under Programme 6: Industrial Financing. From 2021/22, this line will be under Programme 3: Spatial Development and Economic Transformation. It is important to note that this is once-off funding.

It is quite evident from table 5 below that no entity is able to sustain its operation without the government grant. All SEZ entities are loss-making entities and the trend has been sustained since inception. It is critical to note that expenditure numbers include capital expenditure.

Table 5: illustrate financial sustainability of the SEZ operators over the period of ten years.

Table 5: Financial performance of SEZ selected operators

	R'000	2010/2011	2011/2012	2012/2013	2013/2014	2014/2015	2015/2016	2016/2017	2017/18	2018/19
COEGA	**REVENUE**	**773 731**	**579 354**	**706 120**	**842 061**	**635 971**	**995 192**	**783 653**	800 213	795 275
	Total own revenue	137 812	233 459	314 488	490 485	509 041	539 848	565 034	588 296	602 485
	Government funding	635 919	345 895	391 632	351 576	126 930	455 344	218 619	211 917	192 790
	EXPENDITURE	**400 159**	**395 005**	**530 956**	**582 737**	**535 749**	**671 368**	**593 776**	**742 093**	**567 898**
	Profit or (Loss)	373 572	184 349	175 164	259 324	100 222	323 824	189 877	58 120	227 377
	Profit or loss margin as % of total revenue	48%	32%	25%	31%	16%	33%	24%	7%	29%
	Profit or loss based on own revenue	(262 347)	(161 546)	(216 468)	(92 252)	(26 708)	(131 520)	(28 742)	(153 797)	34 587
	Profit or loss as % of own revenue	-190%	-69%	-69%	-19%	-5%	-24%	-5%	-26%	6%
Eeast London IDZ	**REVENUE**	-	-	**39 589**	**196 267**	**251 247**	**169 878**	**303 452**	**407 610**	**529 844**
	Total own revenue	-	-	39 277	83 467	90 196	110 890	129 344	131 526	162 681
	Government grants	-	-	312	112 800	161 051	58 988	174 108	276 084	367 163
	EXPENDITURE	-	**126 897**	**166 161**	**167 990**	**165 109**	**156 202**	**240 558**	**278 493**	**416 508**
	Profit or (Loss)	-	(126 897)	(126 572)	28 277	86 138	13 676	62 894	129 117	113 336
	Profit or loss margin as % of total revenue	-	-	-320%	14%	34%	8%	21%	32%	21%
	Profit or loss based on own revenue	-	(126 897)	(126 884)	(84 523)	(74 913)	(45 312)	(111 214)	(146 967)	(253 827)
	Profit or loss as % of own revenue	-	-	-323%	-101%	-83%	-41%	-86%	-112%	-156%
Richards Bay IDZ	**REVENUE**	**20 107**	**26 357**	**31 169**	**29 921**	**40 506**	**37 641**	**168 221**	**179 915**	**176 486**
	Government grants	19 808	26 160	31 080	29 761	40 120	36 298	166 377	134 688	134 879
	Other income	299	197	89	160	386	1 343	1 844	45 227	41 607
	EXPENDITURE	**21 280**	**30 084**	**39 066**	**39 309**	**50 745**	**53 077**	**198 541**	**119 081**	**125 492**
	Profit or (Loss)	(1 173)	(3 727)	(7 897)	(9 388)	(10 239)	(15 436)	(30 320)	60 834	50 994
	Profit or loss margin as % of total revenue	-6%	-14%	-25%	-31%	-25%	-41%	-18%	34%	-
	Profit or loss based on own revenue	(20 981)	(29 887)	(38 977)	(39 149)	(50 359)	(51 734)	(196 697)	(73 854)	(83 885)
	Profit or loss as % of own revenue	**-7017.1%**	**-15171.1%**	**-43794.4%**	**-24468.1%**	**-13046.4%**	**-3852.1%**	**-10666.9%**	**-163.3%**	-
Dube Tradeport SEZ	**REVENUE**	**1 371 408**	**388 725**	**474 508**	**363 165**	**545 340**	**535 756**	**463 397**	**471 371**	**602 694**
	Own revenue	85 227	68 710	128 304	52 639	90 781	105 018	112 561	117 331	130 783
	Government grants and subsidies	1 286 181	320 015	346 204	310 526	454 559	430 738	350 836	354 040	471 911
	EXPENDITURE	**738 023**	**325 233**	**341 061**	**246 156**	**384 175**	**381 742**	**339 254**	**400 785**	**391 019**
	Profit or (Loss)	633 385	63 492	133 447	117 009	161 165	154 014	124 143	70 586	211 675
	Profit or loss margin as % of total revenue	46%	16%	28%	32%	30%	29%	27%	15%	35%
	Profit or loss based on own revenue	(652 796)	(256 523)	(212 757)	(193 517)	(293 394)	(276 724)	(226 693)	(283 454)	(260 236)
	Profit or loss as % of own revenue	-765.9%	-373.3%	-165.8%	-367.6%	-323.2%	-263.5%	-201.4%	-241.6%	-199.0%

Observations and conclusion: financial self-sustainability of SEZ entities

All SEZ entities still rely on government funding to augment their financial requirements. Own revenue is not enough to sustain current operations for the SEZs. In 2018/19, only Coega was able to cover its operational costs from own revenue. On the other hand, Saldanha Bay and Richard Bay SEZs' operational expenses far exceed their operational incomes excluding government support. The fact that all SEZs are still not able to cover operational expenses from own generated revenue raises concern on their financial sustainability if government funding is withdrawn. Projections suggest that it will take longer for SEZ entities to be financially sustainable without augmentation from the fiscus. As government keeps on designating more SEZs, potential funding pressure may be building up. It therefore means that there is a need to rethink a sustainable funding model of the SEZ programme considering that reliance on the fiscus will remain for years to come.

6 Options

SEZs by nature should provide a suite of incentives to attract and promote certain categories of industries. As a result, government has spent over R25.7 billion on the programme since inception. This funding was used to subsidise top infrastructure for investors and well as for bulk works and operational expenditure for the zones. This excludes other incentives that investors may have benefited from. Over the years, annual spending on the programme increased significantly. This coupled with designation of new SEZs, there is evident pressure on the available funding. On the other hand, the fiscus may not be able to provide adequate funding which has to be justified by demonstration that there is return on investment. Therefore, there is a need for alternative funding options.

While South Africa needs investors, considering that only three SEZs have managed to attract a sizable number of investors (at least some of whom would have invested elsewhere if the SEZs did not exist), it is high time that the country reviews the number of SEZs that can be supported given scarce resources. South Africa cannot afford to continue supporting SEZs that are failing to attract investors and should consider closing down those that have struggled to attract investors since the operators are relying on fiscal funding for their operational expenditure.

SEZ is a real estate business that enjoys the support of government. It must be based on sound and viable business models. It seems this is not the case. However, the SEZ operators should benchmark from privately run industrial complexes. That way, this will save government funding in the long term, as currently there is no prospect that SEZ operators will be profit driven. All operators currently rely on provincial government funding for operational expenditure as own generated revenue is not enough to cover all expenses. In other words, the operators are loss making. And, in the absence of meaningful subsidies, it is hard not to conclude that these activities would not be better managed in ordinary industrial parks unless there is some identifiable strategic/industrial goal that an SEZ might help government pursue and which would not be achieved in the absence of a publicly funded SEZ. If, on the other hand, the SEZs are little more than publicly funded industrial parks, offering no other material differences from the surrounding economy, it is hard to see the justification for public funding.

Alternatively, 20 years of government running SEZs with less significant progress, it may be time to experiment with public private partnership or privately managed SEZs. There were arguments that the SEZ is a government programme, which should not be ceded to the private sector. There is a need for a paradigm shift to allow a redesign of the programme.

Public private partnership model can take different forms such as collaboration in property development and revenue sharing. While there is hesitation that private sector mentality is profit driven which may obscure the special nature of the SEZs, government can always provide other forms of incentives or support without causing strain on the fiscus.

Apart from proposal on the funding aspect, there a need for improved reporting to determine the success of the SEZ programme. This should start by determining what is used to measure success. This should then be incorporated into a centralised reporting system, which allows standardisation.

The SEZ programme was expected to provide clarity on the management of SEZs in view of the challenges that were associated with the IDZ programme. However, six years down the lane, it seems progress in addressing the then identified issues is rather slow. Promised incentives have not been provided in some cases. As a result, investors feel deceived by government that does not honour its promises.

Current SEZ Fund is on a first come first served basis, which creates unhealthy competition among the SEZ. There is no assurance that an SEZ will receive funding in a particular year as each application is evaluated on its own merit. While this approach promotes quality-funding proposals among SEZs, it creates uncertainty on the funding of top structures.

7 Recommendations

It is recommended that in government, like in the private sector, poorly performing business units should be closed down to concentrate support to those that are doing better. A consideration should be made for SEZs that have failed to attract investors or to be operational to be closed down. This should be coupled with a suspension of processes of designating new SEZs especially in areas that have no comparative advantages at all. However, this should be determined by a comprehensive evaluation of the SEZ programme first.

DTIC and government should consider collaborating with the private sector in the management of SEZs under the PPP arrangement. It seems that current approach does not stimulate operators to have the desire to be profitable and be financially self-sustaining. Alternatively, consideration should be given to privately managed SEZ in the same way that office parks or shopping malls are managed.

Considering that not much of the promised incentives have materialised yet some SEZs have managed to attract investors, the key question to ask of a programme such as this is whether and to what extent the expenditure on subsidies and incentives generated economic activity that would not have happened anyway. This is a very hard question to answer, but it cannot be assumed that not every activity that is located in an SEZ would have happened if there were no SEZs. The DTIC, provinces and SEZs should demonstrate the extent of this causality to justify continuous support. This is a very difficult question to answer because the institutional structure and flow of funds is complex and no one seems to be centralizing and standardizing expenditure data. In summary, the spending review did not manage to cover depth that can respond to these questions. A comprehensive evaluation of the programme is therefore necessary.

During the spending review exercise, National Treasury struggled to get data that should ordinarily be available to assess performance of the SEZ programme. Delays in the implementation of the Performance Monitoring and Evaluation Framework has resulted in inconsistent reporting by the SEZs. The DTIC, SEZ Advisory Board and the SEZ licensees must urgently implement the framework and implement an online reporting system.

8 Actions

Government should justify existence of SEZs that have failed to attract investors. Such SEZs continue to receive financial support from provincial governments even though they have failed to attract investment. If closed down, savings can be realised.

Government should consider public private partnerships or privately managed SEZs, which will lessen the financial responsibility on funding for infrastructure and operational expenditure for loss making SEZ operators.

To determine the return on government funding, the DTIC should commission a comprehensive evaluation of the programme to determine its continuous funding.

Investor confidence is critical for the country. With concerns that government has not actually delivered on promised incentives, government should assess whether there is a benefit to extent provision of promised suite of incentives such as the 15 per cent corporate income tax. If there is justification, then this should be expedited. Alternatively, these incentives should be removed on the SEZ value proposition

The DTIC should implement a standardised reporting system to allow easy assessment and comparison among the SEZs. Under the current approach, there is disparity on the information that individual zones report on.

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