THE SIGNIFICANCE OF TRADE POLICY IN PROMOTING THE INTERNATIONAL COMPETITIVENESS OF SOUTH AFRICAN INDUSTRY

THESIS

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ABSTRACT

This study proposes to examine the significance of trade policy in promoting the international competitiveness of South African industry during the period from the early 1970s up until the present day. By providing a background of South Africa's past trade policies, it is argued that the origins of South Africa's low levels of competitiveness essentially lie in the apartheid years where trade policies were not linked to the attainment of international competitiveness and improved productivity. The study then reviews the development of South Africa's trade policies in the 1990s. In so doing, it reveals weaknesses in the areas of implementation which are critiqued in greater detail by using the clothing and textile industries as a case study, and other selected examples. The study finally concludes that trade policy is crucial to global competitiveness and that it is the responsibility of all parties concerned to ensure that trade policies enhance and not inhibit competitiveness.

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CONTENTS

INTRODUCTION

Following the democratic elections in April 1994 and the re-entry of South Africa into the world market, there has been much concern to make up for lost time. South Africa has become a participating member of the WTO, it has become a member of the SADC, it is busy negotiating a free trade agreement with the EC, a future agreement with NAFTA is being explored, and it is keen to become part of the Indian Ocean Rim initiative. Within the country, high on its list of priorities is uplifting the majority of South Africans by creating sufficient employment opportunities. The implications of these developments are extensive. For in order to cope with an intensely competitive world, one of the major issues that has to be addressed is the fact that South African industry is to a large extent internationally uncompetitive.

This can be directly traced back to apartheid whereby trade policies were not linked to the attainment of these goals. Essentially, protection was inefficiently instituted. The protective regime was complex and unpredictable, it was biased against exports, there was no drive to increase the level of beneficiation, there was no policy on the duration of protection and no performance requirements were imposed on protected industries. As long as a producer could supply at least 60 percent of the domestic market, firms were granted protection regardless of their competitive potential (Fallon et al, 1994). As a result, firms became accustomed to permanent protection where it was more profitable to supply the domestic market than to export. They were thus lulled into a state of policy induced laziness whereby it was not necessary to produce goods that were internationally competitive.

With the re-entry of South Africa into the world of international trade, the days of lobbying for protection against foreign competition, thereby effectively hiding behind protective barriers, have come to an end. The signing of the Marrakesh Agreement in 1994 heralded a new era where it has become essential to be internationally competitive in order to survive. The challenges are vast, for as Bell (1990) accurately points out, exposure to foreign competition is a double edged sword; it can just as easily kill off certain industries as spur them to greater heights of efficiency and competitiveness. It is thus essential that the government proceed extremely cautiously when it comes to devising and implementing its trade policies. South Africa cannot simply rely on policies that have been successful in other countries. Of course, there are some valuable lessons that South Africa can draw from the kept in mind that its situation is to a large extent unique and that the policies that are prescribed will work for South Africa, and not prescribed on the basis that they worked for other countries.

Furthermore, there is precious little time for the pursuit of "pie in the sky" ideals. The government cannot cast general dispersions as to how it intends to improve competitiveness. It has to be specific as to how this is going to be achieved and importantly, it has to do this in conjunction with all affected parties.

It is in this context that this study proposes to examine the significance of trade policy in promoting the international competitiveness of South African industry. This is done by examining the impact of past trade policies on the international competitiveness of South African industry. The study then reviews the development of South Africa's trade policies in the 1990s. In so doing, it reveals weaknesses in the areas of implementation which are analyzed in greater detail by using the clothing and textile industries as a case study. By critically looking at the literature surrounding the issues, it is my purpose to provide a modest contribution to this ongoing debate.

The dissertation is divided into five chapters. Chapter one provides a review of the debates surrounding the state, markets and international competitiveness, particularly the role of the government and that of the market in achieving international competitiveness. It then provides a brief analysis of the changes in the world market that South Africa is re-entering and the implications thereof, and within this framework poses the question about the centrality of trade policies in achieving competitiveness.

Chapter two provides a background of the historical development of South Africa's trade policies from the early 1970s up until 1990. It attempts to examine the impact that these past trade policies have had on the international competitiveness of South African industry. This is done by using data to analyze the effect that import liberalization and export orientated strategies have had on general growth rates and hence the competitiveness of the manufacturing sector.

Chapter three provides a review of the development of South Africa's trade policies from 1990 up until the present day. It attempts to show how government has developed its trade policies and what measures it has implemented by discussing various key documents.

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Chapter four provides a critique of policy implementation as well as trade policy in general by using the clothing and textile industries as a case study. In discussing how implementation has taken place within these industries, various issues of contention with regards to implementation are mentioned. These are then analyzed in greater detail and in so doing, the impact that present government policy is likely to have on the international competitiveness of South African industry is discussed.

Chapter five summarizes the arguments and then draws them together into some final concluding remarks.

Chapter One

The State, the Market and International Competitiveness: A Review

1.1. Introduction

Although the central concern of international competitiveness is international trade, the concept has far deeper ramifications than the simple perception that it is merely a measure of a country's ability to sell abroad and to maintain a trade equilibrium. According to ul Haque (1994) and Cohen (1994), international competitiveness is essentially a measure of a country's capacity to maintain and increase its living standards, to expand its employment opportunities and to be able to maintain its international obligations, without running into balance of payments problems. Simultaneously, international competitiveness is about making sure that the same policies that may limit balance of payment problems do not have adverse effects on the domestic front. Devaluation and deflation, for example, are common policies used to stimulate exports and close trade deficits. At the same time, however, they also involve a reduction in domestic income, an effect which would not contribute towards either the maintenance or increase of a country's standards of living.

International competitiveness is based on superior productivity performance and a country's ability to move production towards higher productivity activities which in turn can generate high levels of real wages. A good example of this is the current pattern of intra-industry trade, whereby countries are increasingly moving towards production in higher productivity sectors, such as highly advanced manufactured goods like machinery, pharmaceuticals and instruments, the sectors in which growth, efficiency and hence productivity are the greatest. According to Lawrence (1993:4), these are precisely the types of products in which industrial country exports have increased most rapidly. In fact, trade in manufactured goods has outpaced trade in primary commodities, with trade in the most advanced products having increased even more rapidly. This is also not only a trend that is exclusive to the developed world, for over the past two decades, trade in manufactured goods has become increasingly important for developing countries, particularly countries in Asia and Latin America.

Consequently, the types of products that a country produces impact on the growth of the standards of living. The higher the degree of specialization in high productivity products like pharmaceuticals, machinery and instruments, the higher the increases in standards of living will be.

Merely using the existing productive capabilities, however, is not enough. The newly industrialized countries (NICs) are a good example in this case, for they strove to become internationally competitive in new lines of production, by using the capabilities they had developed in the early phase of their import substitution stage. In so doing, they managed to create comparative advantage in new areas, by constantly introducing new and improved products and more efficient processing techniques. Policies which are not focused to some degree on this type of strategy, face the risk of a declining income rate due to a loss of market share to more competitive countries (ul Haque, 1994).

It then follows that competitiveness requires substantial investment in the necessary technology and skills in order to maintain the continual improvement and innovation in existing industries and the capacity to compete successfully in new industries. This is concurrent with the growth in manufactured trade, where it has increasingly become technology and skills that give a country a competitive edge in the international economy rather than natural resources and raw labour, experience has demonstrated that resources need to be extracted efficiently and that they need to be beneficiated. In today's global economy, countries with a poorly educated and trained work force and inadequate access to technology will not become competitive.

It is in this context that the controversy has revolved around the question, what tools are able to achieve international competitiveness. There are those who assert that the market is the ultimate tool in attaining international competitiveness, while others advocate a far greater degree of government involvement in the attainment of this goal.

The next section goes on to discuss these two approaches to international trade.

1.2. The Neo-Classical Approach

The current and most dominant approach to international trade is the neo-classical approach which is part of mainstream, traditional economic theory. It has its roots in the classical free trade theories which were proposed from the end of the eighteenth century, in reaction to mercantilism, by the likes of Adam Smith and David Ricardo who essentially argued that countries should concentrate on producing those goods for which its resources are most suited, implying those activities in which its costs are relatively cheapest. Accordingly, by exchanging these goods, all trading countries would benefit as, by using their productive capabilities to the highest efficiency, this would increase their combined output and raise their general living standards.

Their emphasis was thus on the gains from trade. Trade, it was argued, resulted in an increased international specialization of production and a division of labour. To this effect, the labour theory of value was developed, the notion that all costs can ultimately be reduced to units of labour, which in turn are directly related to the prices that must be charged for the products (Berry et al. 1993).

Classical theory continued to be refined throughout the nineteenth century and during the early years of the twentieth century. It was in 1933 that neo-classical theory began to take form, when Bertil Ohlin extended the earlier ideas of Eli Heckscher by replacing the classical labour theory of value with a new theory acknowledging the effects, not only of labour, but also the other factors of production, namely, land, capital and management - the Heckscher-Olin Model. Because countries differ in their factor endowments and their factor intensities, each country will export those goods whose production is relatively intensive in the country's abundant factor and import those that are intensive in the factors it lacks. Subsequent authors have continued to refine neo-classical economics, but they all still fall within the realms of traditional theory. What then according to the neo-classical approach determines international competitiveness?

If competitiveness depends on the types of products produced and traded, the logical question that arises from this is, what determines international specialization in production? According to the neo-classical approach, international specialization is based on the assumption that a country's relative factor endowments determines its comparative advantage, and that the market can generally be relied upon to be efficient in its allocation of the factors of production, as well as to determine the optimal pattern of product specialization (ul Haque, 1994). Consequently, it is held that any form of state intervention is unnecessary, and could even be harmful.

It is, however, recognized that free markets are not always optimal and, therefore, the concept of market failure is conceded. The presence of externalities, public goods, increasing returns to scale, imperfect information, 'few' buyers or sellers, are all instances which can lead to market failures, resulting in allocative inefficiencies and unemployment. The onus thus falls on the government to repair market failures.

Nonetheless, a distinction is made between acceptable and unacceptable areas for government intervention. Wade (1990) notes the essential economic functions of the state according to neo-classical economics:

- To maintain macro-economic stability;
- to provide physical infrastructure;

- to supply "public goods", such as defense and national security, education and the legal system;
- to contribute to the development of institutions for improving the markets such as for finance and labour;
- to eliminate price distortions which arise in cases of demonstrable market failure; and
- to redistribute income to the poorest, in sufficient measures for them to meet basic needs.

But more importantly, it is held that the government should desist from becoming an active player and should confine "itself to intervention that guarantees the framework of rules for the market order" and remove the "obstacles to competition and the free play of market forces" (Jones, 1983:69).

It is evident that neo-classical economics is committed to the primacy of economics over the government, as well as to the view that the market and the price mechanism are the most efficient means for organizing domestic and international economic relations. Consequently, it advocates export-orientated trade strategies with the emphasis on comparative advantage.

1.3. Statism

The fact that no country in the world today actually fulfills the theoretical postulations of market theory, indicates that neo-classical economics does not provide an adequate explanation for international trade. In an economic world order which is characterized by countries at varying stages of economic development, with some having distinct advantages and eventually becoming more efficient and internationally competitive than others, the lesser developed of these countries are put under increasing competitive pressures as they become more exposed to the world economy. The major impetus for protection is thus a country intent on improving the position of its domestic producers relative to foreign producers (Frieden, 1991), who will undoubtedly engage in some forms of protectionism. As it is naturally the objective of every country to pursue economic policies that promote national economic growth and development, where it is perceived that the market is failing to achieve or further a country's national goals, the state is expected to intervene.

In addition, as a result of the Keynesian revolution, government's role in maintaining employment and creating an environment where living standards can rise, has a wide following. The neo-classical model is thus no longer seen as infallible. This, however, does not mean that just because the neo-classical prescription is not completely accepted, that the market is necessarily rejected. In fact the debate has in recent times transcended this issue and recent controversy is precisely about what kind of balance should be struck between "how much" government and "how much" market.

Today, the importance of macro-economic policy and the need for policy intervention to support macro policy is not contended. The debate concerns the effectiveness of government policy and identifying the sources of market failure that might require some form of government intervention. Although traditional theory concedes demonstrable cases of market failure which may call for some form of government intervention, there are areas where the government's role has been said to be more "ambiguous" and "controversial" (ul Harque, 1994), but which still demonstrates the need for intervention.

The government's role with regards to national interest is one such area. Take the example of the opening up of trade between the USA and Mexico which has resulted in Mexico's wages rising and the USA's wages falling, and hence its employment and living standards. Another example is the situation of the former Soviet Union where, as a result of the opening up of world trade, output and employment have fallen drastically. In circumstances such as these, where a country's employment and living standards are threatened, the argument that the market is allocating resources efficiently and that all that is needed is for them to move to higher productivity jobs, is not likely to be very persuasive. In such cases, the government clearly has a role in facilitating the re-allocation of labour through macro-economic policy as well as specific actions at the sectoral level. State intervention may also be necessary in order to redress the balance where some are able to take better advantage of the market, than others.

The development of technology is another such area. Progress in technology is crucial with regards to an economy's capacity to grow and compete internationally. A major determinant of progress in technology is the effort put into Research and Development (R&D) (ul Harque, 1994). According to Nelson (1981), because the outcome of R&D is characterized by an intrinsic uncertainty together with the general proprietary nature of technical knowledge, this represents a case of market failure. Factors contributing to this conclusion are numerous. Technology is not a product that can be bought and sold as such, for the cost of acquiring it and its effectiveness varies enormously among firms. Additionally, the market cannot be relied upon to allocate resources to R&D, due to firms lacking the incentive to innovate, as well as being deterred by the knowledge that others can easily imitate them. The result is that the market causes either too much or too little to be spent on R&D, making it extremely difficult for the right balance to be struck. Although there is no guarantee that the government can do any better, government support of R&D is extremely prevalent. The government also has an important role in building the nation's ability to develop and use

Another area is that of the development of the non-tradable sector. This includes technological knowledge. labour, infrastructure and public administration, the efficiency of which is essential to international competitiveness. The NICs, for example, are well known for their superior quality in labour and infrastructure, which are the result of efficient civil services in successfully dealing with the problems of information, administrative capability, transparency, accountability and impartiality (Stern, 1989). The inclusion of public administration is thus significant, for its effectiveness largely determines the success of government intervention.

This brings me to perhaps the most important factor with regards to government intervention, namely that it is not necessarily good or bad trade policies that determine economic success, but the efficiency of the government in implementing them. As Lall (1993:59) appropriately argues:

> "The government itself is the most important 'institution' in the development process. Its ability to design and implement policies is what determines industrial competitiveness, and the best set of policies is not that of a 'minimalist state' which provides law, order and defense and leaves the rest to (perfectly functioning) markets".

Take the case of the NICs which currently rank amongst the world's top exporting countries. It is generally conceded that their outward trade orientation contributed towards their spectacular performance, but more significant than the actual policy orientation, is the fact that this success was attained despite extensive government intervention. Furthermore, although the NICs switched to an export-led path of industrialization, this in not to say that import substitution came to a halt. In Taiwan and South Korea, for example, import substitution and export promotion took place simultaneously (Wade, 1990).

Another neo-classical assumption that the NICs challenged was the static notion of comparative advantage, namely that each country should specialize in those areas where it has the most natural advantages and import those goods that can be bought more efficiently from abroad. These countries, although agreeing with the fundamental principles of comparative advantage, demonstrated that comparative advantage was a dynamic concept which could be created, a notion which has generally gained wide recognition over the years.

Take Japan for example, who had a comparative disadvantage in precision machinery in 1967. According to neo-classical theory, Japan should have opened its borders and allowed foreign competition to wipe out this industry on their way to delivering cheaper products to Japanese consumers. Instead, precision machinery and other industries were protected until they had surpassed their US counterparts (Finance Week, January 14-20, 1993).

The answer, thus, lies in the effectiveness of state intervention. The NICs had governments who were highly effective in carrying out government policy. Amsden (1992), points out the essential difference between governments that are effective in carrying out government policy, and those that are not. Accordingly, effectiveness does not rely on whether subsidies are or not given, for all governments do this. Rather, effectiveness depends on the principles that govern the allocation of subsidies. Countries that have not made the transition from import substitution to export-orientated growth, have failed for a very specific reason, namely that no performance standards have been imposed upon the recipients of subsidies. If there is no discipline, then the industries receiving them are unlikely to become internationally efficient, productive, and hence competitive. The same argument applies to export subsidies.

Countries that have successfully made the transition to outward-orientated growth have disciplined subsidy recipients. According to Amsden, the differences in rates of growth and productivity among late-industrializing countries depends on the degree to which countries are willing and able to discipline capital. The NICs have demonstrated this willingness and attained this ability, while many of the countries who have not made the transition from import substitution to export-orientated growth, particularly the less developed countries, have not.

The same principal can be applied in the case of industrial policy, whereby certain industries are selectively promoted. Although it is now generally accepted that industry is the basis of economic prosperity, and that all governments have policies that regulate and provide incentives to industries, there is little consensus on whether the government should intervene on a strategic basis. Many argue that governments do not have the ability or knowledge for making economically rational strategic choices. This probably explains why strategic industrial policy has been such a failure in many countries. It does not, however, explain why it has been such a resounding success in others, particularly the NICs. Contrary to what many believe, the formation of their industrial policies was not made by government bureaucrats making arbitrary decisions without regard to market signals, rather, it was a consultative process involving all affected parties (Ul Haque, 1994). What it demonstrated was that the government does have an essential role in forming an environment conducive to the creation of "winning" industries.

This leads on to another important point, that of the interaction between government and business. Various models of this interaction exist, the differences of which do not lie in the extent of government intervention, but rather in the *nature* of the relationship between the two. The economic success of countries like Taiwan and Japan, for example, is due to the close and complementary relationship between business and government, a lesson which most countries would be advised to take heed of.

Consequently, the combination of Keynesian and Statist arguments lead to very different trade strategies than those prescribed by mainstream, traditional theory, namely import substitution and extensive government intervention in the operations of the market. This debate demonstrates that competitiveness does not only depend on the market.

The next section therefore discusses the trade strategies that have historically reflected these different theoretical approaches.

1.4. Trade Strategies

Weiss (1988), appropriately sums up the traditional distinction between the two main trade strategies that dominate the literature. Inward orientated policies which aimed at meeting the demands of the domestic market, and outward orientated policies which do not necessarily discriminate against the domestic market and often encourages exports. Accordingly, the general trade strategy pursued by inward orientated economies is import substitution, while export-led industrialization is the trade strategy pursued by outward orientated economies. Both of these have played their roles in history.

Between 1815 and 1914 the economic system became characterized by export-led growth and market orientated policies. Despite this, it was mixed and sometimes dominated by fairly extensive protection, with protection of the import-competing sector becoming a feature of the industrialization process of many countries such as the USA, Japan, Austria, Hungary, Italy and most of the developing countries.

With the economic effects of the Great Depression in 1929, a general pessimism developed with regard to the power of trade in promoting rapid economic growth. In a world economy where there was a marked slackening in the expansion of world trade, and where a number of countries had demonstrated that import substitution was a feasible trade strategy, the option of export expansion became increasingly limited. The onset of World War 2 and the consequent economic effects thereof simply reinforced these sentiments with the government being assigned a substantial role in repairing market failure (Wade, 1990). For the less developed countries which had not "taken off" in the way countries like the USA, Canada, Australia, New Zealand, Japan and Sweden had, an even larger role for the state was required. This led to the import substitution strategy of economic development becoming the dominant trade strategy, the basic rationale being that in order for countries to metamorphose from a stagnant economy to a growing one, protection was necessary in order to give them the chance to mature to the point where they could satisfactorily compete in world markets.

When import substitution was initially established the results of the first stage, involving the production of non-durable consumer goods characterized by intensive unskilled labour, unsophisticated technology and so on, appeared promising. However, by the late 1950s and early 1960s, difficulties experienced in import substitution led to a policy divergence:

- Import substitution resulted in inefficient and uncompetitive industries;
- rent seeking began to divert energies away from actual production;
- resources were inefficiently allocated;
- employment and income distribution worsened;
- exports were detrimentally penalized;
- too many plants produced too small an output;
- quality was inferior;
- capital was underutilized;
- an increasingly monopolistic or oligopolistic industrial structure developed;
- there was a general failure to develop manufactured exports; and
- increasingly stringent exchange control regimes developed. Wade (1990) ,Williamson et al.

(1991) and Fallon et al. (1994)

In general, import substitution was not targeted according to systematic economic criteria, but instead was pursued in a chaotic, inefficient manner and for too long a time (Meier, 1990). Import substitution ordinarily meant high-cost production for limited national markets, leading to inflation and representing a continual drain on economies.

Local markets became saturated and opportunities for further import substitution became exhausted. Only those less developed countries with very large domestic markets like Mexico, Taiwan the Philippines and Brazil have had some success with import substitution and even these countries have had to find new strategies for further growth.

Despite this, in the early 1960s many less developed countries like India, South Africa and most of Latin America went on to the second stage of import substitution, involving the production of more durable consumer goods. For countries with little industrial expertise, the production techniques of capital intensive and some intermediate goods was not as suitable as for the production of non-durable consumer goods, and furthermore it entailed production that was increasingly high cost, the decrease in the rate of growth in aggregate output, and lagging employment as further import substitution became more difficult (Meier, 1990). Other countries, however, in particular, Hong Kong, Taiwan, Korea and Singapore, broke away from import substitution and adopted outward orientated trade strategies.

Against this background, the next section examines import substitution and export-led industrialization in greater detail.

1.4.1. Import Substitution

Import substitution is the process whereby resources are allocated away from production for exports toward production for the domestic market, in the attempt to promote domestic industrialization. The aim is thus to displace imports by producing those goods locally, which is done by employing protection measures such as import tariffs, restrictions on imports and controls on access to foreign exchange (Weiss, 1988). This has the effect of protecting domestic producers from foreign competition and cheapening imported capital goods for production in the domestic market by an over valued exchange rate.

Import substitution has been justified for a number of reasons. One explanation is export pessimism. Because of the low price and income elasticities of demand for the primary products produced by most less developed countries, export revenue grows very slowly. If industrialization is then to proceed, it should be on the basis of producing for the home market. Related to this is the perception that it is easier to save foreign exchange through import substitution rather than to earn it by exporting manufactured goods.

The existence of externalities is another rationale. They can arise in a number of ways, such as in the case where an industry invests in the improvement of worker productivity. If the industry wants to reap the benefits of having better qualified workers, it has to take into account that the worker may leave. If this happens, the industry will be left bearing the costs and will in future not invest in the improvement of the skills of its workers. Protection, it is argued, will encourage the industry to expand production and expenditure (Grabowski, 1994).

Perhaps the most common justification is the infant industry argument. If a new industry has the potential to compete at international standards, but is vulnerable in its initial phases due to high start-up costs and operating inefficiencies, it will not be able to compete with established foreign industries, without some measure of protection. Protection can then be withdrawn after its initial start-up phase which has given the industry enough time to establish itself. This argument is only valid for the less developed countries, and even then, the industry must really have the potential to become self-sustaining and not, as happens more often than not, come to rely on state subsidies.

1.4.2. Export-Led Industrialization

As opposed to import substitution, which is orientated toward the domestic market and whose activities are predominantly determined by government decisions, an outward-orientated export-led trade strategy is geared toward the international market. This, however, does not mean that an outward orientated trade strategy is not influenced by government decisions.

Although an outward orientated trade strategy appears to indicate a preference for foreign markets, this is not the case. Rather, what is stressed is that price incentives are set in such a manner so as to ensure that production for the domestic market does not become more lucrative than production for foreign markets (Bhagwati, 1988). Such a trade regime thus works at reducing the bias against exports, so that the relative incentives for home and export sales are neutral.

The benefits of export promotion are thought to be both numerous and widespread. The static, efficiency arguments for an export promotion strategy imply that once a country follows such a strategy there will be one-time overall gains in efficiency and do not imply that the rate of growth can be raised by following such a strategy (Grabowski, 1994). One such argument is the increased efficiency of the allocation of resources according to a country's comparative advantage in international trade, which will effectively raise a country's income. Another gain it is argued, is the realization of economies of scale. This argument is justified on the grounds that for firms to achieve optimal scale, they must produce for sale for foreign markets in order to achieve increasing returns and hence optimal scale. Domestic markets, it is argued, are simply not big enough for firms to achieve this.

There are also some additional gains which are considered more dynamic by nature and which actually raise the rate of growth. Lal and Rajapatirana (1987) argue that the key to rapid growth is the entrepreneur. In an import substitution environment where governments are free to use policies that can distort the domestic economy in order to guarantee that the domestic market is available for domestic producers, entrepreneurial activities become limited. They argue that an outward orientated trade strategy is more conducive for entrepreneurial activity, as greater opportunities and rewards are produced as well as limiting the options of governments. The effect of more intensive entrepreneurial activity is then higher growth.

Another dynamic effect relates to a country's importing capabilities. It is without question that most developing countries are unable to produce today's sophisticated capital equipment and will thus have to rely on importing such equipment. The rates at which new technology can be applied, however, depends on the ability to import, which in turn depends on how much foreign exchange a country has in order be able to import the goods. The faster exports grow, the greater will be the foreign exchange generated to pay for the imports and as the rate of technical innovation increases, the more likely the overall growth rate is to increase.

Today, it is generally recognized that the gains associated with export promotion are far superior to those associated with import substitution. This, however, does not necessarily mean that protectionist measures should be discouraged. On the contrary, I would assert that there are many countries in dire need of these measures, but they need governments that are highly effective in carrying out policies. Unfortunately, more often than not, these policies are nor pursued according to systematic economic criteria, thus leading to inefficiency. Additionally, these policies, instead of being seen as temporary measures, become permanent fixtures.

Although the attainment of international competitiveness largely depends on effective implementation of trade policies, another significant influence is the importance of participating in the changing nature of the global arena of trade and the demands it imposes on participating countries. This next section analyzes how the changing world economy is likely to impact on South Africa's quest for global competitiveness.

1.5. The Centrality of International Trade

One major lesson that has been learnt over the last 40 years is that increased participation in the world economy has become the key to domestic growth and prosperity. Since 1950 there has been a close correlation between a country's domestic performance and its participation in the world economy (Drucker, 1994). This correlation is seen in countries like Japan and South Korea who have grown the fastest in the world economy and whose domestic economies have also grown the fastest. However, countries like Great Britain have retreated from the world economy with domestic economies that have consistently declined. There are also those countries like France and the USA who have maintained their participation rate in the world economy within a fairly narrow range, and whose domestic economies have performed neither exceptionally nor persistently badly as Great Britain. In fact, according to Drucker (1994), the evidence of the last 40 years convincingly demonstrates that participation in the world economy has become the controlling factor in the domestic economic performance of developed countries.

In a recent World Bank study of Japan, South Korea, Hong Kong, Taiwan, Indonesia, Singapore, Malaysia and Thailand, two common economic policies surfaced (Drucker, 1994:106). Firstly, these countries did not try to control the economic weather. Instead, they focused on creating the right economic climate. Secondly, it was found that these countries adopted policies that would reinforce the competitiveness of their industries in the world economy, paying only secondary attention to the domestic effects.

South Africa has a small economy, relatively speaking, and does not amount to much in world trade as its share therein is relatively small. Today it is internationally uncompetitive in many sectors. To overcome its many limitations, it is crucial that the South Africa economy becomes fully integrated into the global community.

It is through international trade that countries earn necessary foreign exchange. However, for a country like South Africa, whose productivity levels are far behind those in developed countries, it is also a crucially important source of know-how, for it is only by competing in global markets or with open domestic markets that countries can be sure that their products meet world class standards (Lawrence, 1993). It is thus very important for South Africa to subscribe to the current tendencies in world trade, as they not only act as indicators of what can be learned from the experiences of other countries, but they also enhance the importance of South Africa's trade policies corresponding with the current world trading environment.

However, for South Africa to be able to do this, it has to have a sound understanding of the traits, dynamics and implications of global developments and an awareness of the realities and challenges facing the economy. As Scott (1995:200) states, "It will require realism, good planning and sound management of the country's reintegration into the global economy". For South Africa, the challenge is vast, as it is years since it has participated as a full member of the global community. Furthermore, South Africa's emergence has coincided with the unfolding of a new world order. So it is imperative that South Africa find a place for itself in the new world order.

In the next section, we examine in brief terms some of the important changes the world market has experienced, changes crucial to South Africa's global competitiveness.

1.6. Trends in International Trade and their Implications for South Africa

It is without question that the world economy has become increasingly integrated. Extraordinary advances have been made in transport, electronics and communications technology coupled with the trend towards deregulation and the lowering of barriers between national markets for production factors, and goods, which has resulted in a dramatic increase in trade especially between industrial countries. As a result of these advances, many of the obstacles which previously affected the location of production facilities, have been removed. The Global Economic Village has become a reality.

Production factors, notably the capital components have become tentacles in their quest for the most lucrative opportunities. Indeed, foreign investment abroad has grown dramatically and there is intense competition between countries to establish the most conducive conditions. Countries who are not competitive producers of goods and services, and who have not created an environment receptive to international business, have no hope in this competitive game. Traditional foreign investment, however, is rapidly shifting to alliances such as joint ventures, partnerships, knowledge agreements and outsourcing arrangements (Drucker, 1994). In fact formal and informal alliances are becoming the dominant form of economic integration in the world economy. The implications are vast, for although alliances increasingly generate both trade and investment, these are secondary. Instead they are based on the sharing of knowledge.

It is perhaps surprising that the concept of pooled knowledge has only recently come to the fore in such a large way. It all comes down to an increasingly competitive world. The speed in bringing new products to the world market has become a competitive race, critically important to competitive success. With increasingly complex and costly research and development, what better way to overcome this than by pooling knowledge. An increasing number of businesses are discovering that they can no longer produce technology and growth internally and are increasingly looking outside for strategic assets, and thus the trend for the formation of transnational alliances, to develop and market new products.

Some examples are the alliances between many university research labs and businesses. Then there are alliances in which organizations outsource support activities by letting independent suppliers do their data processing, maintenance and so on. An example of this shift to alliances is that of Intel, a US based microchip designer and Sharp, the electronics manufacturer who decided to divide the design and production of an advanced microchip between them resulting in both Intel and Sharp sharing the final product. According to Drucker (1994:103):

> "Integration in the Common Market is proceeding far more through alliances than through mergers and acquisitions, especially among the middle-sized companies that dominate most European economies".

Although alliances have become an important element of international trade, this does not imply that foreign investment no longer plays an important role. On the contrary, the period from 1985 to 1990 was marked by massive increases in foreign investment which grew three times as rapidly as the pace of world exports and the rate of world GDP. Although the annual global direct investment flow decreased in 1992, it recovered in 1993 and basically maintained an ongoing recovery trend in 1994, though the recovery rate slightly slowed (Jetro White Paper, 1996).

Foreign investment has been growing particularly rapidly in services, representing close to 50 percent of the total world stock of foreign investment by the late 1980s. This can be understood by the developments in information technologies, which have increased global integration in many service sectors that were once isolated. Additionally, the trend towards financial liberalization, privatization and deregulation has created investment opportunities in service sectors such as banking, communications, utilities and transportation in which investment opportunities were once limited.

For South Africa, the challenges are vast, for it needs sustainable higher levels of economic growth in order to grow. Attracting inflows of capital is an important way of doing so, especially in the form of equity and direct investment, for this is the type of capital that builds factories, thus leading to increased employment and increased exports. Furthermore, foreign investment also means securing access to essential technology, and facilitating the development and accumulation of skills in the local economy. The latter is significant for it is important for the South African economy not to become to reliant on foreign technology.

However, due to the intense competition for these limited resources, South Africa will have to attract foreign investors by being a competitive producer of goods and services and by creating an environment hospitable to business, thereby becoming an investor-friendly country. This is no easy task, for according to Scott (1995), for South Africa to be a serious contender for international investment, it will have to reconcile domestic political and social agendas with the realities of international competitiveness. Scott goes on to argue that social objectives cannot be allowed to overshadow economic business realities if the country is serious about attracting foreign resources. The government, the trade unions and the business sector all have a part to play in attracting much needed foreign investment.

At present there is some foreign interest in South Africa. By the end of 1995, R8.5bn was committed by foreign firms in investment money (Weekly Mail & Guardian, December 8, 1995). Although these figures are based on press reports, they are nevertheless indicative of a trend. Significant investments, for example, have been made by the Malaysian group Samrand, which has invested R1 billion in property and banking, Renong which is building a R201 million Hilton Hotel in Durban and is planning a R1 billion development at the Durban Point, and the Business Focus Group which is developing the R220 million Hilton Hotel in Sandton (Financial Mail, August 2, 1996, Internet). Recently, Malaysia has also injected R1.88 billion into Engen. In fact, the conservative estimate of the value of Malaysian investment in South Africa is around R5 billion.

The number of firms from the US coming back to South Africa is also on the rise. From 280 firms in 1985, this figure had dropped to 104 in 1991 and rose to 235 in 1995. Additionally, over 12 US firms invested over R200 million each in 1995 (Weekly Mail and Guardian, December 8, 1995).

However, despite this trend, relative to the size of the economy, foreign investment is still small and is not yet being converted into the type of large-scale, long-term investments that will expand the economy's productive capacity that creates jobs and wealth. According to South Africa's Mercedes-Benz chairperson, this is likely to continue, for foreign investors and governments are fast losing patience with South Africa's lack of urgency in implementing investor-friendly economic policies (Weekly Mail & Guardian, June 7, 1996). In particular, labour disruptions and pay demands are serious reasons why South Africa is not seeing this type of investment. Labour costs are a fraction of what they are in South Africa compared to countries like Indonesia. In this scenario, foreign investors are far more likely to go to these countries as opposed to South Africa.

In a world which is as competitive as it is fast-moving, it is necessary for South Africa to make the most of the current foreign interest. However, it is just as important for the government, the trade unions and the business sector to reach a mutual understanding on the issue. Without that the economy would soon collapse. As labour costs are not going to change, it appears than that South Africa is not going to see much of the employment creating investment. Instead, the type of investment that is likely to continue to predominate, are foreign firms opening up branch offices through assuming direct control of distributorship or through non-equity ties such as licensing and distribution agreements, foreign investors investing in South Africa companies (by far the largest type of investment at R4.5bn in 1995), foreign aid, soft loan funding and commercial lending.

Despite an integrated world economy, one contradictory consequence of this is the pattern of regional integration as the world has moved towards the formation of competing regional trade blocs. The impetus originates from the breakdown of the philosophical barrier between the market-orientated industrialized world and the state control-orientated Third World, and the military and ideological barrier symbolized by the Iron Curtain in Europe (Hormats, 1994). Both have artificially obstructed trade and investment among regional neighbours for decades. The removal of these barriers has allowed geography to play a decisive role in determining trade and investment.

The new order thus appears to be evolving along two broad tracks. The one will emphasize regional negotiations between newly market-orientated economies as well as between them and industrialized market economies, while the other will consist of ensuring the cooperation that will be required to ensure the consistency between global and regional trade expansion (Hormats, 1994).

Elements of threat and opportunity are inherent in the trend towards the formation of regional blocs. Regional free trade agreements can improve resource allocation by enlarging markets, expanding investment flows and creating economies of scale. They can also result in a further lowering of trade barriers and can improve cooperation on domestic policies. On the other hand, there is the fear that regional blocs could turn inward and erect protectionist barriers that would not only harm outsiders, but would also cripple the potential growth of the world economy. Although Asia, more than any other part of the world, has practiced open regionalism, with the majority of regions being partly closed, it is unlikely that there will be a shift towards closed blocs. Although countries may benefit from regional arrangements, extra-regional trade is simply too important to sever trade ties with the rest of the world. To date, the fears that regionalism will derail globalism appear to have been overcome.

By the end of 1994, at least 100 regional trade groupings were in existence. In fact, about 60 percent of world trade currently takes place within free trade agreements or among countries that have decided to achieve free trade by a certain date (Bergsten, 1996). Examples are the North American Free Trade Area (NAFTA), Mercosur in Latin America, the Asia-Pacific Economic Cooperation (APEC), the Association of South East Asian Nations (ASEAN), the European Union (EU), an EU agreement with 12 Mediterranean countries to establish free trade by 2010 (Euromed), the prospective Free Trade Area of the Americas devised by the 34 democracies of the western hemisphere (FTAA), the Southern African Development Community (SADC), the prospective Indian Ocean Rim trade bloc, and many more.

In order for countries to secure a solid position in the world economy, it is crucial that they cultivate links with the emerging major trading blocs. Additionally it is just as important for countries to develop intra-regional trade links in their own part of the world.

For South Africa who is not a member of a strong or potentially important trading bloc, it is essential that it forge bi-lateral and/or multi-lateral links with all the major global trading blocs in order to be able to win export concessions in exchange for favoured access to a large market. These are the European Community, the North American Free Trade Agreement and South America, and the emerging Asian trading area. Additionally, it is important that South Africa focus on its own region. This includes Southern, Equatorial and North Africa, and the Indian Ocean basin countries. South Africa's agenda should also include the reforming command economies of Eastern Europe, the former Soviet Union and China, and then the Middle East.

The EU has been South Africa's major market for the past few decades. More than half of South Africa's total exports are directed towards the EC, with a similar proportion of its imports coming from the area. It is thus important for South Africa to negotiate a favourable trade deal with the EU, as according to Elty Links, the new ambassador to the EU, "Securing worthwhile access to EU markets could lead to economic growth at home" (Financial Mail, July 19, 1996, Internet).

South Africa was unsuccessful in the bid to get preferential treatment in terms of the Lome Convention, a trade agreement between the EU and the African, Caribbean and Pacific (ACP) countries. Instead, the EU proposed a bilateral Free Trade Agreement. Negotiations between the EU and South Africa regarding the conclusion of the Free trade

Agreement were resumed this year after an eight month break, during which time South Africa drew up its negotiating mandate. The negotiations pertain to a two-part deal giving South Africa immediate access to the European market while allowing a ten year phase-in period for reciprocal treatment, and providing South Africa with limited membership of the Lome Convention. However, the EU's stance in trade negotiations has proved to be disappointing with their opening negotiation mandate not living up to South Africa's expectations or their original promises. At best it has offered a decidedly limited free trade deal, which has been rejected as one-sided by South African business.

The official feeling from Pretoria is that the EU's exclusion of almost 39 percent of South Africa's farm exports, including zero-trade items, on a list on which import duties will be levied for up to twelve years (Financial Mail, June 7, 1996) from the free trade accord is unacceptable and that it fails to address the concerns of SACU who greatly fear losing revenue from the Southern African customs union pool, which will certainly be affected by the reduction of tariffs for the EU. Thabo Mbeki, however, returned from his eight-nation European tour confident that the EU would back down from its position with regard to South Africa's farm exports, particularly in light of the fact certain EU members like the UK and Sweden are adamantly opposed to the EU's "blocking" mandate.

At this point, serious negotiations to conclude the trade deal are scheduled to start in the new year.

Although only 12 percent of South Africa's total exports by value go to the SADC countries (Angola, Botswana, Lesotho, Malawi, Mozambique, Swaziland, Tanzania, Zambia, Zimbabwe, Namibia and Mauritius), over 30 percent of its total manufactured exports by value go to these countries. This implies that South Africa's trade with Southern Africa is particularly important, with many South African manufacturers exporting only to the African market. However, the GNU envisions something far more than simply ensuring the continuation of advantageous trade with Southern Africa. According to an electronic document concerning South Africa and the SADC (1996), the GNU's vision for the Southern African region, "is one of the highest possible degree of economic co-operation, mutual assistance where necessary and joint planning consistent with socio-economic, environmental and political realities. South Africa strives to achieve regional economic development by using the SADC". This vision corresponds with the aims of the SADC, namely to provide for regional peace and security, sector cooperation and an integrated regional economy.

South Africa demonstrated its commitment to the aims of the SADC by acceding to the SADC Treaty on the 3 August 1994 and becoming the organization's financial and investment sector coordinator.

At the SADC's 16th summit in Maseru in August of 1996, the SADC including South Africa moved a step closer to becoming a free trade area by signing a trade protocol agreement which should be in place by May. The protocol provides the legal framework for the phased reduction and eventual elimination of import duties and other measures restricting free trade in the Southern Africa region over an eight year period.. In addition, it makes provision for existing arrangements like the customs union and bilateral agreements. The protocol, however, does not go into detail about the time period over which the tariffs will be reduced. Although the general feeling is that the process should be a speedy one in the hopes that it will open up South Africa's markets and address the massive trade imbalances within Southern Africa, South Africa is in favour of a longer phasing period. According to Alec Erwin, Minister of Trade and Industry the assertion that this is an attempt for South Africa to maintain the status quo has no foundations as "the fact is that the trade imbalance within the region is growing rapidly in our favour in spite of tariffs....if you remove these trade barriers faster, they will accelerate even further in our favour" (Africa News Service, 1996, Internet).

It is to South Africa's advantage to become part of the mooted Indian Ocean Rim Trade Bloc that could eventually comprise 22 member states stretching from Australia right through to Malaysia. For there are identifiable interests, unity of thought, confluence of size and levels of development that favour the encouragement of free trade through market-friendly policies that have already been applied voluntarily (Financial Mail, October 27, 1995). Furthermore, such an initiative would offer a total population of around 1.5 billion people, amongst which one third are urbanized. This has vast implications for the development of skills as well as a market for consumer durables and industrial equipment.

The idea of the formation of the Indian Ocean Rim Trade Bloc was first mooted publicly by Pik Botha in Delhi in 1993. India and Mauritius who were becoming increasingly concerned at being shut out of its foreign markets responded positively. As a result, the three countries became the main driving force behind discussions held in Mauritius in April 1994. Together with Australia, Kenya, Singapore and Oman it was then decided to create a forum that would "pursue mutual co-operation in trade, investment, infrastructure, tourism, science, technology and human resource development" (Financial Mail, December 1, 1995, Internet).

However, the official stance is a cautious even exploratory one with the initial emphasis on building up mutual trust. It is also apparent that any formalized structure is not on the cards for quite a few years. At this point in time it appears as if South Africa is more interested in forging bi-lateral trade relations.

1.7. Conclusion

This chapter set out to review the theoretical debates around international competitiveness. It showed that although outward-orientated strategies have the highest correlation with economic success, the government has an important role to play in guiding the development process and that the issue of whether the government should intervene or not has shifted to "the nature of its role and the conditions under which intervention can be effective" (Black, 1993:204). However, emphasized was the very real risk of a government failing to design or implement sound policies due to a variety of factors. Despite this it was argued that the fact remains that it is possible to intervene effectively and that there is a strong need for pro-active government policy to promote international competitiveness.

It was in this context that the next section went on to attempt to demonstrate that although trade policy can be a significant influence in the attainment of international competitiveness, the changing nature of the global arena of trade and the demands it imposes on other countries, is just as important a factor. Hence the importance of South Africa finding a niche in the current world economic order. It was therefore argued that South Africa would have to design policies that are consistent with trends in international trade. However, in order to do this South Africa would have to have an intimate understanding of to its own needs, interests, its priorities and how to pursue them. Only once a balance between the two is attained would South Africa be able to truly become part of the international world of trade.

It is in this context that the next chapter goes on to examine the effect that past trade policies have had on the international competitiveness of South Africa's industries.

Chapter Two

A Background of South Africa's Trade Policies, 1972 - 1990

2.1. Introduction

The previous chapter provided a review of the debates surrounding international competitiveness and the changing world economic order that South Africa is presently re-entering. It emphasized the centrality of sound policies corresponding with effective government intervention. This chapter attempts to demonstrate this point by examining how South Africa's past trade policies have effected its international competitiveness and productivity.

2.2. South Africa's Economy

South African industry is not without its merits. It has a large and diversified manufacturing sector and has established several areas, mainly in heavy and technologically demanding industries such as metallurgy, chemicals, paper and some industrial mining equipment, that have matured behind protective barriers into international competitiveness.

Despite such achievements, large areas of South African industry suffer from a wide spread malaise of uncompetitiveness, the lack of technological dynamism and declining productivity. It is a well documented fact that South Africa's annual average growth rate in real GDP has been declining consistently since the mid 1960s. Table 1 demonstrates that between 1961 and 1992, the average annual growth rate in GDP declined from 5.94 to 1.03.

Table 1

Average Annual Growth Rates in Real GDP (percent)

	1961-65	1966-70	1971-75	1976-80	1981-85	1986-92
GDP	5.94	5.15	3.49	3.13	1.36	1.03

Source: Fallon and da Silva, 1994

The composition of GDP has also changed. Traditionally the sector accounting for the largest share of GDP, the mining sector has declined tremendously since the mid-1960s, not only in absolute terms, but also in relation to other sectors of the economy. As a result, the manufacturing sector has replaced mining as the leading sector of the economy and is now the principal component of GDP (Fallon et al. 1994). The performance of the manufacturing sector, however, also reflects the decline in real GDP growth. For it has been characterized by low (and occasionally negative) total factor productivity growth, combined with much lower employment and output growth for the last two decades.

2.3. What is to blame?

There are many factors that have contributed to the slow growth experienced since the 1970s. High inflation, negative real interest rates at times, acute balance of payments deficits and excessive government spending have all played their part. After all, the importance of a viable macroeconomic framework for sustainable growth is most important.

Political factors have also influenced growth. The Sharpville massacre in 1960 appears to have had little impact, as GDP growth continued until 1965. After the Soweto Uprisings in 1976, however, growth declined substantially and the imposition of trade and financial sanctions in 1985 exacerbated its downward decline. Although their was a recovery in growth between 1986 and 1988, increasing political uncertainty and growing social unrest have contributed to the subsequent decline.

According to (Moll, 1994) the evidence points more to inappropriate trade policies and ineffective state intervention. South Africa performed very well during the 1930s and 1940s, due to appropriate policies. However, economic policy became internally orientated rather then taking advantage of the potential opportunities on rapidly expanding world markets. Industrial exports received negligible attention and the rand was to strong to make industrial exports profitable (Moll, 1994). As a result, in order to keep the balance of payments healthy, inefficient direct controls over imports were instituted, while the tariff structure became world renown for its complexity and intractability.

There is then the issue of government intervention, the size and type of which has also been proven to be crucial in developing countries. In South Africa's case, prior to 1950, intervention in the markets worked well and was appropriate given the external environment it faced. Thereafter, it became incompetent and ineffective. The South African state intervened extensively in industrial development. Endeavouring to control and steer labour and capital markets favouring low-productivity sectors and firms at the expense of modern manufacturing and services, it had poor technology policies and high government spending (Moll, 1994). In addition, intervention as a support for political objectives appears to have been a high priority with government initiatives such as Armscor, Sasol, Atlantis Diesel Engines and Mossgas absorbing massive quantities of investment in capital-intensive projects.

Consequently, South Africa currently faces complex problems of restructuring and industrial competitiveness, the origins of which lie in its trade strategy of import substitution, which was instituted in the early twentieth century.

2.4. Trade Policy in South Africa, 1972 - 1990

Industrialization in South Africa has taken place mainly through a process of import substitution, whereby production for the domestic market has been favoured by high protection, thereby making production for the domestic market more profitable than production for exports. While the basis for South Africa's export expansion has been a heavy reliance on its minerals and highly capital-intensive first-stage processing industries. By 1972, it was evident that import substitution was no longer a source of growth and had become increasingly capital-intensive. As a result, South Africa began the process of liberalizing its protection system accompanied by a reorientation of trade policy towards exports, whereby export promotion and assistance schemes were introduced in order to accommodate the lack of international competitiveness.

2.4.1. Import Liberalization

Prior to 1972, the main instrument of protection was the use of import controls which were tightened or relaxed according to the state of the balance of payments (Bell, 1992). The GATT, however, frowned on the use of import controls on balance of payments grounds and as a result in 1972 the government began the process of eliminating quantitative restrictions and replacing them with equivalent tariffs.

Between 1972 and 1976, quantitative restrictions were gradually relaxed. However, due to major episodes of the real appreciation of the rand, no further progress was made until a partial recovery was experienced in 1983, after which the process of eliminating import controls accelerated. Furthermore, in 1985, the authorities relaxed import permits, also a form of import control. Further relaxation of quantitative restrictions continued after 1985, and by the early 1990s had been reduced to around 10 percent (mainly on agricultural products and textiles). Considering that around 77 percent of South Africa's imports had been subject to import controls in 1983, this was a considerable achievement.

As import controls were reduced and replaced by increasing tariffs to limit the impact on industry, this did involve a certain amount of liberalization, as according to Bell (1992), the new tariff levels were lower than the tariffs implicit in the import controls. Tariffs took the form of higher *ad valorem* tariffs and import duties, giving a higher level of protection against lower import prices.

In the latter half of the 1980s there was a partial erosion of the substantial progress in import liberalization that had been achieved by 1985. It started with the severe economic downturn experienced between 1984 and 1986, which had the obvious effect of increasing the number of applications for protection in the form of ad valorem and formula duties. Furthermore, substantial import surcharges were introduced in October 1988 to compensate for balance of payments disequilibrium caused by sanctions which were instituted in 1985.

Despite the substantial liberalization of the trade regime in the past decade, serious problems still remain. Much still needs to be done to the tariff structure in order to reduce the distortions created in the local manufacturing industry such that competitiveness is not at any real level. South Africa's tariff structure is also one of the most complex in the world due to excessively frequent tariff changes, the profusion of tariff rates and the complicated manner in which tariffs are levied. Compared to developed countries, South Africa is a highly protected economy with an average duty rate twice as high as New Zealand, the country with the next highest level of protection.

2.4.2. Export Promotion

Traditionally, the mining industry and highly capital-intensive first stage industries have contributed the greatest share to total merchandise exports. Exports in manufactured goods have been neglected, as protection has made it far more lucrative to produce for the domestic market with insufficient efforts having been made to counteract these effects. With the long-term prospects of the mining industry looking extremely gloomy, and the subsequent decline in the terms of trade against primary goods and simple manufactured goods, it was becoming clear that manufactured exports would have to be relied upon to a far greater extent, to become the source of much needed economic growth. In fact, it was becoming evident that the main burden for the expansion of total exports was falling chiefly on the manufacturing industry.

Several significant events in the early 1970s indicated that South Africa was becoming serious about restructuring its export trade. The first of these was the appointment of the Reynders Commission of Inquiry into the Export Trade of South Africa in 1972. The Commission recommended that South Africa diversify its economy, focus on the need to expand the manufacturing sector while simultaneously looking for new markets for its exports (Leysons and Thompson, 1994). Although an export incentive scheme was not proposed by the Commission, the Export Development Assistance Scheme was, however, introduced in 1972, involving a tax allowance for marketing expenses incurred in connection with exporting.

The trend continued when in 1977, the van Huysteen Committee was appointed to review the system of export incentives. The result was a new, considerably reinforced system of export incentives to assist exporters with the comparatively higher cost of local production and the high cost of delivery to markets, which came into effect from September 1980. Accordingly, exporters became eligible for customs duties drawbacks and exemptions from customs duties paid or payable on imported materials used in manufacturing goods for export (Bell, 1992). This system was however, unwieldy, and was not used as an instrument to acquire free access to more competitive inputs. It also coincided with a massive real appreciation of the Rand and the onset of world recession, the result of which was the beginning of a sharp decline in South Africa's exports.

In 1988, the Board of Trade and Industry (BTI) published "A Policy and Strategy for the Development and Structural Adjustment of Industry", proposing much greater support on a selective basis to promote the structural adjustment of chosen industries (Black, 1993). The central objective was to enable the manufacturing sector to compete effectively in export markets by instituting a series of sectorally based structural adjustment programmes aimed at improving the competitive capability of local industry. Export industries were divided up into three groups. The first category comprising mainly primary and intermediate products would not require export assistance either because of a natural comparative advantage, or because assistance would not substantially increase exports to warrant it, or because the product should only be exported in a more beneficiated form. The second category comprising those industries already contributing significantly to exports would for a variety of reasons need assistance to maintain and increase the export performance. Finally, the third category comprising mainly intermediate and finished manufactures with export potential would require encouragement through assistance. Importantly, the BTI emphasizes the need for performance requirements as a criterion for the granting of assistance.

The Report argued that government policy should act in support of industries with actual or potential comparative advantage. Additionally, it emphasized the necessity of supply side measures such as the improvement of productivity and the mode of technology transfer. Although the BTI's structural adjustment programmes were never fully accepted, important components were adopted by the motor vehicle industry. Additionally, other structural adjustment programmes were partly put into practice, such as for the clothing industry.

The BTI's proposed structural adjustment programmes have, however, been the source of a major disagreement between the BTI and the Department of Trade and Industry (DTI), with the DTI arguing that they were complicated, unmanageable, unaffordable and not "in line with the emergence of a more market orientated direction" (Black, 1993:212).

The DTI's rejection of the BTI's selective support was followed, in April 1990, by the introduction of the General Export Incentive Scheme (GEIS), a new and more powerful system of export subsidies, currently the major export incentive scheme in place. The GEIS was designed to assist firms in offsetting the price disadvantage faced by South African exporters in international markets, by providing a tax-free financial incentive to exporters based on the value of exports, the degree of processing and the local content of the exported product. Furthermore, the DTI went on to release its "Modification of the Application of Protection Policy" in June 1990, a Report proposing the reduction of protection and reorientation of industry towards external markets, to be discussed in the following chapter.

2.5. The Effectiveness of Export Promotion Measures

According to Holden (1990), the export incentives introduced in the 1970s were simply an attempt to address part of the bias which existed against manufactured exports in the 1950s and 1960s and did not necessarily mean a switch to a trade strategy of export promotion. In fact, the strategy was initially implemented in a half-hearted manner due to the differences in opinion within government on the importance and means of promoting exports, as well as the imposition of sanctions which resulted in the main thrust of policy intervention remaining in support of strategic self-sufficiency (Black, 1993).

Considering the performance of exports since 1970, (See Table 2), the dismal performance of exports between 1980 and 1985 from 4.1 percent to 1.5 percent is significant. Between 1985 and 1990, exports improved somewhat from 1.5 to 2.4 percent, despite the imposition of sanctions. Significant, however, is that they did not reach the export growth rates experienced between 1970 and 1980 (See Table 3).

Taking the export performance of the manufacturing sector as a whole in relation to the need to accelerate the export growth rate, the results have been disappointing, as the growth rate between 1985 and 1990 at 12.7 percent was lower than for the period from 1970 to 1980 at 20.4 percent (See Table 3).

Table 2

Exports of Major Economic Sectors of the South African Economy, 1970 - 1990 (Percentage Share of Sector in Total Exports)

	1970	1975	1980	1985	1990
Agriculture	6.2	6.3	4.1	1.5	2.4
Mining	44.6	46.6	54.1	53.2	42.4
Manufacturing	43.5	40.3	37.5	39.4	47.8
Services	5.7	6.8	4.3	5.9	7.5
TOTAL	100.0	100.0	100.0	100.0	100.0

Source: Bell, 1992

Table 3

Exports of Major Economic Sectors of the South African economy, 1970 - 1990 (Annual Rates of Growth in percent)

	1970-75	1975-80	1970-80	1980-85	1985-90
Agriculture	21.9	13.1	17.5	25.4	18.3
Mining	22.5	26.7	24.6	-9.1	3.6
Manufacturing	19.5	21.2	20.4	-7.9	12.7
Services	25.6	12.2	18.7	-2.8	11.8
Total	21.4	23.0	22.2	-8.8	8.4

Source: Bell, 1992

When examining the individual components of the manufacturing sector, however, these results are seen not to be a true reflection of the export expansion of other sectors (See Table 4). This is because South Africa's natural-resource-based sectors, in particular food products, chemical and basic metals, have traditionally contributed the most to its manufactured exports and hence the export growth rates are largely a reflection of movements in these sectors. Table 4 demonstrates this point, for the annual rate of growth for food products declined from 12.9 percent between 1970 and 1980 to 8.5 percent between 1985 and 1990. Similarly, chemicals declined from 28.3 percent to 5.7 percent and basic metals from 27.3 percent to 7.1 percent during the identical periods. Hence the slower percent experienced between 1970 and 1980 (See Table 3), which was largely due to the deterioration of chemical and basic metal exports, which in turn was due to a worldwide decline in demand in commodity-type exports of the two sectors. On the whole manufactured exports, excluding chemicals and basic metals, actually grew significantly faster in the period 1985 to 1990 than 1970 to 1980. (See Table 4).

Most significant, was the remarkable increase in the export growth rate of the metal products groups of industries, the metal products sector itself, machinery, electrical machinery and transportation equipment excluding motor vehicles (See Table 4).

Table 4

Average Annual Rates of Growth of Exports Valued in Current US Dollars (percent)

	1970-75	1975-80	1970-80	1980-85	1985-90
Food Products	21.5	4.9	12.9	-10.2	8.5
Beverages	16.9	27.7	22.2	-1.1	39.3
Textiles	-1.5	10.1	4.1	2.9	14.6
Leather Products	11.3	13.8	12.5	3.3	14.6
Printing	42.3	-4.5	16.5	-10.7	25.7
Chemicals	18.6	38.8	28.3	-6.4	5.7
Rubber Products	12.6	21.6	17.0	-8.5	20.2
Plastic Products	-4.1	17.0	5.9	-1.2	35.2
Pottery	41.2	-18.1	7.6	-12.2	28.5
Non-Metallic Mineral Products	24.9	15.2	20.0	-19.9	22.7
Basic Metals	11.8	44.9	27.3	-7.1	7.1
Metal Products	21.2	8.8	14.9	-12.6	27.9
Machinery	11.5	17.8	14.6	-10.8	22.6
Electrical Machinery	14.9	16.4	15.7	-11.7	35.1
Transport Equipment	4.8	-3.5	6.7	-6.1	49.8

Source: Bell, 1992

Even though the primacy of manufactured exports as a policy objective was becoming increasingly firmly established by the mid-1980s, the acceleration of export growth in non-traditional exports, was largely due to the fact that the manufacturing sector only exported in times of recession. The problem started in the early 1970s when the South African economy became increasingly susceptible to problems of demand insufficiency (Fallon et al, 1993). The accelerated growth of manufactured exports came at a time where South Africa had experienced adverse foreign exchange shocks, the subsequent devaluation of the rand and the accompanying domestic recession. Manufacturing firms and suppliers alike, were therefore, pressed with declining domestic sales. The recession, thus, not only pushed manufacturing firms into the international export market but also allowed them to get their inputs at internationally competitive prices from suppliers who were forced to lower their prices. According to Holden (1985), subsequent interviews with the main exporters of manufactured goods indicate that on the whole, the South African manufacturing sector has only attempted to export when domestic sales have been falling.

Export expansion did not occur because industry came to accept it as the general way to go, rather, it occurred because exporters had to cover their costs, and finding markets abroad was the only way. According to Bell (1992):

> ".... domestic recession was a significant factor underlying the growth and structure of South African manufactured exports after 1983."

The representatives of most of these exporting firms actually stated that with a recovery of domestic demand, they would not look for export markets and would even have cut down on their existing exports (Belli et al, 1994).

This raises the question of what role government policy actually played in influencing the performance of exports? Compared to export growth in the 1980s, manufactured exports grew relatively rapidly at 20.4 percent between 1970 and 1980, with negligible export subsidies (See Table 3). Between 1980 and 1985, exports deteriorated significantly to -7.9 percent, despite the "new, considerably reinforced system of export incentives", which was introduced in early 1980 on the recommendation of the van Huysteens Committee. With the same system in place, non-traditional exports then increased between 1983 and 1990. The implication is that exports were on the whole determined by other factors rather than the export subsidies. The export incentives involved in the structural adjustment programmes and the GEIS may have contributed to export growth in 1989 and 1990, but there had already been a noticeable increase in a wide range of manufactured exports before these measures were introduced. According to Bell (1992), policy makers were in effect swimming with the tide of a favourable export trend, not created by them.

2.6. Has Trade Policy Contributed Towards Making Industry Competitive?

We have argued in the previous chapter that the attempts made by the South African government during the 1970s to expand industrialization by means of export-led growth, while at the same time protecting and subsidizing capital intensive industries have generally been a failure. These policies, together with the imposition of trade and financial sanctions led to economic and social decline in the 1980s. By the late 1980s it was well recognized that on the whole, South African industry was not internationally competitive and that effectively, South Africa had not successfully made the transition to a more outward-orientated trade regime.

It has already been discussed how the measures that have been introduced to counteract the negative effects of protection, have not been sufficiently effective in reducing the policy-induced anti-export bias. Import substitution has made production for the domestic market more profitable than for exports as these policies have biased producers in downstream, "end-stage" manufactures towards the domestic market and against exporting. Although South Africa has witnessed a resurgence in exports since 1985, much of this export growth has been driven by excess capacity rather than a genuine commitment to profitable exporting (Belli et al, 1993). This has effectively neutralized the stimulus that export activity can provide to the upgrading of competitive abilities, as it has enabled firms to raise prices in the domestic market above those prevailing under free-trade conditions, thus effectively raising the costs of inputs which have increased production costs, and made exporting firms less internationally competitive. Attempts have been made to compensate exporters for the high costs of domestically supplied inputs, but as discussed earlier they have been ineffective. The introduction of the GEIS in 1989 helped, but these export subsidies are excessively costly and the scheme is due to be phased out at the end of 1997, in any case.

Furthermore, South Africa has also foregone many potentially lucrative opportunities by deepening import replacement instead of using the capabilities that had been developed in the early and easier phase of import substitution as a basis for penetrating export markets in consumer goods industries, the route the East Asian countries took. This is not to say that import substitution is a "bad" strategy, as the initial stage did contribute to employment creation and economic growth, but this was largely in consumer goods. Efficient import substitution industries in many intermediate and capital goods, like machinery and motor vehicles, however, require advanced expertise and markets and production runs which are considerably beyond the size of the South Africa economy, which is why import substitution in South Africa can only be seen as a partial success.

Resources have also not sufficiently been diverted towards commodities with low domestic resource cost per unit of foreign exchange, and are predominantly skewed to highly capital intensive upstream sectors of industry. For sure, these industries have become more export-orientated, but their terms of trade are highly correlated with mining and have been declining. As outward-orientated trade strategies are more conducive to building competitive industries, this means that South African industry has not been sufficiently exposed to those forces which can create competitiveness. For activities geared to world markets should benefit the economy by improving productivity performance and by making fuller use of capacity, due to the fact that exporters usually face stronger pressures to develop competitive capabilities in quality and price, than producers relying on the domestic market. International competition tends to encourage capabilities that are more directed to cost reduction and product development. The need to be cost efficient forces firms to upgrade both capital and labour markets, while the need for product development makes it vital for firms to continuously upgrade production techniques by developing or importing new technologies. This technological diffusion and transmission of ideas is extremely important for continued growth, as it is a well documented fact that technical inefficiency in developing countries is an important source of low productivity and poor competitiveness (Pack, 1988).

The entire tariff structure is also problematic. The system is subject to excessive frequent changes, the tariff structure is overly complex, and the dispersion of the tariff schedule is exceedingly high. Additionally, the tariff structure reflects the influence of a "haphazard system that has grown up over time and has no underlying strategy of protecting infant industries during their learning period" (Lall, 1993:60). For a country justifying protection on infant industry grounds, this is a poor reflection of a lack of coherence in trade policy. There has been no policy on the duration of protection and there have been no performance requirements imposed on protected industries. Essentially, South Africa has protected industries regardless of their competitive potential, for as long as a producer could supply at least 60 percent of the domestic market, protection has been granted. As a result, South African firms became used to a state of permanent protection without having to worry about foreign competition. This had the effect of lulling firms into a state of policy induced laziness whereby it was not necessary to have cutting edge technology and hence quality, which inhibited the advancement of other important factors, like the development of skills training.

It is a well documented fact that one of the major causes of lack of competitiveness is high production costs. The effect of import substitution in South Africa has been exactly this, for according to Fallon and da Silva (1994:73), it has meant that the South African economy has "undertaken the production of commodities requiring progressively higher domestic costs per unit of foreign exchange earned". If the basis of exports is the requirement of having an underlying cost competitiveness, it is clear that South African exporters are at a distinct disadvantage. In the South African Chamber of Business document "A Concept for the development of a New Industrial Policy for South Africa" (SACOB:1991), it is argued that the main source of the lack of competitiveness are the high costs of manufactured intermediates, together with high capital and labour costs. According to this document, the cost of manufacturing in South Africa is on average 15 percent higher than the average OECD country. Finally, there has also been little concept of the selective promotion of activities that may have led South Africa's future exports.

2.7. Conclusion

This chapter set out to demonstrate that South Africa's past trade policies have not been effective in facilitating competitive development and have, in fact, detrimentally affected the international competitiveness of its industries. This was demonstrated by analyzing data clearly indicating that past trade policies did not have the desired effect of improving overall growth and hence competitiveness. The conclusion was thus reached that the effectiveness of South Africa's past trade policies were not beneficial to industry, for they were neither related to gains in industrial competitiveness nor effectively implemented.

By 1990 it was generally recognized that South Africa was not internationally competitive and that some major restructuring was in order. It is in this context that chapter three goes on to examine how trade policies have developed in the 1990s.

Chapter Three
A Review of South African Trade Policy in the 1990s

3.1. Introduction

As we have argued in the previous chapter, by the mid-1980s the primacy of manufactured exports as a policy objective was becoming firmly established. This was accompanied by general government consensus for the restructuring and reorientation of industry towards external markets. However, substantial differences arose as to how this was to be achieved. This became particularly clear when the Board of Trade and Industry (BTI) released "A Policy and Strategy for the Development and Structural Adjustment of Industry", which resulted in a major clash with the Department of Trade and Industry (DTI) who had different prescriptions to those advocated by the BTI. It is in this context that this chapter attempts to provide a review of the development of trade policies in the 1990s.

3.2. The Development of Trade Policy in the 1990s

Trade reforms were imminent when in 1990 South Africa became a participating member of the GATT which had set itself the task of eliminating direct controls from world trade as well as lowering tariffs 30 percent across the board for all nations. Having previously opted out of the many voluntary codes of the GATT, South Africa could no longer avoid participation for as Stel Naude, Trade and Industry Director-General at the time, argued, "There is no way that we can reintegrate with the global economy outside of the GATT" (Financial Mail, May14, 1992).

In June of the same year, the Industrial Development Corporation (IDC) released its "Modification of the Application of Protection Policy", a report proposing the reduction of protection.

The IDC saw the current system of protection defective due to the cost raising implications of the relatively high level of protection and the misallocation of resources resulting from the sectoral variation in protection levels (Black, 1992:214). It also identified a number of more specific deficiencies in the system:

- the lack of regular tariff reviews;
- no comprehensive lowering of tariffs;
- the limited scope for further import substitution;

- the selective approach to protection which in South Africa's case meant that protection was on the whole granted according to need rather than potential comparative advantage;
- the administrative difficulties of selectivity;
- the use of excessively high formula duties which had notable cost raising implications; and
- duties imposed to replace quotas and supposed to counter dumping, instead being used against normally priced goods.

It proposed that South Africa put far more emphasis on export growth and less on domestic protection. The major instrument to achieve this would be the reduction of protection, accompanied by measures to encourage exports and supportive macroeconomic policy.

Tariffs would be reduced by the abolition of formula duties and their replacement by more specific anti-dumping measures, and by the gradual downward adjustment of tariffs to pre-determined target level over the next five to six years. The Report recommended a virtually immediate 10 percent reduction on all tariffs of 40 percent and higher and a five percent reduction on tariffs of between 20 and 39 percent. The setting of target rates for tariff levels would be determined by a consultative process with the affected industries and for the most sensitive industries, provisional plans would be made. Infant industries would still qualify for protection at levels similar to those prevailing in more established industries. In exceptional cases, protection would be granted at higher levels, subject of course to phased reduction. Although the Report indicated that protection levels would remain quite high after the reductions, the main instrument of protection would revert to an undervalued exchange rate. Furthermore, it recommended the immediate abolition of import surcharges.

Influenced by the 1987 World Development Report which argues in favour of a neutral trade regime, the IDC argued for a much more uniform and lower tariff structure and opposed selective intervention, by proposing an automatic system that would operate within the overall framework of lowering levels of protection. Despite this, it stated that the existing selective schemes for the clothing and motor vehicles industries, should continue, and that the capital goods and electronics sectors deserved special support, although protection was not the best instrument in providing this.

The Report proposed the expansion of exports through the encouragement of a series of supply-side measures such as lower company tax, encouraging higher domestic savings, a realistic exchange rate, the improvement of skilled labour. The reduction of tariffs would lead to lower subsidies under the GEIS and the phasing out of other export subsidies as well as tax concessions designed to favour exports, with compensation taking place in the form of lower company tax rates. The Report also argued for the implementation of a stable and realistic exchange rate in order to reduce uncertainty and to increase confidence.

The BTI's "A Policy and Strategy for the Development and Structural Adjustment of Industry", discussed in the previous chapter, is seen to differ markedly from the IDC's proposals as to how to go about reorienting industry to external market. For while the BTI envisioned the reorientation of exports towards external markets through export assistance in the form of input cost assistance, the IDC envisioned the implementation of supply side measures to do the job. The BTI rejected the removal of protection, while the reduction of protection formed an integral part of the strategy proposed by the IDC. Yet another substantial difference was the BTI's justification of selective intervention on dynamic comparative advantage grounds, while the IDC outrightly rejected selectivity with some exceptions. . Essentially, however, the view that it was necessary to reorientate industry towards external markets was held in common by both, it was just the means that differed.

According to Black (1993:213), the IDC report "was representative of government thinking". However, when by the end of 1991 no moves had been made to discourage demands for higher protection the question then is posed as to whether this was indeed "representative of government thinking", for a major reason for this lag was a stalemate within government echelons. On the one hand their were those who argued that tariffs could not be reduced until taxes were lowered, inflation reduced and productivity improved, while on the other hand there were those who argued that inflation could not be reduced and that competitiveness could not be enhanced until tariffs were reduced (Financial Mail, August 16, 1991). The excuse given was that the government was still waiting for comment from the South African Chamber of Business (SACOB), who had already indicated that the slashing of tariffs without measures to reduce the high capital costs, tax, interest and inflation rates, would be tantamount to committing suicide.

In September 1991, SACOB released its long awaited report which essentially supported the DTI, but expressed that "a more cautious approach will be required than what is apparent in the IDC Report" (SACOB, 1991:28). Further reservations were expressed regarding the insufficient attention accorded to the transitional costs of adjustment and the abandonment of selective intervention.

By April 1992, almost two years after the government had received the IDC Report and despite the fact that it had received SACOB's reply, no decision had been taken on its implementation. It was becoming evident that although the lowering of tariffs was generally supported, the IDC's Report was a bit too progressive for everyone's liking, including the government's. According to Finance Minister at the time, Derek Keys, the lowering of tariffs should be done "carefully" and not "too quickly if no mechanism existed to retain employment or to re-employ the unemployed" (Financial Mail, April 24, 1991).

The debate provoked by the IDC's recommendations of a phased sharp reduction in tariffs died down and with it the hopes of it ever being implemented, particularly when Key's released his "Normative Economic Model" which omitted any programme of bold reform. For although it was argued that South Africa would only be able to achieve an envisaged GDP growth target by becoming fully competitive in internationally tradable products by creating "smarter industries", it was decidedly vague on any policy guidelines as to exactly how this was to be achieved (Financial Mail, March 19, 1993).

However, the debate was revived in February 1993 when the World Bank released its "South Africa: Economic Performance and Some Policy Implications", a Report arguing for South Africa to reform its costly and unwieldy trade policies. In particular, the report highlighted South Africa's excessively high trade barriers, the detailed and complex tariff schedule and the excessively wide range of tariffs. Additionally, it criticized the strong anti-export bias that was still prevalent and argued for a streamlined and modified rebate system in order give exporters greater access to imported inputs and capital goods at world competitive prices (Financial Mail, March 19, 1993).

At the same time, 1993 was South Africa's turn come under the microscope of the GATT Council. The purpose of such reviews was aimed at creating transparency and understanding of two-way problems and needs, between the GATT and the country under review at the particular time. This entailed the presentation of two reports, one by the GATT secretariat and one by the concerned country.

The secretariat's report for South Africa was published at the beginning of June 1993. Full credit was given for the reforms to normalize the post-apartheid economy with the report welcoming the lowering of tariffs and reduced import controls and the increased emphasis on export promotion and open-market reforms. However, it found that the latter was only being "cautiously pursued" and that the tariff structure and review mechanism underlying it were far from stable or transparent (Financial Mail, June 4, 1993). The implicit message was that South Africa could do better. Despite this, it took numerous revised offers before the GATT accepted South Africa's industrial offer. South Africa finally became bound by all the GATT codes (with a few exceptions) by signing the Marrakesh Agreement in April 1994, thereby making a full commitment to reform the protective system and to reduce protection levels by a third within five years. South Africa's industrial offer became effective from 1 January 1995, coinciding with the GATT becoming the World Trade Organization (WTO), had the following main characteristics:

- The replacement of all quantitative import controls on agricultural and industrial products with *ad valorem* tariffs;
- the rationalization of the 10 000 odd tariff lines into between 5 000 and 6 000 tariff lines, to be completed by the end of the five year period;
- the increase of the 55 percent odd tariff lines bound to the GATT to 98 percent, thus ensuring that tariffs could not be raised without permission from the WTO;
- the standardization of tariff lines from the current 80 different levels of between 0 and 100 percent, into six levels with raw materials and capital goods having tariffs of between 0 and 10 percent, intermediate products-components having tariffs of between 10 and 15 percent, and consumer goods having tariffs of between 20 and 30 percent; and
- the majority of industries having to comply with the GATT programme over the prescribed five years, the exceptions being the clothing and textiles industries which would have 12 years to reach a maximum tariff of 45 percent instead of 30 percent, and the motor vehicle industry which would have 8 years to reach a maximum tariff of 50 percent instead of the 30 percent (Hirsh, 1994).

The GATT recommendations represented an upper limit above which the tariffs could not go ie. a ceiling and not an absolute level. This flexibility meant that the government would be able to set tariffs at a lower level than the GATT ceiling, at the recommendation of the Board on Tariffs and Trade (BTI), which as will be discussed further on, is exactly what happened.

Another notable occurrence in early 1994 was when the National Economic Forum (NEF) commissioned the Monitor Company, international experts in national industrial strategy formulation, to assist South Africa in this area. The NEF constructed a Project Committee, with representatives from business, labour, government, the IDC and the Central Economic Advisory Service (CEAS) which in consultation with the Process Convenors of the NEF managed all aspects of the Project. Hence the Global Advantage of South Africa Project was born.

The first stage of the project was intended to diagnose the current competitive situation and indicate the critical weaknesses that would have to be overcome to increase economic growth. It was not intended to develop specific national policies and cluster strategies, which is to comprise phase two of the Global Advantage of South Africa Project.

Eventually, in April 1995, the Monitor Company released "Global Advantage of South Africa Project, Phase One: National Industrial Strategy Issues", an 83-paged document in which an objective analysis of the South African economy, especially the weaknesses that would need to be overcome in order to achieve international competitiveness, was provided.

The report argued that the principal economic goal of the nation is to provide a high and rising standard of living depends on the nation's ability to achieve high and rising levels of productivity growth. This requires continual upgrading which in turn requires improving productivity in existing activities, moving into higher productivity segments of the industries in which it competes and entering entirely new industries with actual or potential prospects of high productivity.

Accordingly, the Monitor Group Report suggested an alternative path towards improving competitiveness informed by five main factors, namely, factor conditions; related and supporting industries; demand conditions; and strategy, structure and rivalry, the Diamond of national advantage, and finally the role of the government. Factor conditions are referred to as the basic inputs necessary to compete in an industry. Basic factors refer to the resources that are inherited by a nation such as natural resources and climate, or that are created through moderate investment such as unskilled or semi-skilled labour. Advanced factors refer to those resources that are developed through sustained and advanced investment in both human and physical capital, such as modern digital data communications infrastructure, world-class university research institutes ad highly skilled technicians. It is argued that it is the latter that are more important to developing competitive industries and that "a nation's stock of factors at any particular time is less important than the rate at which they are created, upgraded and more specialized to particular industries" (Monitor Group, 1995:9).

Related and supporting industries (the cluster) are referred to in the context of the presence of home-based suppliers and related industries in those products, components, machines or services that are specialized and/or integral to the process of innovation in industry, strongly influence competitive advantage. For not only do they create advantages in downstream industries in various ways, but far more significant is the advantage created by the fostering of close working relationships, the exchange of know-how and the mutual pressures to progress.

Demand conditions are referred to in the context of a demanding market which is what underpins success for the closer a company is to leading edge buyers, the sharper are the signals sent by the firm and its management. Home demand can thus play a significant role in influencing the perception of buyer needs and the capacity of firms to improve their products and services.

With regards to strategy, structure and rivalry, the report maintained that domestic rivalry plays a vital role in achieving international success. Although foreign competition is acknowledged as an important stimulus for improvement, it is argued that it is rarely an effective substitute for domestic rivalry which "provides the essential motivation for firms to make investments and take the risks necessary for competitive advantage" (Monitor Group, 1995:12).

With regards to the role of the government, the report argued that the most productive role of the government is to "improve the quality of the inputs (factors) firms can draw upon and to define a competitive environment and rules of the game that promote innovation and upgrading" (Monitor Group, 1995:13). It is not the role of the government to forge comfortable business-government partnerships, to relax pressures on industry and to seek to eliminate risks. Rather, the role of the government is perceived to be one of a catalyst and a challenger, to encourage and even to pressure companies to improve their competitive performance even if the process entails painful and difficult adjustments.

According to the report, it was asserted that it is the achievement of these five attributes which together with a stable macroeconomic framework create the base for competitiveness and growth. After an overview of South Africa's position in world trade using detailed studies of individual firms and the clusters in which they resided, the Monitor Group concluded that South Africa has what is referred to as a weak "national diamond" with only few strengths. Essentially, however, poor bureaucratic capabilities; poor strategic capabilities; weak clusters; low rivalry and poor skills, machinery and work organization have resulted in high relative costs and/or low quality and service.

The report pointed out that policies like the GEIS, high tariffs, quotas and subsidies have all had a negative impact on international competitiveness, implying that policies have been designed without understanding how competitiveness is created. Furthermore, the administration of policies had been inefficient and rates very low in terms of effectiveness. Although the purpose of the Monitor's Report was to produce the framework for policy and not the specific policies themselves, it nonetheless included some criteria which were seen as the basis for achieving competitiveness. These included strong, co-coordinated clusters;

world-class strategic capability; strong skills, machinery and work organization; high rivalry and a capable bureaucracy

The monitor's analysis appears to be a comprehensible document that shows great potential if it proceeds to the second phase. However, we will have to wait and see if phase two is released as to whether it was taken seriously.

3.3. Conclusion

The purpose of this chapter was to examine how trade policies developed in the 1990s. It was shown that although there was the general agreement that industry should be restructured and reorientated towards external markets, the prescriptions as to how this was to be achieved differed, sometimes markedly. Despite this policy makers have battled ahead with 1995 seeing the implementation of various measures designed to ultimately make industry more internationally competitive. However, certain weaknesses in the area of implementation were revealed and it is in this context that the following chapter goes on to provide a critique of the implementation of these policies by using the clothing and textile industries as a case study.

Chapter Four

A Critique of Trade Policies: The Textile and Clothing Industries

4.1. Introduction

In the previous chapters, discussions and reviews of trade policies has revealed weaknesses in the areas of implementation. This chapter therefore proposes a critique of implementation using the clothing and textile industries, as a case study.

4.2. A Critique of Implementation: The Textile and Clothing Industries

The clothing and particularly the textile industry have historically been accustomed to hiding behind high tariff barriers which has discounted them and other sectors from having to compete against more efficient overseas firms.

Currently, the textile industry is in a serious predicament, the roots of which lie in import substitution policies implemented in 1963. Between 1963 and 1974, the policies worked very well with the average annual growth in textile products reaching 9 percent per annum. However, since then the industry has been in decline. Between 1975 and 1983 rates fell to 3 percent per annum and to a further 2 percent by 1991. Between 1991 and 1993 the figure had reached a dismal -2 percent per annum (Weekly Mail and Guardian, July 15, 1994).

Initial moves were made in the direction of reform in 1989 when the textile and clothing industries both agreed upon a five-year tariff reform plan. However, the textile industry, accustomed to high levels of protection, delayed implementation. The clothing industry on the other hand continued to push for low tariffs on textiles so that they could make clothing as cheaply as possible. In April 1992, the clothing and textile industries were granted interim protection in order to adjust and to make changes in preparation for the introduction of tariff reforms. However, by September 1993 large sections of both the clothing and textile industry had not taken advantage of this respite for "they had neither adjusted nor attempted to make any changes in order to face the reality of the international textile trade in the next five years" (Financial Mail, September 3, 1993). According to Textile Federation President, Mervin King, however, there was no need to accelerate the commencement date of the phase-out period for tariffs, or to apply a shorter period than eight years to any sector of the textile pipeline.

In the same year, a working group chaired by the Board on Tariffs and Trade's Nic Swart was commissioned to devise a new long-term strategy for the two industries.

However, the report was more an industrial strategy outlining how the government could help the industries upgrade their technology, training and productivity, reduce costs and compete globally, and did not include recommendations on the tariff issue. In fact, the industries were granted yet another interim one-year period, which became effective from November 1 1993. According to Swart, however, during this period, "the industries would continue their discussions and various committees would be looking into the problem areas" and "the long-term tariff policy together with the new industrial strategy should be in place by January 1, 1995" (Financial Mail, September 3, 1993).

In April 1994 the "good times" well and truly became something of the past when the textile industry was forced to face the real world of the GATT, higher competition, strained profit margins and much-needed improvements in efficiencies. However, indications were not good, particularly when the textile industry started to attempt to obtain concessions to delay the implementation of the GATT. It became evident that the textile industry, so used to getting its own way in the past, was "not changing strategies or even recognizing that these could affect their companies" (Weekly Mail and Guardian, July 15, 1994).

In July 1994, Swart's working group finally came completed the long-term strategy with recommendations that were accepted by the industries as well as their trade unions. They included:

- the phasing down of duties on imports over 10 years;
- the extension of the Duty Credit Certificate System and the GEIS; and
- government support in the form of low-interest Industrial Development Corporation (IDC) loans for upgrading technology and improving skills and assistance for export ventures. (Finance Week, July 29-August 3, 1994).

The government's view that the industry could do a lot better, however, came across clearly when the then Minister of Trade and Industry, Trevor Manuel, criticized the industries expectations of extended periods of grace for tariff reform together with huge financial assistance from the state (R4.2 billion), to see it over the long adjustment period (Financial Mail, September 2, 1994).

Industry experts also expressed concern at the demands of a ten year phase-down period, particularly as a ten year period was regarded to be virtually the equivalent of two technological life times. Furthermore, doubt was expressed as to whether the textile industry was actually prepared to face international competition, particularly without substantial tax breaks from or the government propping up the market. As if to reinforce the view that the days when manufacturers could rely on government intervention were over, 1995's budget announced the elimination of import surcharges.

Eventually the government's final proposals for the clothing and textiles industries was for a seven-year phase-down period implemented in September 1995, without the extension of the GEIS and the Duty Credit Certificate System and without the high degree of government intervention envisioned by the industries. It was argued that it was not the purpose of the proposals regarding restructuring to drive companies out of business but rather "to serve to make a break with the past in policy-making; they are negotiated, and place South Africa beyond the exclusive reliance on tariffs as the policy instrument" and that instead "we have developed new instruments which focus on supply side measures such as human resources development, work organization and technology enhancement" (Weekly Mail and Guardian, June 15, 1995). However, noticeable was a lack of clarity of what precisely these supply side measures would be.

The National Clothing Federation had proposed that protection on textile fabrics be phased out more quickly in order to give clothing manufacturers the time to acquire a competitive export footing by having their input costs reduced. This was rejected even though in a budget speech Manuel had criticized input suppliers who practiced import parity pricing behind high tariff barriers, implying a gap between what the government would like to do and what it actually does. However, it has been suggested that Manuel was more lenient on the textile industry because of its proposed R3 billion investment plan to upgrade archaic and globally uncompetitive equipment, in line with the view that there is a general need for re-investment and the upgrading of plant and machinery to the standards of foreign technology (Financial Mail, June 23, 1995).

The government's final offer came as a big disappointment to the industries with, the Textile Federation together with the SA Clothing and Textile Workers Union (SACTWU) arguing that tariff adjustments would be meaningless without other changes and that "the phase-down must be postponed until the necessary supply side measures are devised and implemented" without which "we will have no strategy and just a seven-year duty phase-down" (Financial Mail, August 18, 1995). The supply side measures that were envisaged included:

- an export incentive package to compensate for the abolition of the GEIS and the Duty Credit Certificate System;

- training support measures with the government providing 50 percent of the cost; interest rate subsidies to equalize South Africa's high rates with much lower rates in competitor countries; and

- a social restitution program to train and assist workers loosing their jobs as the industry upgrades itself and reinvests in modern technology.

It was emphasized that these measures would not be handouts but assistance schemes on the condition that industries increase productivity and meet export targets. However, apart from a R5 million per annum management consultancy subsidy and a small working group looking into other general measures, Trevor Manuel had already indicated that the government had no funds for such measures.

Although the National Clothing Federation argued that it would be unreasonable for the government to grant yet a further reform extension, it was also concerned by the supply side measures issue, particularly with regard to the failure to extend the Duty Credit Certificate System (DCCS) to the import of material for the manufacture of value-added clothing, a system which allows clothing and textile exporters a 30 percent credit against any future import tariffs, based on the value of exports. This caused much discontent, especially as the clothing industry had been identified by the GATT as the trade sector with the biggest global growth potential due to the fact that value-added business was one of the fastest growing sectors. However, on cue the government then decided to extend the scheme for a further three years.

Furthermore, it criticized the government's failure to control the widespread illegal import of clothing and textiles that was flooding the industries, due to lax customs controls. Government proposals to let Zimbabwe export clothing and textiles to South Africa at preferential tariff rates just exacerbated the issue as it raised the fear that the Zimbabwean border would become an open door for even more illegal imports to flood the industries (Financial Mail, September 1, 1995).

South Africa's anti-dumping system has in fact been the subject of much debate and criticism from:

> "local industries and unions who believe the system is not responsive to concerns about unfair imports that are causing material injury, particularly in the face of liberalization and lower tariffs; foreign exporters and importers who believe the system is administered in a way that is protectionist; and trading partners who are concerned about it's inconsistency with international rules and practices" (Weekly Mail and Guardian, March 22, 1996).

In response, the Board on Tariffs and Trade (BTT) was urgently requested to investigate and make substantive recommendations on the restructuring of the anti-dumping system.

Apart from this, the issue of supply side measures has not abated, particularly with regard to how the restructuring of the textile industry will be financed. These fears were allayed when in the 1996 budget Chris Liebenberg announced that R180 million would be set aside for supply side packages for the entire manufacturing spectrum, a far cry from the R4.2 billion that was envisioned only for the clothing and textiles industries proposed by Swart in 1993 (Weekly Mail and Guardian, March22, 1996). The Textile Federation dismissed it as an insignificant amount. SACTWU's Ebrahim Patel agreed with the Textile Federation, arguing that subjecting the industries to the market before restructuring has taken place was equivalent to abandoning it, and that instead "the industry should be restructured along three pillars: active industry policy measures to improve technology, quality and training; trade reforms to gradually liberalize tariff barriers and promote exports; and a social adjustment programme to retrain workers" (Weekly Mail and Guardian, March 22, 1996). What the government has done instead was just to phase-down import duties with only vague mentions of supply side measures. According to a SACTWU survey, an analysis of over 200 companies shows that between September 1995 and February 1996 close on 20 000 jobs had been lost in the clothing, textiles and leather industries and that another 100 000 jobs are estimated to go as a result of the seven-year phase-down period.

To date, pressure for the implementation of supply side incentives has not abated. In May of 1996, submissions were made to the government on investment-led growth and development options in the clothing and textiles industries. The views were wholly supported by SACTWU who once again emphasized that "tariff reduction on its own does not constitute an effective industrial policy" and that it "needs to be accompanied by a range of supply side measures and social support during the restructuring process such as worker skills and technology" (Financial Mail, July 26, 1996).

The government has however proceeded full speed with liberalization and have proposed various changes which are arguably meant to improve the competitiveness of South African industry. It is this area to which we turn in slightly greater detail.

4.3. Tariff Liberalization

The reduction of protection is finally well underway in the clothing and textile industries with the government's seven-year tariff phase-down period for the industries implemented in September 1995. Furthermore, general progress towards an outward orientated stance is reflected in a number of achievements, namely, the replacement of former quantitative restrictions with tariffs, the rationalization of the tariff structure by almost halving the number of tariff lines, the abolition of surcharges in September 1995, the phasing down of tariffs which for the majority of industries began early on in 1995 and the phasing out of the GEIS which is to be completed by the end of 1997.

What about the effectiveness of tariff reductions thus far? According to a document released by the Department of Finance in June 1996 and the government's main macro-economic strategy "Growth, Redistribution and Employment, a Macroeconomic Strategy" (GEAR), at the sectoral level the evidence is mixed. Among the sectors facing the largest declines in nominal protection, some increased both output and employment, while others showed the opposite trend (Gear, 1996:47). It should, however, be noted that the five sectors facing the largest tariff reductions in 1995 account for only 17 percent of total manufacturing employment. Those sectors which are major employers namely food, clothing, motor vehicles, electrical machinery and metal products showed that despite tariff cuts a range of firms managed to expand output and employment. (See Table 4). Thus far, preliminary indications are that the potentially negative effects of liberalization have been kept low, partly as a result of the economic recovery and a resurgence in exports, with the recent depreciation of the rand shifting relative prices in favour of exporters.

Table 4

Changes in Tariffs, Output and Employment, 1994 - 1995 (in percent)

	Employment	Output	Exports	Imports	Tariff Changes
Food	-1.5	0.0	25.8	26.1	15.4
Beverages	-5.8	5.7	-11.8	22.2	64.3
Leather Products	3.6	7.0	15.0	10.2	-78.7
Wood Products	-5.1	4.8	-16.2	18.2	-20.0
Paper Products	4.8	10.9	71.0	35.7	-40.0
Printing and Publishing	2.1	-3.9	12.1	12.5	-81.9
Glass products	-3.9	6.6	-14.5	26.8	-52.9
Other Non-Metallic Mineral Products	-7.1	9.1	29.0	37.8	-50.0
Iron and Basic Steel	0.8	14.0	22.9	28.6	-72.7
Non-Ferrous Metal	-3.4	17.9	119.3	122.9	-16.7
Metal Products	-2.2	5.4	55.1	29.8	-56.3
Machinery	13.1	12.5	66.8	2.5	-77.8

Electrical Machinery	-3.0	23.4	58.7	32.3	-58.8
Motor Vehicles	9.4	15.8	19.1	41.0	-62.5
Other Transport Equipment	-4.9	-14.2	N/A	N/A	0.0
Other Industries	-3.5	-11.7	-6.7	-18.6	-12.5
Tobacco	-6.7	-2.3	69.8	-8.1	110.0
Textiles	-7.6	12.0	16.5	15.8	-7.9
Clothing	9.9	14.1	18.0	-8.7	-4.1
Footwear	7.6	5.7	2.6	40.6	20.0
Furniture	6.3	8.5	39.2	37.6	-40.0
Chemical Products	-1.4	6.4	43.7	28.5	-36.4
Rubber Products	7.6	8.6	58.3	31.3	-71.0
Plastic Products	14.6	10.2	49.7	28.4	-81.0
Total Manufacturing	1.1	7.4	33.7	27.5	-5.6

Source: Growth, Employment and Redistribution, a Macroeconomic Strategy. 1996

It appears then, that to all extent of purposes, reduction in protection has been successfully implemented and that although various industries are not having an easy time, government is not succumbing to lobbying pressures to slow down the process. In fact, as a result of the current real depreciation of the rand, the government is pushing for a compensating lowering of tariffs. Although stating that they will be implemented in such a manner so as to lower prices for industrial inputs and low-income households, avoid job losses in sensitive sectors and to remove price distortions in domestic markets, extreme caution should be adopted in assessing the potentially negative impact that these faster reductions may have on the economy. The words of Trevor Bell (1992) should be heeded in this case, who as early as 1992 was questioning whether it was necessary for South Africa to further liberalize its foreign trade. He noted that a major consideration with regard to further import liberalization through tariff reductions was that without a measure of macroeconomic stability such measures could pose serious problems for the economy. He concluded that "comprehensive tariff reductions must await a substantial improvement in the performance of the economy, so that they can be implemented without the danger of foreign exchange or fiscal crises, or intolerable effects on output and employment in import-competing industries" (Bell, 1992:34).

Although the reduction of protection has gone relatively smoothly, a significant complaint, not only from the clothing and textile industries, is that the phase-down of tariffs has not been accompanied by enabling supply side and other support measures, the area to which we now turn.

4.4. Supply side and Other Support Measures

A valuable lesson that can be drawn from the experience of the NICs is that without the complementary measures the correct general trade orientation does not amount to much. These not only included tariffs, quotas and subsidies but importantly supply side measures "aimed at securing competitive advantage through attracting investment and technology into specified sectors, thus accelerating productivity growth and technical change " (Black, 1993:217).

It goes without saying that it is vital to strengthen a country's human capital base in order to promote the growth of technological capabilities. This includes both pre-employment education as well as on-the-job training and further formal training of employees sponsored by the private sector. This does not come about on its own and many governments accept the role that they must play to support the education system. The NICs, for example, clearly demonstrate that their industrial success depended to a large extent on the creation of human capital by extensive and continuous investments by the government.

It is also not only the volume of investment in education that is important, as the quality and relevance of the education is just as significant to industrial development. Unfortunately, especially in developing countries, the private sector invests relatively little in upgrading skills. According to Lall (1993), this may be due to three reasons. Firstly, the failure to be fully aware of the skill needs of the technologies being used. Secondly, not having access to skills training facilities despite enterprises realizing that skills are deficient. Finally, enterprises who are not sure whether they will be able to recoup the full benefits of their investments and hence are not be willing to investment large amounts in the upgrading of skills.

It is essential that the development of technological capabilities also form an integral part of the supply side measures implemented by government. This development can only effectively take place if firms can access the formal and information technology networks that exist between firms and between firms and research and other institutions. Unfortunately a serious problem in many countries with the science and technology infrastructure is the lack of effective linkages with the productive sector (Lall, 1993). As a result, although most countries do have networks of technology institutions the inability of mostly developing countries, especially, to harness them means that they have been unable to raise productive efficiency in industrial enterprises. It is thus up to the government to design policies which link them intimately to the needs of manufacturing enterprises.

The term supply side, however, does not only include capability development. The document, "Support Measures for the Enhancement of the International Competitiveness of South Africa's Industrial Sector" (1995) submitted by the Trade and Industry Chamber of Nedlac demonstrates the point. Apart from proposals to enhance technology and the need for active government policies which will help increase investment in human capital, a number of other proposals are put forward. Among other things these include assistance to sensitive industries, assistance packages to competitive industries who have invested in their own competitiveness in the past, concessionary finance for specific policy aims, incentive packages which should ideally lead to viable ventures being undertaken which would never have been undertaken without the incentives, and a shift from grant-based incentives to selective tax incentives (Financial Mail, November 24, 1995).

I have discussed the concept of supply side in relative detail because the new approach to trade and industrial policy in South Africa is the shift away from demand side interventions like tariffs and subsidies which in the past have raised the price of outputs, to supply side measures designed to lower the cost of productivity enhancing investments and to expedite progress up the value chain. In the government's GEAR, this shift to supply side measures is emphasized.

In the area of concessionary finance, it mentions that the IDC will continue to provide loan finance, equity and credit guarantee facilities and will adapt its programmes to satisfy new needs, while the Regional Industrial Development Programme (RIDP) has been expanded to include a simplified scheme applicable to smaller enterprises (Gear, 1996:11 & 12).

In the past the IDC was actively involved in providing equity and loan capital for massive new projects which were initially encouraged by tax concessions introduced in late 1991, which were recently been stopped. These allowed for write-offs of capital expenditure on machinery and installations beginning in the year that it was incurred rather than when production began. To qualify for these concessions, however, projects had to be on a scale which made it internationally competitive, by adding a minimum of 200 percent to the value of the product as well as exporting at least 60 percent of it.

The IDC, for example, has recently assisted Hulett Aluminium with a R2.5 billion hot-and-cold aluminium milling facility and Alusaf with a R5 billion aluminium smelter thereby making it the seventh largest producer in the world (Black, 1993). Although in the long term this kind of capital intensive investment, which if the industry is successful, earned substantial amounts of much needed foreign exchange which would in turn strengthen the balance of payments and the gold and foreign exchange reserves, a major concern is that such highly capital intensive investments will create little direct employment. However, these additional strengths would make it possible for more expansionary macroeconomic developments to take place, which would necessarily include a whole host of labour-intensive low-tech industries. Additionally, the sophisticated industry would generate other employment from suppliers and from services both to the company and its employees (Finance Week, July 8-14, 1993). The implication is that although employment gains would initially not be great, they would not only improve over time, but also be long lasting.

The recent signing of a 10 year metal supply contract between Alusaf and Hulett Aluminium, for example, is likely to provide the impetus for substantial growth and development of the downstream aluminium industry. It is this kind of endeavor that should be encouraged by the government, for not only is it a step further up the beneficiation ladder (added value), but it is also likely to expand the potential market for fairly labour-intensive products.

It is thus important for the government to have a clear strategy with regard to downstream development. This should form part of a long term development plan for industry as a whole. It goes without saying that this cannot be done without equal participation by all affected parties. The phasing out of this capital cost write-off is an example of a lack of clear cut policy, for it is actually an effective incentive. Take for example a most recent case concerning the wool textile industry. With world demand currently building for wool-based clothing, and with South Africa beneficiating only 10 percent of its wool crop and exporting 90 percent in its raw form, it is not surprising that the industry has realized the huge potential. In fact, it has estimated that if the total output of wool was beneficiated into manufactured garments and exported this would increase exports to about R15 billion as opposed to the present export value of R1 billion, as well as providing employment for a further 400 000 people. But "the high capital cost of building a world-competitive worsted textile plant, with state-of-the-art technologies and expensive machinery", according to chairman of SA Fine Worsted, Malcolm Hughes, "requires an incentive package" (Financial Mail, May 17, 1996). Accordingly, incentives were proposed by the industry which included corporate tax rates at 10 percent, 8 percent fixed interest loans (for 15 years) from the IDC, duty-free import of production plant, equipment and inputs, a 100 percent investment allowance in all new plant and machinery, and accelerated depreciation.

However, the government appears to have got the message for in GEAR, measures to stimulate competitive and labour absorbing industrial development were indeed mentioned. Apart from these schemes introduced by the IDC, other measures included an accelerated depreciation scheme which would be introduced for all new investments in manufacturing; the tax allowance programme which would apply to qualifying plant and equipment which is acquired and brought into use for the first time during the period from July 1 to the end of September 1999; the replacement of the Regional Industrial Development Programme (RIDP) by a tax holiday available to completely new pre-approved projects initiated during a window of three years. This would begin in the last quarter of 1996. with approved projects getting tax exemptions for a period of time determined by regional allocation, job creation and priority industries. The tax holiday would come into effect as soon as the project became liable for tax, not to be used beyond the tenth year after the initial investment is undertaken (p.12).

Closely related to this are the twelve industrial priority industry investigations as well as the regional industrial locational studies with the aim of identifying mechanisms to enhance the competitiveness of selected industrial sub-sectors which may be eligible for the proposed tax holiday, while specific interventions would be considered when necessary.

Only time will tell whether these measures are effective in stimulating competitive and labour absorbing industries, but at least it appears as if government has realized the importance of encouraging endeavours such as that proposed by the textile wool industry.

In the area of technology and training, GEAR refers to various industrial innovation support programmes. These include the incentive in terms of the Special Programme for Industrial Innovation, the matching grants under the Technology and Human Resources For Industry Programme which is designed to strengthen the relationship between educational institutions and industry, and the technology transfer programme of the DTI which is to be converted into an agency dedicated to facilitating access by firms to needed technologies.

However, in a document released by the National Institute for Economic Policy (NIEP), "From the RDP to Gear: the Gradual Embracing of Neo-liberalism in Economic Policy", the proposed "enhancement" of industrial innovation support programmes is criticized for a lack of detail (NIEP, 1996:15). It is crucial that this form an integral part of industrial strategy with extensive and continuous investments by the government. This is particularly significant in light of the fact that the development of technological capabilities in South Africa has been poor and is in a state of decline. Strong in scientific research, South Africa is far weaker in technology application. Although a more outward-orientated trade regime and a restructured import regime will most likely be associated with enhanced investments in technology there is no automatic link between trade orientation and the development of technological capabilities. To improve the chances of this happening, however, extra government support is a necessity.

According to Joffe et al. (1993), there is a need for specific policy interventions designed to:

- reverse the current decline in overall national expenditure on R&D and, in particular the decline in business expenditures on R&D;
- strengthen the incentives to firms to invest in the development of in-house technological capabilities;
- affect the terms of technology transfer;
- restructure the funding and other incentives that currently affect the operations of the system of statutory science councils;
- encourage links between the universities and manufacturing industry; and
- identify and acquire capacity in significant future technological developments.

Certainly some of these issues have been addressed. Additionally the textile industry's proposed R3 billion investment plan to upgrade capital technology is encouraging. However, the necessity for the government to invest in the enhancement of technological capabilities cannot be overemphasized, for it plays a crucial role in the development of internationally competitive industries. It is thus important for the government to pledge a full commitment by designing policies that address the source of the problems.

It has already been mentioned that an important element to the success of industrial development in the experience of the NICs was extensive and continuous government investment in the enhancement of human resource development. In assessing the stance of the government towards the issue it appears as if it is high on their list of priorities. In 1995 Manuel went on about the development of new instruments "which focus on supply side measures such as human resources development, work organization and technology enhancement" (Weekly Mail & Guardian, June 15, 1995, Internet). In GEAR, "enhanced human resource development" (p. 2) is mentioned as one of the factors that will contribute towards the expansion if the economy.

As mentioned earlier, Gear mentions the matching grants under the Technology and Human Resources For Industry Programme designed to strengthen the relationship between education institutions and industry. However, in a world where it is becoming apparent that intra-firm education, various forms of supplementary adult education and industry-wide training are a primary requirement in industrial competitiveness, is this sufficient to reverse the drops that have been experienced in training as well as in the attempts to re-train the unemployed? It is clear that some sort of nationally integrated system of training which links different levels of training and education system is going to have to be established, so that "workers will be afforded the potential to proceed along a career path to which modules of accredited training contribute (Joffe et al. 1993:112). Furthermore, the past failure to invest in training must be extensively analyzed so that recommendations can be made to rectify the situation. This would mean the development of some sort of communication network between firms, education institutions and the government in order for firms to be fully aware of the skill needs of the technologies they are using, to be able to effectively remedy deficient skills, and being confident that they will recoup the full benefits of their investments. Simply strengthening the relationship between educations and industry is only partially addressing the problem, especially as it is the attitudes of the business sector towards the participation and development of its labour force which needs fundamental altering. Certainly, the exposure to higher levels of international competition are bearing fruit as both the business sector and the government are realizing the importance of human resources development in contributing towards the development of industrial competitiveness, but focus must now be on designing a national strategy as soon as possible, before South Africa falls even further behind.

Noticeable in GEAR however, is the lack of detail as to the extent of its involvement in developing human resources. This is one area that needs extensive public sector involvement. In fact, I would go as far as to assert that the government must lead the way with significant support and even pressure, for firms to invest extensively in employee training. If this does not happen the private sector is extremely likely to underinvest and not capitalize. However, at the same time the government cannot expect the entire burden to fall on the private sector. This means that it is going to have to put an end to the chronic dissaving that is so prevalent in government echelons in order to ensure that some resources can at least be diverted to investing in the development of human resources.

4.5. Selective Intervention

Although it appears that selective intervention is on the agenda, not much is elaborated on the twelve industrial priority investigations mentioned in the GEAR.

The experience of the NICs has demonstrated that the targeting of support rather than a neutral trade regime was the key factor in attaining new areas of international competitiveness. South Africa has to a large extent been scarred by protection which was not linked to the attainment of international competitiveness and improved productivity. However, this should not deter from the fact that if protection is used with these goals in mind, it can be successful. This is once again demonstrated by the strategy used by the NICs who unlike classic import-substituting economies which generally use protection indiscriminately, very much like South Africa, used limited protection by promoting a few activities at one time.

The message is clear. If a government is looking at creating new areas of comparative advantage through state intervention, or protecting infant industries:

> "assistance needs to be targeted at a limited number of sectors and must be based on the principle of reciprocity, with stipulated requirements in terms of performance objectives, productivity gains, export targets, new investment, employment creation and the like" (Black, 1993:224 & 225).

Furthermore, it is essential that the main goal is improved competitiveness and productivity. A good example in this case is South Africa's electronics sector which has far weaker domestic capabilities than most other economies at its income level (Black, 1993). A measure of import substitution could assist the sector in improving its performance, but it is absolutely crucial that it is done in such a way that the top priority is to become competitive in world markets within a specified time frame.

Although selective targeting can result in misguided intervention and large scale rent seeking behavior and corruption, this need not to be the case if stipulated requirements such as those mentioned above are effectively implemented. Additionally, it is crucial that retribution measures are taken if firms do not meet the requirements, for leniency simply leads to exploitation and increasing lobbying. South Africa especially, cannot afford firms to once again become used to a complacent way of life.

Closely related to the misperception that import substitution cannot be used as an effective strategy in the short-term, is the assumption that reduced trade protection will automatically see the rise of new and/or expanded internationally competitive industries and export expansion. See Strydom (1994), Cline (1982), Black (1993), Edwards (1993), Agosin (1993) and Joffe et al. (1993). This misperception is based on two assumptions. Firstly, reduced prices for imported goods will reduce overall production costs. Although this is self-evident, it should be noted that the same result can be achieved by other methods (Black, 1993). Additionally, Helleiner (1990) points out that domestic prices will not fall given the possibility of formerly oligopolistic producers becoming importers with market power.

Secondly, is the assumption that firms will respond to foreign competition by becoming more efficient and competitive. However, exposure to foreign competition is a double edged sword. For as Bell (1990:17) points out, it "can just as easily kill off certain industries as spur them to greater heights of efficiency and competitiveness". Import liberalization itself does not automatically lead to improved competitiveness and export expansion, but has to be accompanied by efficient allocation and measures to reduce the potentially negative impact of the costs of adjustment.

Outward-orientated policies are simply not sufficient to shift an economy to higher levels of growth. Appropriate supply-side measures, which address the issues of productivity, technology and other factors are crucial to export success. For this secures competitive advantage through attracting investment in the development of human resources and technology and thus accelerates productivity growth and technical change. Without this, a country is unlikely to effectively improve its export performance.

4.6. Customs and Excise Control

A major concern to so many industries is the issue of South Africa's flawed system of customs and excise control. As mentioned in the previous chapter, thus far the government had failed to control the flood of illegal imports into South Africa. Amongst the most hard hit are the clothing and textiles, electronics, tyre, music, edible oils, pharmaceutical, drugs, arms, vehicle spares and liquor industries.

At the moment, the Customs and Excise Act allows a company accused of import fraud to plead guilty and be fined, but the matter never comes to court, the company is not convicted and not even its name may be revealed, as this would constitute an invasion of privacy (Financial Mail, December 22, 1995). Perhaps it is time that a more hard line approach is taken where the accused is brought to a court of law, after all import fraud is an illegal act. A stance has to be taken wherein the message is clear that offenders will simply not be tolerated.

At the source of the problem are the high levels of staff demoralization and corruption. The administration of an extremely complicated and irrational tariff system which hinders the effectiveness of anti-dumping mechanisms and which leads to misdocumentation coupled with a lack of basic technology, simply exacerbates matters. As a result, of the containers that enter South Africa only a tiny proportion (between 1 and 3 percent) can be examined. Durban is the main culprit, being responsible for overseeing more then 70 percent of South Africa's containerized goods. However, less then 1 percent of the containers entering South Africa via Durban are actually inspected (Weekly Mail & Guardian, March 22, 1996). Additionally, the break down in customs policing has become so severe in sectors like clothing, textiles and electronics, that some companies have resorted to hiring private detectives to protect their interests. The situation has grown so bad that a private sector initiative, the Customs and Vat Enforcement Caucus representing the most hard hit industries, has been set up which aims to stop the flood of illegal imports into South Africa. The Caucus has recently been given permission by cabinet to work closely with the police, Inland Revenue, Customs, Trade and Industry and the Reserve Bank's exchange control division to prosecute offenders. The number of death threats that have been received by members, and the commonplace bribes and corruption amongst government-employed officials gives substance to the fact that illegal importing is big business in South Africa.

Other initiatives include the National Business Initiative, a private sector body that is advising the government how to combat crime, as well as the Clothing Federation attempts at setting up codes of conduct with unions to try and ensure that all prescribed duties are paid on goods (Financial Mail, April 12, 1996).

It is clear that there has been a decided lack of active government involvement in the area of customs and excise, including its Customs and Excise and Inland Revenue Agencies. Recent events, however, indicate that at last "the slumbering giant appears to have come out of its coma" (Financial Mail, April 12, 1996). The government has appeared to have overcome budgetary restraints and has been able to harness financial assistance and expertise from the private sector. It has allocated a substantial R1.1 billion to the new SA Revenue Service, an amalgamation of Customs and Excise with Inland Revenue. This money will be used to overhaul the entire system with short-term measures including new border posts, more customs officials and tax inspectors, the upgrading of computer systems, mechanical sniffers and scanners.

Furthermore, South Africa's anti-dumping laws are presently being investigated with a potential area of amendment being the separation of the functions of the tariff setting and anti-dumping determinations, with further changes potentially including the shortening of the time frames in anti-dumping investigations and the aligning of South Africa's anti-dumping laws with the provisions of the World Trade Organization (Werks News Desk, 1996).

Considering that an estimated R2 billion is lost in Customs and Excise duties each year, excluding the associated Vat fraud and lost opportunities, these reforms are long overdue. It is, however, imperative that resources are allocated efficiently and that some sort of national strategy is developed consistent with international rules and practices.

4.7. Conclusion

This chapter set out to critique implementation by using the clothing and textile industries as a case study. It demonstrated that the restructuring and development of industry is without question a mammoth task, one which is going to require active but effective government involvement in the process. This was done by discussing how implementation has taken place within and how it has affected the clothing and textile industries. In so doing the contentious supply-side issue and that of the widespread illegal import of clothing and textiles, was mentioned with the implication being that government was not showing signs of clear direction. It was in this context that the chapter went on to analyze in more detail how the government was handling these issues. This was done by discussing the governments macroeconomic strategy in detail.

It was concluded that although a national industrial strategy is slowly taking place, there is still a lack of clarity on this matter, and it is essential that government ensure that any present and future measures never deviate from their goal of achieving improved international competitiveness and productivity in order to provide jobs for the majority of impoverished South Africans.

Chapter Five
Conclusion

5.1 Introduction

This study set out to assess the significance of trade policy in promoting the international competitiveness of South African industry. It covered the following areas: a review of the debates surrounding international competitiveness; a background of South Africa's trade policies; the development of South Africa's trade policies over the last six years; and a critique of implementation using the clothing and textile industries as a case study. This was necessary in order to demonstrate the centrality of trade policy in promoting the international competitiveness of South Africa industry. The following section discusses the individual chapters in greater detail.

5.2. Summary of the Arguments

Chapter one provided a review of the debates surrounding international competitiveness, assessing the theoretical arguments for the state, markets and international competitiveness in attaining international competitiveness. The centrality of trade policy was established by demonstrating that effective government intervention can promote international competitiveness.

In this context, the chapter then went on to discuss the trends in the world market that South Africa is re-entering and the implications thereof. It was argued that in order for South Africa to find a niche in the current world economic order, it would have to design policies consistent with trends in international trade. Furthermore, South Africa would have to develop an intimate understanding of its own needs, interests, it's priorities and how to pursue them in order for it to be able to truly become part of the international world of trade.

In Chapter two it was demonstrated how trade policies can influence international competitiveness. This was done by examining the effect that South Africa's past trade policies had on the international competitiveness of it's industry since the early 1970s up until 1990. It was argued that these past trade policies were not linked to the attainment of international competitiveness and improved productivity and were thus responsible for the difficult problems with regards to industrial competitiveness, restructuring and the reorientation of industry towards external markets that South African industry is presently faced with.

Chapter three provided a review of how South Africa's trade policies have developed in the 1990s. It argued that although their was general government consensus that South African industry was internationally uncompetitive and was in dire need of restructuring and being orientated towards external markets, the means as to how this was to be achieved differed markedly. This was demonstrated by referring to various key documents clearly showing that the development of trade policies has been an uphill battle. Together with chapter two, chapter three revealed weaknesses in the area of implementation.

Chapter four provided a critique of the implementation of these trade policies by using the textile and clothing industries as a case study. It was shown, particularly in the case of the textile industry, how reforms were initially resisted, but how the signing of the Marrakesh Agreement heralded an era where industry would have to reform or die. Furthermore, it showed that although industry had accepted the inevitability of reform, much discontent was expressed at the government's lack of clarity with regard to the supply side measures issue which it had promised to implement, as well as the widespread problem of illegal imports. It was argued that the reduction of protection did not amount to much without these issues being addressed. This led to an analysis of how the government was handling these issues which was done by discussing its macroeconomic strategy in detail.

It was concluded that, although the government was moving in the right direction, there was still a lack of a coherent industrial strategy which appeared to be rather fragmented. Furthermore, not enough was being done by the government and an increasing burden was falling on the private sector, such as investment in skills training.

In conclusion, the debate therefore demonstrates a number of things:

- That South African industry has traditionally been overprotected which has manifested as industrial laziness, low productivity and overall uncompetitiveness.
- That even when the necessity of trade policy was recognized, implementation was quite lax.
- That the transition to democracy in South Africa and the changing nature of the global economy has fostered global competition on the agenda and South African business, labour, the government and academics have started debating these issues. This debate clearly demonstrates that it has been recognized that trade policy is crucial to global competitiveness.

Hence, despite the difficulties that lie ahead, in the long term internationally competitive industries and all the factors that go into making them, will assist in providing sustainable economic growth which will in turn improve the lot of many South Africans and South Africa as a whole. The effectiveness of trade policies in promoting international competitiveness, therefore, cannot be overemphasized. The challenge which faces the government is thus to ensure that future trade policies promote the international competitiveness of South African industry.

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