What if South Africa had a special economic zone **that was actually special?**

Executive Summary

Following considerable work on SEZs by CDE over the past decade, we hosted a roundtable involving some of the world's leading SEZ experts and practitioners in November 2019. This report sets out what SEZs could offer South Africa in the country's quest to achieve faster employment growth. The landscape of debate about SEZs has changed, with new voices including the National Treasury, the ANC, Kgalema Motlanthe's High Level Panel and Joel Netshitenzhe increasingly expressing interest in implementing an SEZ that is focused on attracting firms engaged in the production of labour-intensive goods and services for export.

South Africa's economic woes are deeper now than ever before – the need for such an SEZ has never been clearer.

An SEZ is a formally incorporated geographic area with a single administration bureau, as well as specially provided infrastructure and incentives, fiscal and non-fiscal, such as a one-stop service shop or custom procedures. This definition captures the idea that SEZs must be differentiated and flexible to respond to the specific requirements of a local context.

The key issue that makes an SEZ a success is how, and by how much, the business environment in the zone differs from that of the rest of the economy. But success can sometimes be driven by what is happening in the economy as a whole, so the key question in assessing SEZs is how much additional value is created.

SEZs are no panacea for this country's economic ills. For every Shenzen success story, there is an expensive white elephant. The most successful SEZs are those that have become instruments for accelerated integration into global trade, and that have made possible the combining of foreign companies' technology and knowhow with the local labour force. Access to a global market vastly increases the potential for employment growth. Bringing local firms together with foreign managers and investors (who know global markets and how to run relevant production processes efficiently) in an SEZ facilitates the transfer of relevant knowhow, which spills over into the rest of the economy.

When zones fail, it is generally because they were the wrong instrument. This is the case when they are established in the hope that they will become the catalyst for local development in a marginalised area. The ambition for South Africa to have one or two zones in each province is unlikely to work: not only are zones' prospects maximised when they are near a port, but the forces that shape the spatial distribution of economic activity are not easily manipulated. SEZs may also fail if they are not special enough. This happens when the characteristics of the zone meant to differentiate it from the rest of the economy do not do so adequately.

Subsidising the rents paid by zone tenants is unlikely to be sufficient to lead to meaningful changes. This is especially so in South Africa, where there are many deeper causes of poor economic performance that cannot be addressed by providing physical infrastructure. Despite this, CDE believes that SEZs have a key role to play in stimulating the economy.

In South Africa today, the most compelling case for SEZs is that they offer a way around the vexed political challenges that slow the pace of economic reforms: their establishment may make it possible to address some kinds of policy deficiencies piecemeal or in geographically defined zones than it would be to implement reforms nationally. Done this way, an SEZ might become a kind of policy laboratory-cum-shopwindow in which the impact of proposed reforms can be tested and their benefits showcased to sceptics.

May 2021

CDE's case for an SEZ is underpinned by two key facts. The first is that the greatest challenge we face is creating jobs for millions of young, unskilled, and inexperienced work-seekers; the second is that the policy reforms needed to provide a platform for growth in labour-intensive industries are opposed by a significant fraction of the ruling party and its alliance partners. The SEZ we propose would be, in effect, a policy experiment designed to test whether it is possible to do better in the creation of low-skilled work in labour-intensive industries. This is essential if South Africa is ever to deal with a labour market catastrophe that sees only two adults in five having any kind of job.

The key reforms that are needed include exemption from agreements reached at collective bargaining councils for small and newly formed firms that are not party to the agreement. CDE proposes that working conditions and wages, which would have to be in line with the national minimum wage and basic health and safety rules, would be negotiated at factory level. Goods made in the zone would have to be produced exclusively for export. Skilled foreign managers should be brought in for their expertise in low-skilled, labour-intensive manufacturing. The zone should be located in Coega, because there is access to a deep-water port, a large workforce on its doorstep in Motherwell, and all the amenities that might be needed to attract foreign investors. Everything produced in the zone would have to be exported so that zone-located firms did not compete in the South African market.

An important feature of the proposal is that Coega has already been built. While it has absorbed resources from the rest of the economy (and continues to do so), these are sunk costs, and, apart from costs incurred through the employment tax incentive, creating an export-focused SEZ of the kind contemplated here at Coega would not expose the South African tax base to further erosion or expense.

A couple of cautions are warranted. The first is that, to the extent that low-skilled manufacturing has been the principal entrée for developing countries' industrialisation, the power of this appears to be diminishing: automation and digitisation mean that manufacturing is less and less reliant on human labour. Nevertheless, while automation will impact on all manufacturing jobs, many of the most labour-intensive manufacturing sectors are least vulnerable to this, at least in the short and medium terms.

This means that South Africa has to act urgently: this may be the last opportunity for developing countries to develop meaningful numbers of new industrial jobs. There are no guarantees, therefore, that an SEZ of the kind we describe will work. However, it is all but certain that if we wait too long, South Africa will miss the last opportunity to do this.

One of the great merits of this proposal is that it would test whether more jobs could be created in low-skilled, low-wage sectors, and it would do so in a way that did not diminish the rights or incomes of any existing employee of any existing firm.

The SEZ would be the functional equivalent of an island off the South African coast and would serve as a laboratory to test whether South Africa has any hope of ever creating the kind of labour-intensive manufacturing jobs that have been the lynchpin of industrialisation throughout the world since the 19th century.

We think that this is an experiment well worth trying. Perhaps that is why some parts – at least – of the ANC appear keen to run it, too.

Read the full report available on CDE's website (www.cde.org.za)
What if South Africa had a special economic zone that was actually special?

This report has been made possible with funding from Absa. The funders do not necessarily agree with the views expressed.

Published in May 2021 by The Centre for Development and Enterprise
5 Eton Road, Parktown, Johannesburg 2193, South Africa | PO Box 72445, Parkview, 2122
Tel +27 11 482 5140 | info@cde.org.za | www.cde.org.za