

## **Budget Vote debate by Dr Rob Davies, Deputy Minister of Trade and Industry**

29 March 2006

Madam Speaker, Minister, comrades and colleagues, I want to take this opportunity to speak on two areas of work I have been involved in since my appointment as Deputy Minister: Industrial Policy and International Trade Negotiations.

It is pretty much common cause in the serious economic policy debate in this country, that we need a more effective and robust industrial policy. Economic history teaches us, that those very few developing countries that have succeeded in breaking out of their historical places in the global division of labour as mere producers of raw materials, have all had active industrial policies. Industrial policy, to paraphrase Vivek Chibber, can be recognised as a series of state interventions in which the focus shifts from managing the effects of the accumulation process to accelerating its pace. In the case of the prominent examples of successful industrial policy governments of various East Asian countries were all prepared to assert leadership to the extent of getting prices wrong and directing investment into the development of lines of industrial activity not then recognised by markets, but which through active industrial policies were subsequently developed into a major competitive advantage. Behind the more recent rise of China as a major economic power have also been active industrial policies.

The Accelerated and Shared Growth Initiative for South Africa (AsgiSA) adds its voice to calls for a more robust and active industrial policy in South Africa. Our Department is in the final stages of preparation of a broad strategic framework document which we hope will pass through the governmental processes within the next few months. In addition to the overall framework document, we anticipate that there will also be a need for the development of new strategies on important key related matters like industrial finance and capacity building for Industrial Policy. We also need to push forward with, refine and improve the sectoral work which has been underway for some time. I have had the privilege to chair a review team, which has engaged in a self critical reflection of some of the challenges which face us in making our industrial policy more effective.

Industrial policy is of course not new in South Africa. In the period since 1994 we have produced several industrial policy strategic documents and for some time have engaged in sector processes, some of which, for example in the motor industry, have scored important successes. But our reflection has led us to conclude that some of our efforts in the past were too dispersed, too unfocussed and we have often failed to deploy sufficient resources to actually make a real difference to the performance of, and activities within, industrial sectors. Among the themes which we will be emphasising in our new approach to industrial policy, will be the need for government to facilitate and encourage all stakeholders to engage in a process of self discovery. Self discovery needs to take place both at macro level and at specific sector level. At macro level, the process of self discovery and analysis needs to lead to the identification of sectors, which will be targeted in our industrial strategy. Considerable work has, of course, already been done in this regard and our reflections and self discovery at macro level have led us to recognise that we have in South Africa a fairly diversified industrial sector with strengths in a variety of areas, and also that there is a need to break down artificial divisions between industrial and service sectors, and between industrial or manufacturing and agricultural sectors. There are four broad areas that have been identified for more focused attention:

(1) Firstly, there are sectors which have been identified by AsgiSA, as ripe for an early harvest in terms of growth and job creation, where work has already been done, and where the intention is to build on and consolidate those efforts. In this category we find the Business Process Outsourcing and Off-shoring and the tourism sectors, where significant job creation has already taken place, and where with further efforts, we can add many thousand more jobs by 2014.

(2) The second category includes a number of sectors with potential for growth and employment creation in the medium term, but would need significant restructuring and reorganisation in order to achieve their potential. Many of these sectors were identified by the 2003 Growth and Development Summit, and are the subject of Customised Sector Programmes at various stages of progress. They include clothing and textiles, the motor industry, chemicals industry, agro industries and so on.

(3) In the third category are sectors which have not been the subject of industrial policy work up to now, but in which job creation potential could be significant. These are sectors also that link into the Second Economy. Included here are bio-fuels initiative and the proposed CSP type process for non tradable service sectors ranging from informal repair shops and personal services like hairdressing, through to a range of social services provided also with the assistance of government departments. The draft industrial policy strategy document which we will be tabling shortly, suggests that there should be a CSP process for these sectors.

(4) Finally, there are sectors in which we believe South Africa could develop cutting edge technological excellence and become a world leader. They include parts of the aerospace industry, parts of the hydrogen economy, medical technology, biotechnology more generally and so on.

Self discovery also needs to take at sector level and lead to the identification of key action plans needed to take our sectors from where they are to where we need them to be. Here again we need to build on, accelerate and improve on Customised Sector processes already underway. Through CSPs we need to identify the kinds of contributions which are necessary from government, business, labour and other social partners to advance action plans. A further conclusion from our self assessment is that we, as government, must be willing to employ our resources in a more concentrated way that can actually make a difference. Greater customisation of industrial financing and incentive programmes and alignment with action plans identified in sectoral processes, will also be necessary if we are to make the impact which we need. This will require much greater coherence between the processes at sectoral level, and those in which industrial incentives and financing measures are actually designed.

We will also need to look more closely at the issue of conditionality and reciprocity in the deployment of incentives and offerings. We need to be offering sectors and firms significant resources for programmes and projects that will make a difference, but we must insist on reciprocity and be willing withhold or withdraw support if appropriate agreed restructuring does not take place.

In addition to all of this, there are of course the cross cutting interventions which are identified in the Micro Economic Reform Strategy programme and which are refined and in AsgiSA. They include the infrastructure development programme, regulatory reviews, and critically the Joint Initiative on Priority Skills Acquisition (JIPSA) skills initiative and other training programmes.

To pursue a more effective and robust industrial policy of this kind, we will have to address some very, very important challenges of capacity building. We will have to significantly enhance our own capacity within the dti and to make sure that this capacity is optimally located in the various divisions of the department. We will also need to find better mechanisms to bring in and co ordinate industrial policy capacity that exists outside of the immediate framework of the dti in Council of Trade and Industry Institutions (COTII) institutions like the Industrial Development Corporation (IDC), and in other government departments. Beyond this, we need to create mechanisms to draw in and build on expertise, which exists outside of the governmental framework, in Universities, research institutions and the like. This all has to relate to our institutions of social dialogue and must be reflected in sector processes that are in fact exercises in self discovery by key stake holders involved in industries and sectors themselves. These will be major challenges that we in the Ministry and the Department will have to confront as we go ahead. We look forward to, and welcome an active engagement with the portfolio committee and with Parliament in this process, which we believe does not lead to the production of an industrial policy that is going to be written in stone, but an industrial policy which is constant work in progress, and which needs to be reviewed periodically at three year intervals.

Let me move now to the area of trade negotiations.

Madam Speaker, Chairperson, we meet at a very critical moment in the ongoing World Trade Organisation (WTO) Doha negotiations. At the end of last year, South Africa along with all the other members of the WTO, participated in the sixth Ministerial Conference held in Hong Kong, China. According to the original milestones for the Doha negotiations, Hong Kong was supposed to have agreed on full modalities to give effect to the principles agreed at Doha in 2001 for agricultural, non-agricultural and service negotiations. It was recognised even before Hong Kong, however, that there was not sufficient agreement among the membership to achieve this, and Hong Kong tried to reach a half way house short of full modalities. It did however set a target of reaching full modalities by 30 April this year and intensive behind the scenes activities are taking place in Geneva and elsewhere in an attempt to explore the possibilities of reaching this target.

Madam Speaker, Chairperson, it's a matter of great regret that we need to report to this house that the chances of achieving a developmental outcome by the new target date for modalities look as remote as ever. In Doha in 2001, developing countries, ours among them, put forward a powerful and convincing case that the fundamental requirement for an equitable and effective world trading system, was to address a number of imbalances and inequities that affected negatively developing countries. These included prominently the issue of agricultural trade and the thorny question of subsidies. Previous rounds of multi lateral trade agreements, up to and including the Marrakesh agreement of 1994, had largely left intact a system of agricultural trade in which developed countries were able to maintain substantial protectionism against competitive products from developing countries, through high tariffs and subsidies paid to small numbers of farmers in the developed world. Average tariff cuts in non-agricultural products allowed the continuation of tariff peaks and tariff escalations on industrial products where developing countries had an export interest. Developing countries argued that the focus of a new round, and indeed the basis on which they would agree to a new round, was that distortions in agricultural trade as well as tariff peaks in escalations and non tariff barriers on industrial products where developing countries have potential, should be the focus of the work programme. Of course the Doha mandate also included a number of demands of rich countries, but we should not forget that the Ministers at Doha agreed to place the needs and interests of developing countries at the heart of the work programme of the Doha round.

Speaker, Honourable Members, unfortunately the period since Doha has seen an attempt both to water down necessary adjustments by developed countries and to combine this with highly ambitious demands directed at what are called advanced developing countries. We have seen extremely modest proposals from both the European Union and the United States for cuts in agricultural domestic support that would still leave in place the possibility to deploy large resources to subsidise activities of a small number of uncompetitive farmers in those countries. At the same time we have seen a wholly inadequate offer from the European Union on the question of agricultural market access. The G20, the Cairns Group in the United States, have all concluded that the proposal from the European Union could block any real additional access for all current products of export interest to developing countries.

This has been coupled with demands in the non-agricultural market access area that would see countries like South Africa being obliged to make very significant cuts not just in bound, but also in applied tariff rates.

Chairperson, in the run up to Hong Kong, South Africa along with a number of other developing countries tabled a document in the WTO which we entitled "Reclaiming Development". We argued that we needed to reassert proportionality in the negotiations; that the biggest adjustments needed to take place in the sector that was most distorted i.e. agriculture; that the biggest adjusters needed to be the developed country blocks, that were involved in these distortions and that the obligations of developing countries according to the principle of special and differential treatment needed to be smaller.

During Hong Kong, our delegation under the able leadership of our Minister, Mandisi Mpahlwa, managed to play an active role on these and other issues. We consolidated the group of developing countries, which had signed on to the "Reclaiming Development" paper, and constituted it into the grouping, which we called the NAMA 11.

NAMA 11 resisted an attempt to try to force a premature agreement on modalities in non-agricultural market access ahead of any significant agreement on the main issues in agriculture. We also managed to have included in the Hong Kong declaration, a paragraph on the balance of the outcome of the round as a whole. Paragraph 24 speaks of there needing to be a comparable level of ambition in market access in agriculture and in NAMA. And it goes on to say that this must be achieved in a balanced and proportionate manner consistent with the principle of special and differential treatment.

Recent technical work undertaken by a group of 10 countries, six developed, for developing, has established that even in NAMA itself, developed countries would have to accept a very low coefficient in the application of Swiss formula of around two to ensure that they take a bigger percentage reduction in industrial tariffs than developing countries applying a coefficient higher than in many proposals of around 35.

Madam Speaker, colleagues, I am happy to report that the NAMA 11 continues to be an active and significant force in these negotiations. We will do all we can as South Africa to ensure that we do not find ourselves in a situation where we are obliged to make large adjustments in our industrial sectors to achieve little or nothing in the area of agriculture. That cannot be a developmental outcome. Where the WTO process goes from here will not be easy to predict. What we need is a high level political decision in developed countries in favour of developed countries taking the lead and making the adjustments which are necessary, not just in the interest of developing countries but in the interest of an equitable global trading system as a whole. Failing this, there are real prospects that we may end up coming out of the Doha process with little that can be recognisable as a development round.

The danger in the latter scenario is that we will be faced with the alternative of aggressive bilaterals, in which ambitions that the major economic powers have not realised in the multilateral process are recycled and placed on agendas of bilateral negotiations. We can see signs of this in some of the bilateral processes we are engaged in. The Southern African Customs Union (SACU)/United States (US) negotiations have failed to make progress partly because we have faced what we believe are inflexible proposals on tariff reductions that do not take sufficient account of our different levels of development and the principles of asymmetry. These have been combined with demands that would effectively require us to accede to US systems and positions on a host of so-called "new generation" issues including competition policy, state procurement, intellectual property and so on. One of the difficulties we face in this regard, is that we now negotiate not as South Africa, but as the Southern African Customs Union. As a Customs Union of five countries including one least developed country, we do not have common positions on these kinds of issues, and the actual regimes of the five members of the Customs Union on intellectual property and on competition are fairly divergent. A meeting at the level of "deputies" is scheduled for next month. If we are to make progress, it is essential that our partners show much greater flexibility than they have up to now.

The Economic Partnership Agreement negotiations between the Southern African Development Community (SADC) configuration and the European Union (EU), in which we are at present participating observers, are at the point where we are seriously beginning to discuss their scope and content. Here too, it is essential if we are to make progress, that our interlocutors adopt flexible approaches and also genuinely place developmental needs and the promotion of developmental regional integration, at the forefront of their objectives.

We need in the light of this to be reviewing much more intensively our approach to promoting regional integration. The most credible analytical work on regional integration that I am aware of, has argued that in regions of developing countries many of the major barriers to promoting intra regional trade, do not arise from tariffs and regulatory regimes, so much as from under developed production structures and inadequate infrastructure.

Some of the most informed and credible studies that have been done for example of the Southern African Region in the 1990s, argued that what was needed was a programme that combined sectoral cooperation, policy co-ordination and integration in a broad developmental programme. What we need to interrogate much more rigorously, the extent to which our regional programmes and ambitions for customs unions, monetary union and the like, legitimate and valid as they undoubtedly are, are actually grounded in a programme that makes such steps realistic and viable.

Finally Madam Speaker, Chairperson, we need to think much more strategically about how we relate to the new important players in the global economy, countries like China and India. There is a growing body of opinion which is suggesting that these countries are not just emerging as important players, but also as potential new poles in the global economy.

Some analysts are suggesting that their path of industrialisation and the pattern of external relations that emerges there from, is significantly different from that of the advanced industrialised countries of Europe and North America. There may be real new opportunities for South-South trade in mineral products and beneficiated mineral products arising from this. Of course, at the same time these countries have become very dynamic forces, and strong competitors, in a range of industrial sectors. What we need is a much more rigorous analysis of these trends as a basis for informing a programme of economic diplomacy aimed at reaching mutually beneficial and development orientated agreements with these countries.

This is all work which the dti will need to be engaging in during the course of this budget year, in particular through the International Trade and Economic Division.

Madam Speaker, colleagues, in the divisions dealing with these important areas of industrial policy and trade policy, not to mention divisions which are dealing with important issues like small business development, co-operative development and so on, the department continues to put forward a relatively modest budget. A budget, however, which is showing some growth from that of previous years. Our challenge in the dti is not so much one of money, but in getting value for money, by working harder, smarter and more effectively than we did in the past.

In calling for the support of this house for the budget vote of this Department, we indicate that the Ministry and the Department is committed to rising to the challenge in this regard.

I look forward to your support for this budget vote and I thank you for your attention.

Issued by: Department of Trade and Industry

29 March 2006