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South Africa's Investment and Export Incentives

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'Businesses trade to invest and invest to trade'
Renato Ruggeiro, Former Director
World Trade Organisation

The above quotation elegantly summarises the relationship between investment and exports, and highlights the importance of complementary policies to stimulate investment and promote production for export.

South Africa's incentive programme is administered by the **Department of Trade and Industry (DTI)** with **Trade and Investment South Africa (TISA)** managing the investment side and the **National Export Advisory Council (NEAC)** the export side. The aim of South Africa's incentive programme is to simultaneously boost fixed investment (with the ultimate objective being increased international competitiveness and thus international trade) and encourage export-enhancing industrialisation. It is consistent with the objectives of the **Growth Employment and Redistribution (GEAR)** policy and aims to aid in the transformation of SA from a highly protected and inward looking economy to one that is fully integrated into the global economy.

It is a carefully constructed programme and is focussed in its support structure. The main features of this programme are tax incentives, industrial financing incentives, the Small Medium Enterprise Development Programme (SMEDP) and its complementary programmes, Research and Development (R&D) grants, the Critical Infrastructure Facility (CIF), Industrial Development Zones (IDZs) and Spatial Development Initiatives (SDIs), Community Public Private Partnerships (CPPPs) and the various export incentives.

The main feature of this integrated programme is that incentives are used to target specific high-growth sectors and industries as well as geographic regions. The **spatial concentration of infrastructure** is deemed to be crucial to SA's growth path.

Tax Incentives

The following accelerated depreciation allowances and tax write-offs are in existence:

- **R&D expenditure**: 25% of the capital expenditure approved by the Council for Scientific Industrial Research (CSIR) (if the research is discontinued, compensating payments must be made).
- **Employee housing**: 50% of the cost of a house built for an employee (or money donated/advanced for the building of a house), with a maximum value of R6000. Or, 10% in year one and 2% thereafter for the building of 5 or more houses to let/house employees.
- For new and expanding businesses (both local and foreign) **plant and machinery** is depreciated over 3 years and land and buildings over 5 years. The rates for plant and machinery are 20% (manufacturing), 2% (hotel equipment) and for farming equipment the rates are 50%, 30% and then 20% over the 3 years.

Buildings are depreciated at 5% (industrial), 5% (hotels) or 20% (hotel expansions).

- **Other non-manufacturing fixed assets** are depreciated at variable rates (between 10% and 20%).

SA has **double tax agreements** in place with a large number of countries.[1] It also has limited **sea and air transport agreements** with Brazil, Greece, Portugal and Spain.

Industrial financing incentives

To aid the development of the private secondary manufacturing sector, the state-owned Industrial Development Corporation (IDC) provides medium- to long-term loans. The fixed IDC rate is currently 17% and the variable rate is 2% below prime for most projects or 4.5% below prime for entrepreneurial or job creation projects. There are number of financing facilities in place:

- **Employment Promotion Scheme**: 3 year loans are available to company's creating at least 10 new jobs, provided the capital cost of creating the job is less than R50000 and the total assets of the company are less than R100 million. If the cost per job is between R50000 and R100000, half the loan will qualify for the low rate and the other half will be charged IDC's normal rate.
- **Export of Capital Goods and Services Scheme**: loans are available for 2 to 10 years.
- **Import Financing**: importers of capital goods and services are provided access to credit and guarantee facilities.[2]
- **Economic Empowerment Scheme**: industrialists from previously disadvantaged communities enjoy preferential treatment in terms of project financing.
- **Venture Capital Finance**: loans are available for entrepreneurs starting up a high technology business.
- **Eco-tourism Scheme**: loans are granted to projects that develop, improve or expand tourist facilities in conservation areas/national parks (greater than 10000h), provided the owner finances 40% of total assets.
- **General Tourism Scheme**: loans (maximum of R10 million) are granted to hotels providing accommodation for foreigners. Turnover from accommodation (including meals) must be 70% of total turnover and the owner must finance 40% of total assets.
- **Orchards Scheme**: loans are available to employment generating projects in rural areas.
- **Multi-Shift Employment Creation Scheme**: independent industrialists with assets greater than R1 million and equity greater than 33% of the value of total assets, are granted finance at low rates (for 3 years) for projects that add at least one extra 8 hour shift.

[1] Algeria, Australia, Austria, Belgium, Botswana, Canada, Croatia, Cyprus, Czech Republic, Denmark, Egypt, Finland, France, Germany, Hungary, India, Indonesia, Iran, Ireland, Italy, Israel, Japan, Korea, Lesotho, Luxembourg, Malawi, Malta, Mauritius, Namibia, Netherlands, Norway, Pakistan, People's Republic of China, Poland, Romania, Russian Federation, Singapore, Slovak Republic, Swaziland, Sweden, Switzerland, Taiwan, Thailand, Tunisia, United Kingdom (extended to Grenada and Seychelles), USA, Zambia and Zimbabwe.

[2] The Deferment of Payment Scheme and Duty Drawback Scheme are examples.

- **International Competitiveness Finance**: this scheme was in place from 1995 to 1999 and aimed to help industrialists that were adversely affected by tariff reduction regarding the importation of capital equipment. They were granted finance at low rates for 3 years (after which they will pay the IDC rate).
- **Bank Indemnity Scheme**: This is applicable to SMEs where contribution and collateral equals 50% of the facility granted. The bank is given indemnity against 60% of any loss for SMEs borrowing up to R400000.
- **Standard Leased Factory Building Scheme**: the IDC leases properties to industrialists at competitive rents.

The Tax Holiday Scheme (replacing the Regional Industrial Development Programme) was available to manufacturing enterprises formed after 1 October 1996 and approved before 30 September1999. Successful applicants in this time period are exempt from income tax for a maximum of 6 consecutive years and this tax holiday must be utilised within 10 years of approval. Two years tax free income is granted for each of the following criterion met: product on the approved list, plant in a designated location and Human Resource (HR) remuneration to value added ratio greater than 55%. This scheme has been phased out (although it was successful in stimulating investment) and has been replaced with other incentives.

Certain **key industries** have been designated priority areas. They are: motor vehicle assembly and components, clothing, building materials, textiles, household electrical durables, electrical distribution equipment and professional electronics, pulp and paper, commodity plastics, mineral and mineral-based fabrication, food processing, beverages, footwear, engineering and labour intensive agro-industries. The government has committed itself to aiding productivity increases in industry by promoting HR and technical development as well as workplace restructuring in terms of organisation and democratisation. In addition, the development of forward linkages between primary commodities and manufacturing industries will be encouraged.

R&D Grants

These grants are in place specifically to develop skills, and promote the innovation of new products and processes. There are 4 programmes:

- **Support Programme for Industrial Innovation (SPII)**: two schemes fall under this programme. **The Matching Scheme** gives a grant equal to 50% (capped at R1.5 million) of the direct costs of a development activity. **The Feasibility Scheme** (only small, medium or micro enterprises qualify) makes available a grant of 50% of the costs of a feasibility study undertaken by a consulting company.
- **Partnerships in Industrial Innovation (PII)**: this fund provides support for large R&D projects. Tax-free loans are awarded to development projects (for a maximum of 50% of its qualifying costs).
- **Technology and Human Resources for Industry Programme (THRIP)**: this programme is administered by the National Research Foundation (NRF) and it

provides grants to joint research teams (comprising of members from government, industry and academic institutions). It favours research in the natural sciences, engineering and technology.

- **Innovation Fund**: R&D in the following areas - information society, genetic biotechnology, value added in the exploitation of natural forna and flora, value added in advanced materials and manufacturing - are eligible for funding of between R1 and R5 million over a 3 year period.

Incentives for SMEs

The Small Medium Enterprise Development Programme (SMEDP)

Both new and expanding businesses are eligible for this grant with the maximum value of the investment equal to R100 million (the previous programme, the small/medium manufacturing development programme (SMMDP), set its maximum investment at R3 million). Businesses must apply within 180 days from the date of production and production must have commenced on or after 1 September 2000.

The following SME's qualify for the incentive packages: manufacturing, agricultural projects and agro-processing, aqua-culture, bio-technology, tourism, information and communication technology, culture industry and business service. SMEs can be private or public incorporated entities, close corporations, sole properties, partnerships or co-operatives. Projects can be new activities or expansion of existing activities.

Assets that qualify for the grants are as follows: owned (at cost) and leased (capitalised) land and buildings, equipment and commercial vehicles plus R&D capital costs. The following minimum equity requirements hold: 10%, 25% and 35% for projects with qualifying fixed assets up to R5m, between R5 and R15m and above R15m respectively.

With respect to expansion activities (defined for machinery and equipment as additional investment of at least 35%), each entity is only eligible for one expansion grant, and this grant cannot be used in conjunction with other incentive programmes. Jobs cannot be lost as a result of the expansion, and turnover must increase by at least 25% and then 50% of the predicted application figures for the first and second grant years respectively.

The 3-year incentive package

- **Strategic Investment Programme (SIP)**: an investment grant is awarded for 2 years on qualifying assets on a regressive scale and on the third year if HR remuneration is 30% of manufacturing costs (gross operating surplus plus HR remuneration).
- **Foreign Investment Grant (FIG):** this grant sponsors imported plant and equipment provided by foreign investors. Grants are limited to US$150000

(US$50000) for new machinery and equipment costing less than US$20 million (US$5 million).

- The **value** of the tax-free grant is calculated as follows: for the first R5m - 10%; for the next R10m (5-15m) - 6%; for the next 15m (15-30m) - 4%; for the next R20m (30-50m) - 3%; for the next R25m (50-75m) - 2%; for the next R25m (75-100m) - 1%.
- The value of the grant depends on whether it is for a new or expansion project.

Skills Support Programme (SSP)

This programme complements the SMEDP and only those companies eligible for that programme may qualify for it.

- It involves a performance based 3 year cash grant to assist in the training of new skills required for a new or expansion project.
- It is composed of training (on the job or off the job), curriculum development and capital grants.
- 50% of the training costs are subsidised, and this amount is capped at 30% of the annual wage bill.
- A capital grant for training equipment is also available.
- Facilities are provided to assist in the construction of course materials.

Critical Infrastructure Facility (CIF)

- **Critical infrastructure** is (by definition) economic infrastructure that supports strategic, economically robust and competitive investments that aim to generate employment as well as improve environmental performance. Thus, it supplements infrastructure that is provided by existing public and private players.
- Grants are provided for economic infrastructure required for **specific** committed productive investment (as opposed to investments in basic infrastructure).
- Projects must have a value of over R100 million, and grants of between 10% and 30% of the capital costs incurred may be made to municipalities and the private sector.

Industrial Development Zones (IDZs)

The IDZ initiative (modelled on Export Processing Zones - EPZs) is run by the DTI and is only in the preparatory phase of its establishment. However, the ultimate goal of IDZs will be to boost manufacturer's international competitiveness within a structured environment. This environment is envisaged to be world-class, complemented by state of the art transport, communication and utility networks. In order to reduce transport costs, IDZs will be situated near an airport or seaport, with efficient customs operations and duty-free incentives stimulating the production of goods for export.

Some areas earmarked for development of IDZs are the Coega harbour near Port Elizabeth, Saldanha Bay, Richards Bay and the West Bank near East London.

There will be a **Customs Secured Area (CSA)** within each IDZ and these offices aim to clear goods efficiently and speedily. The following incentives are offered:

- Raw materials and inputs are exempt from duty if used for the production of exports.
- Local supplies used in production are not subject to VAT.
- Goods manufactured in the zone and sold within South Africa are treated as imported goods.
- Imported final goods for sale within South Africa can be received in these zones.
- There is no minimum export quota.

The other component of the IDZ is the **Industries and Services Area (ISA)**, which is comprised of industrial/office parks.

There will be a major emphasis on human resource development and labour friendly policies within the IDZs with the government providing learnership programmes as well as skills audits and recruitment selection and training. All disputes are to be settled via official channels. Another important facet of the programme is government's commitment to insuring that all companies comply with the new 'green' standards of production. This is becoming increasingly important in the global economy and South Africa cannot afford to be 'left behind' on this count.

Spatial Development Zones (SDIs)

- The DTI has been responsible for the research, joint planning, investment packaging and promotion of these initiatives. The implementation of the plans (as well as follow up activities) will be undertaken by appropriate national, provincial or local government departments.
- The locations were selected because of their under-utilised potential as areas to accommodate productive investment. Lead sectors for this investment have also been identified.
- There are 11 local and 3 transnational SDIs at varying stages of delivery. They are: **Blyde River** SDI in the Northern Province; **Durban** SDI; **Fish River** SDI (split into 2 nodes - eMonte Kei and Greater Algoa Initiatives) in the Eastern Cape; **Gauteng** SDI; **Gariep** SDI (a transnational initiative in Namibia and the Northern Cape Province); **Lubombo** Initiative including the Greater St Lucia Weland Park (a transnational SDI in KwaZulu Natal, Swaziland and Mozambique); **Maloti Drakensburg** Initiative (a transnational SDI in Lesotho, northern Eastern Cape, KwaZulu Natal and Free State); **Maputo Development Corridor** (a transnational initiative in Swaziland, Mozambique and Mpumalanga); **Phalaborwa** SDI in the Northern Province; ,**Pietermaritzburg/Msunduzi** SDI in KwaZulu Natal; **Platinum** SDI in North West Province; **Richards Bay-Empangeni** SDI in KwaZulu Natal; **West Coast** Investment Initiative in the northern Western Cape; and, **Wild Coast** SDI in the Eastern Cape.

- These SDIs comprise approximately **800 investment opportunities** worth approximately **US$32.4 billion** and, an estimated **85000 new jobs** are to be generated by the schemes.
- Many of these SDIs are currently being handed over to **provincial governments** – this might hamper progress if the local authorities do not have the capacity to successfully implement the programmes.

Community Public Private Partnerships (CPPPs)

The CPPP programme facilitates investment in rural economies. The ultimate aim is to boost employment and educate people on how to achieve a **sustainable livelihood** in these areas. Sustainable resource usage is a key component of the programmes and joint partnerships provide the management expertise and funds to uplift the areas.

Export Incentives

The Export Marketing and Investment Assistance (EMIA) Scheme

- EMIA funds promotional activities, trade missions as well as research activities. Exporters are assisted with undertaking the following activities: primary export market research (PMR), FDI research, exhibition assistance, outward selling trade missions, outward investment recruitment missions, inward buying trade missions, inward investment missions and assistance to industry specific sectors. The table at the end of this policy brief summarises the terms of assistance under each activity
- In each programme there are a number of rules and regulations that exporters have to comply with. The criteria for approval of a trip are strict and all receipts/invoices must be produced when claims are made. With regards to research trips, reports must be submitted to the DTI detailing the undertakings/findings.

The Export Credit and Foreign Investment Reinsurance Scheme

- This scheme makes available credit at preferential rates plus provides insurance companies with reinsurance for loans to exporters. All facilities are provided by the **Credit Guarantee Insurance Corporation of Africa Limited (CGIC)**. The CGIC offers five different facilities: short-term insurance, medium/long term insurance, export finance for capital goods or projects, foreign investment guarantees and export finance guarantees for SMEs.
- Short-term insurance consists of pre-shipment cover, post-shipment cover and consignment stock cover. It is used with respect to commercial or political risk where credit terms are less than 180 days. Medium/long term insurance consists of: contractor's cover, cover against the unfair calling of bonds, financial credit cover, foreign exchange risk cover and investment guarantees.

The Export Finance for Capital Goods and Projects Scheme

- This scheme aims to enhance exporters competitiveness by fixing exchange rates enabling exporters to offer quotes/tenders in US dollars. In terms of repayment of capital projects (amortisation period of 10 years), exporters can offer extended repayment at fixed international market related interest rates (expressed in US dollars). When the project is delivered, the IDC or a participating commercial bank will pay the exporter and extend a loan to the foreign buyer (denominated in rands or US dollars). The fixed rates for export credit loans denominated in dollars are 6.25% (up to 7 years) and 6.5% (between 7 and 10 years) (the rates include a foreign exchange premium of 0.5%) and for loans in rands the rate is floating.
- Foreign investment guarantees are provided to South Africans investing a minimum of R100000 abroad and these guarantees protect them against expropriation, confiscation and nationalisation. Export finance guarantees for SMEs provide these businesses with CGIC guaranteed finance (loans between R50000 and R1m and not greater than 90% of the value of the export order) that is reinsured with the DTI.

Customs and excise duty refunds, drawbacks and rebates

- These concessions are for manufacturers of exports as well as businesses importing goods for re-export.

Rail, road and shipping costs

- Reduced rail rates are available for commodities exported on a contractual basis
- Road transport concessions can be negotiated with the local Road Transportation Board.
- Reduced Ocean Freight Rates can be negotiated directly with shipping companies or with the South African Shipping Board if exporters believe that shipping costs are preventing them from exporting their products at competitive prices.

Export Councils

- The DTI encourages the formation of **industry based export councils** and makes funds available for the formation of these councils.
- These councils select target markets and set export targets for the industry as a whole.
- There are 20 existing export councils: structural steel, steel pipes and tubes, wire, stainless steel, aluminium, jewellery, furniture, footwear and leather, plastics, cosmetics, food and wine, cut flowers, clothing, textiles, electrical and electronics, motor assembly and auto components, water treatment and chemicals, capital equipment, small exporters programme and arts and crafts.

Conclusion

SA's incentive programme is comprehensive and offers investors and exporters many opportunities for growth. In general, it aims to boost SA's **manufacturing industry** and encourage **personal economic empowerment** through the promotion of SMEs.

Most importantly, the incentives in place aim to promote employment-generating business - so, by reducing unemployment, SA citizens can enjoy greater welfare as SA becomes part of the global village.

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Summary of EMIA terms of assistance for export activities

	Summary of compensating assistance[1]:	Economy airfare	Subsistence allowance	Transport of samples	Marketing materials[2]	MBus rental
PMR[3]	Costs of developing new export markets.	80% PDI, 70% SME	R1000 (15days)	R 1000	R 10000	
		50% other				
FDI Research	Costs of attracting FDI through overseas trips.	As for PMR	R1000 (15days)		R 10000	
Exhibition Assistance	Costs of participating in foreign trade exhibitions.					
National Pavilions[4]	For official South African participation at a show.	80% PDI, 70% SME	R1000 (duration)			
Individual participation in exhibitions[5]	For individual exporters at a show.	80% PDI, 70% SME	R1000 (duration)	R 10000	40% or R3000	
Adhoc group participation	For groups not represented individually.	70% of airfare	R1000 (duration)	R 10000		
Outward-selling trade mission	Costs of making contact with foreign buyers.	As for PMR	R1000 (15days)	R 1000		
Outward investment recruitment missions	Costs of missions to stimulate FDI.	As for PMR	R1000 (15days)	R 1000		
Inward buying trade mission 1	Costs of organising foreigners contact with SA exporters.	External and internal	R600 (10 days)			R 5000
Inward buying trade mission 2	Costs for foreigners to contact individual SA exporters.	50% economy/business	R600 (5 days)			R 5000
Inward investment mission 1	Costs of organising missions to attract FDI in SA.	External and internal	R600 (10 days)			R 5000
Inward investment mission 2	Costs for individual foreign companies to visit SA.	50% economy/business	R600 (5 days)			R 5000
Assistance to industry specific sectors[6]	Assistance in developing new export markets.				R50000 brochures R50000 video	

[1] All assistance is for one representative per enterprise.
[2] Marketing materials include promotional brochures, videos and CD Roms.
[3] For the PMR program, the DTI also sponsors product registration (patents, trade marks and quality marks).
[4] For national pavilions, the DTI also pays the following costs: space rental, construction and maintenance of stands, electricity and water charges and freight costs (maximum of 3 m^3 or 2 tons per exhibitor). Exhibitors are responsible for all promotional material plus insurance cover.
[5] For individual participation in exhibitions, the DTI will also pay 80% (to a maximum of R40000) of the following costs: space rental, construction of stand, telephone installation (excluding calls), furniture rental, directory listing, electricity, interpreting fees, cleaning and security fees.
[6] In order to establish an export council, the DTI will pay a matching grant of R400000 in year one and R200000 in year two plus cover costs of up to R40000. The following costs will be covered: buying or leasing office equipment; furniture and fittings; salaries and wages; consulting service fees; office rental; land line and cellular phone costs; stationery and postage; audit, legal and bank charges; local travel (maximum R10000); SME export training; local advertising and promotions; insurance; office maintenance. Financial assistance is also provided for: foreign trade exhibitions (as per ad hoc group participation), trade exhibitions in South Africa (50% of rent and stand construction - maximum R100000), outward selling and inward buying missions, generic advertising campaigns (R100000 per annum) and export marketing consultants (R25000 per visit).