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Industrial Policy, the Manufacturing Sector and Black Empowerment in South Africa[1]

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Abstract

Black economic empowerment (BEE) in South Africa has undoubtedly been ambitious in seeking to transform ownership, control, and management of the economy's productive assets and resources. It is ambitious because the changes that are needed to reverse decades of entrenchment of economic power in the hands of a few are far-reaching. Extensive transformation means challenging the position of incumbents in the economic system and the interests that work together to maintain those positions, in the context of a decidedly liberal economic policy context. While BEE policy has been applied as the African National Congress government's primary strategy for bringing about transformation in the ownership and control of productive assets in the economy, the outcomes in key sectors of the economy have been poor in terms of inclusion. This paper considers the interrelations between the black empowerment programme and industrial policies in South Africa, with specific reference to transformation in the manufacturing sector.

The paper examines the extent of transformation in the manufacturing sector in South Africa. The paper seeks to understand why South Africa has not seen the emergence of a large, economically significant black industrialist class that owns and controls economic assets and resources that are competitive at different levels in the manufacturing sector. The paper further explores the extent to which South Africa's industrial policy strategies have contributed to or undermined deep transformation in the manufacturing sector. The paper identifies key limitations of BEE and South Africa's industrial policy framework, and the gaps between these policies in terms of addressing the factors that restrict the inclusion of black-owned firms in manufacturing. It further considers how industrial transformation could be accelerated in South Africa.

Introduction

The optimism for economic transformation at the dawn of post-apartheid South Africa has turned to disenchantment with the slow pace of inclusion and empowerment. Despite the transfer of political power to majority rule in 1994, South Africa remains one of the most unequal societies in the world today. The remnants of apartheid and its system of exclusion of black people and other minority South Africans from access and ownership of economic resources remains, and to a large extent has festered, along racial lines.

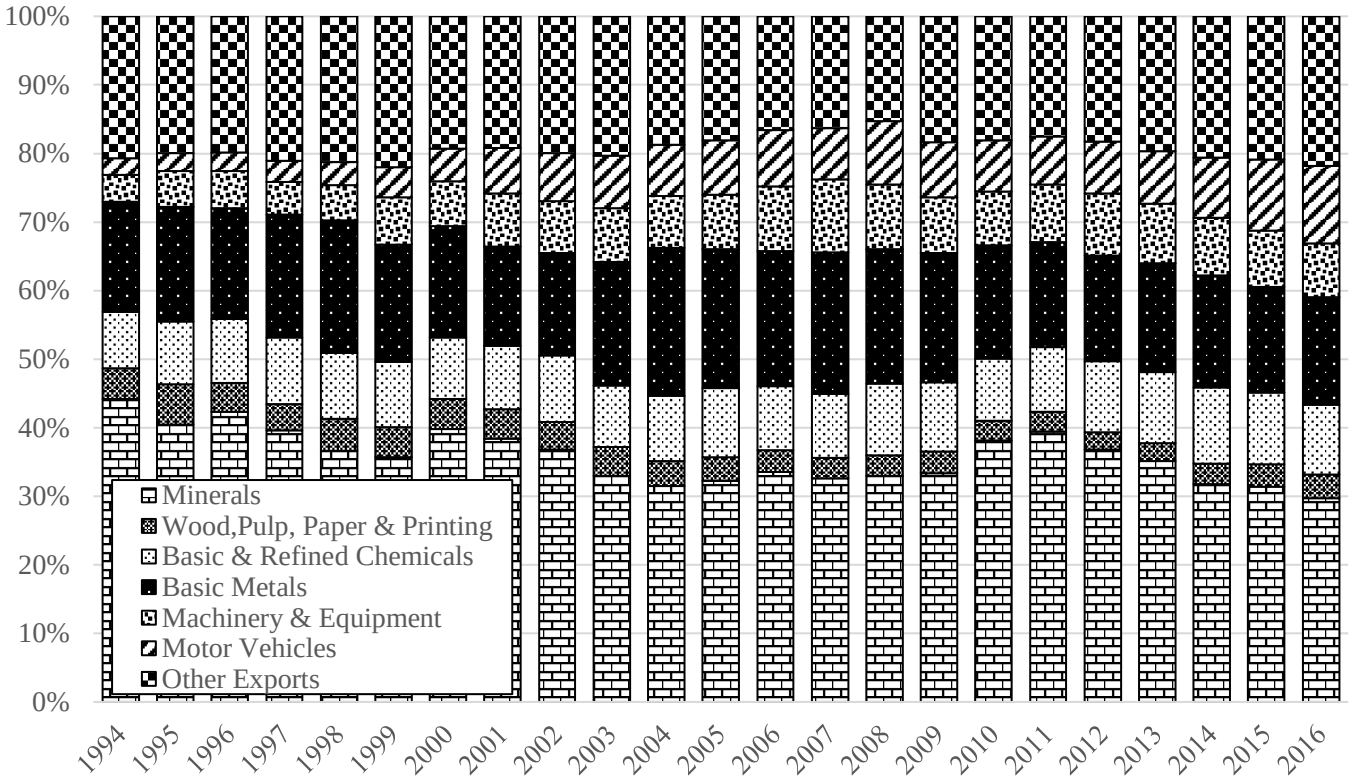
This paper considers two main questions: i) what is the extent of transformation in the manufacturing sector in South Africa? and ii) what has been the impact of industrial policy strategies in South Africa on the emergence (or not) of a significant black industrialist class? In doing the latter, we consider the kinds of industrial policy pursued by government and assess the impact of stances and instruments in contributing to transformation.

South Africa remains a country in economic transition with a fragile social contract and a weak economy (World Bank, 2018). The weaknesses in the economy are embodied in rising rates of unemployment and deindustrialisation (Andreoni & Tregenna, 2018; SEDA, 2012). There is recognition that industrial development and growth in manufacturing value added is imperative in driving sustainable and inclusive growth. The manufacturing sector, in particular, is important for creating large-scale decent employment opportunities with better wages and labour conditions, and generating linkages with other sectors and spill-over effects (UNIDO, 2013). In this paper, we focus on the impact of Black Economic Empowerment (BEE) and industrial policy on empowerment and transformation within the manufacturing sector.

A significant challenge in South Africa is the entrenched structure of the economy. Table 1 shows that the opening of the economy failed to result in a significant change in the export profile of the economy, and resource-based exports (including basic metals and chemicals) are still prevalent. More generally, South Africa has performed poorly in terms of diversification and industrialisation post-apartheid[2], even when compared to other upper-middle-income countries (Andreoni & Tregenna, 2018).

[2] The contribution of manufacturing to GDP in South Africa declined from 21% in 1994 to 14% in 2018.

Table 1: Share of merchandise exports, %



Source: Quantec

In addition, the concentration of ownership and control, with a small number of firms dominating key sectors (as a result of the conglomeration of capital under capital controls during apartheid), remains a significant challenge to the economy (Roberts, 2017). Concentration is a challenge for inclusion and entry – market power within concentrated industries raises barriers to entry, impacting on the entry of potentially innovative firms that could improve the competitiveness of the industry. It also reduces the incentives for large firms to invest in upgrading, thereby undermining capability development and decent employment creation.

How to create decent jobs for all in a more resilient manufacturing sector remains a key policy concern, given the systemic exclusion and suppression of black people from access to critical productive resources, including capital, land, product markets and manufacturing jobs in the apartheid era (World Bank, 2018). The BEE policy, now Broad-Based Black Economic Empowerment (BBBEE), is a policy of successive post-apartheid governments to make corrections for the ills of apartheid and to bring about critical transformation in the ownership and control of productive assets in the economy (Ponte, Roberts & Van Stittert, 2007; Vilakazi & Ponte, 2020).

The literature on BEE is expansive, with a plethora of evidence examining the BEE policy and its consequences (see, for instance, Mondliwa & Roberts, 2020; Olivier & Bracking, 2017; Vilakazi & Ponte, 2020). However, there is little in the way of reflection on the impact of BEE policies on transformation in the manufacturing sector and, more generally, on the role BBBEE plays in enhancing and/or inhibiting the industrial development and growth of black-owned manufacturing firms in South Africa.

In this paper, we synthesise the available evidence on BBBEE in the manufacturing sector and argue that BEE policies are not sufficient for empowerment, transformation and inclusion in the South African manufacturing sector. Specifically, we advance the argument that transformation in manufacturing requires that various instruments of industrial policy work together to drive inclusion that goes beyond transfers of ownership. Given South Africa's particular context of entrenched big firms and a bias towards upstream manufacturing industries, industrialisation

in the South African context means supporting the entry of diverse and labour-absorbing firms in downstream industries. That is, supporting the establishment and development of new and emerging (black) manufacturing businesses is a key part of industrialisation.[3] South Africa's broader empowerment and transformation policies, such as the promotion of learning and capability development of black industrialists, are thus pivotal, not only in their own right but also as a means towards greater diversification, industrialisation and development.

The remainder of the paper is structured as follows. The second section reflects on the impact of BEE policies on inclusion and entry in the economy, while the section following that considers the available evidence on transformation and empowerment within the manufacturing sector of South Africa. In the fourth section, we critique the impact of industrial policy instruments and stances on economic empowerment in the South African manufacturing sector. We critically review industrial policy initiatives of government that have focused on manufacturing, and assess whether the instruments have performed well together, if at all, as tools to counteract entrenched economic power in value chains and support entry and transformation in the manufacturing sector. We also consider how government has engaged with big business and whether state-business relations have compromised the implementation of industrial policy and entry of dynamic firms at the downstream level. Finally, we draw some conclusions and policy implications.

Empowerment within the current Black Economic Empowerment (BEE) framework[4]

While the need for economic transformation and inclusion of those previously kept outside of economic opportunities was recognised with the advent of democracy in 1994, there was no formal policy around black economic empowerment in the 1990s.[5] As a result, the system for economic empowerment of previously disadvantaged citizens was voluntary in the early post-apartheid years. Between 1994 and 2003, economic empowerment took the form of several "BEE deals", that is, transactions through which BEE firms and consortia would acquire stakes in existing firms as BEE partners. There were several problems with this approach, including that white businesses were offloading non-core business assets to empowerment partners in highly leveraged transactions. Furthermore, very few black people had access to capital to make these investments, with the result that a few black companies and individuals emerged as leading partners for various deals. As there was no formal policy in place, there was not a mandatory push to change the structure of the economy (Vilakazi & Bosiu, 2021).

With the promulgation of the Broad-Based Black Economic Empowerment Act (BBBEE) of 2003, "black empowerment" was expanded to include seven dimensions of empowerment – ownership, management representation, employment equity, skills development, preferential procurement, enterprise development and corporate social investment. Furthermore, the Codes of Good Practice provided the basis for empowerment scorecards against which a firm's empowerment credentials could be measured when competing for government contracts.

But compliance was still not compulsory, and many private sector companies did not have to comply because they had relatively small turnovers (BBBEE Commission, 2017a; Tangri & Southall, 2008). In addition, large companies could score points for spending on corporate social investment schemes that were not related to their core activities, which meant that they were getting "empowerment" points without spending resources on incorporating black businesses or individuals into their value chains (Bracking, 2019). The creation of the scorecard system has turned empowerment into a "technical exercise" that has led to a focus on compliance rather than substantive change (Ponte et al., 2007; Vilakazi & Bosiu, 2021).

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[3] Evidence shows that black-owned enterprises operate in the micro, small and medium-sized enterprises (MSME) sector that is experiencing low growth in South Africa (IFC, 2018).
[4] This section draws mainly from Vilakazi and Bosiu (2021).
[5] See Ponte et al. (2007) and Mondliwa and Roberts (2020) for historical discussions on the BEE/B-BBEE policy.

In the light of the slow process of actual transformation, the 2013 BBBEE Amendment Act resulted in a number of changes. Such changes included measures to enhance compliance by public entities, strengthening of enforcement, monitoring and evaluation of BEE, a new and specific definition of fronting together with penalties[6], and incentive schemes to support black-owned and managed businesses. Amendments to the Codes of Good Practice in 2015 reduced the scorecard to 5 elements (from 7) and set minimum targets of 40% on ownership, skills development, and enterprise and supplier development.

While the changes have been welcome given the poor progress with transformation, many studies have argued that the approach to empowerment through the BEE system has been problematic. There is no clear strategy to deal with the power of entrenched large firms and high barriers to entry in the context of significant concentration and the very real and complex challenges of building new and dynamic black businesses (Chabane, Goldstein & Roberts, 2006; Hamann, Khagram & Rohan, 2008; Bell, Goga, Mondliwa & Roberts, 2018).

There is also a significant challenge with including black capitalists in the ownership and management of existing large businesses, in that it has served to entrench the position of incumbents. Aligning the interests of the emerging black middle class with the interests of existing white firms has been to the detriment of broader transformation because it "has made it far less likely that black capitalists will agitate for more extensive reforms to address the entrenched racial skewing of capital ownership" (Vilakazi & Bosiu, 2021). The BEE project has thus been part of South Africa's "elite transition" (Bond, 2000), in which a small black elite with strong political links has joined with historically entrenched white businesses. There is then an incentive to protect the interests of those businesses. What is rather required is an opening of the economy to support entry and expansion of new and dynamic businesses (Vilakazi, Goga & Roberts, 2020).

Some studies show that the BEE system, as an instrument for transformation, counter to its aim, has actually served to obscure the extent of real transformation. For instance, in the fisheries sector, Vilakazi and Ponte (2020) find that while the main companies in the hake sector have complied with the government's prescriptions and outperformed firms in other sectors, there has been very little real transformation and entry in value-added downstream activities. Other studies show that BBBEE policies have played a role in maintaining the market power of incumbents (see Mondliwa & Roberts, 2020, for case studies on liquid fuels and telecom industries). The World Bank (2018) finds similar results suggesting that government interventions often inadvertently protect incumbents, and thereby undermine competition and racial inclusion.

Meaningful participation and entry into the economy require engagement with several realities. There are high barriers to entry in many sectors of the economy, and particularly for black businesses because of a plethora of reasons, including that black businesses are excluded from well-established networks and value chains, and access to finance is a real problem (Vilakazi et al., 2020). Considered together with other challenges, including anticompetitive behaviour and strategic conduct by incumbent firms, high switching costs in some industries, challenges in accessing routes to market and structural features in industries like finance, banking and telecoms, it is clear that the odds are stacked high against new and black entrants in many sectors.

What is required to support entry and entrants is a broader policy agenda than what the still narrow provisions of the evolving conception of BEE have been able to provide. The dynamics of specific sectors and value chains, and the specific challenges within them, need to be grappled with to build purposeful policies.

Black empowerment within the manufacturing sector

[6] A practice where black business partners are brought in as 'nameplate' partners to win contracts and create the perception of compliance.

This section reflects on the performance of the BEE policy, with a focus on the manufacturing sector. We do this by looking at the evidence available in recent BBBEE Commission reports[7] as well as in the empirical literature. In general, the BBBEE Commission reports conduct analyses on the status and performance of BBBEE by focusing on uploaded BBBEE certificates and compliance reports submitted in a calendar year.

BBBEE performance is measured using the Code of Good Practice 100 to 500 generic scorecard for different elements. This is then used to assign a BBBEE status level. The five elements (revised in 2013 from seven) under the Code of Good Practice are ownership; management control; enterprise and supplier development; socio-economic development; and skills development (see BBBEE Commission, 2020a; BBBEE Commission, 2020b). Of these, ownership, enterprise and supplier development and skills development are considered the "priority elements" (BBBEE Commission, 2018). There are eight status levels with the ninth being the non-compliant level. BBBEE status level 1 depicts that the sector and/or firm attained an average score of ≥100 on the generic scorecard with BBBEE recognition level of 135%, while level 8 depicts an average score of ≥40 but <55 on the generic scorecard with recognition level of 10%. That is, BBBEE status level 1 entities receive 135% recognition during procurement while level 8 entities receive 10% procurement recognition. Non-compliant entities (<40 points on the generic scorecard) receive 0% procurement recognition.[8]

In practice, annual assessments are done by an accredited BBBEE verification agency who issues an annual BBBEE certificate confirming the entity's status.[9] The BBBEE codes define three main types of entities: Exempted micro-enterprises (EMEs), Qualifying Small Enterprises (QSEs), and Large Entities.[10] EMEs and start-ups (less than a year old) are automatically assigned level 4 BBBEE status. EMEs and QSEs with 100% black ownership are assigned level 1 BBBEE status, while those with 51% or more black ownership are assigned level 2 BBBEE status.[11] EMEs and QSEs do not require certificates to confirm their BBBEE status.

The analysis below is based on BBBEE certificates uploaded onto the BBBEE Certificates Portal System by accredited verification agencies and BBBEE Compliance Reports submitted by all reporting entities.

Empowerment based on BBBEE certificates

Firstly, the recent national status and trends report by the BBBEE Commission shows an increase in the number of total BBBEE certificates uploaded in the portal from 1674 in 2018 to 5818 in 2019, suggesting an increase in compliance by entities in 2019 (BBBEE Commission, 2020a).[12] In 2017, a total of 2861 entities (1139 EMEs, 851 QSEs and 871 large entities) were reported to have uploaded their BBBEE Certificates on the portal (BBBEE Commission, 2018). It is not clear why there was an increase in BBBEE certificates uploaded in 2019 compared with 2018. The significant drop in the number of uploaded certificates in 2018, relative to 2017, is attributable to the amendment of the BBBEE Act that no longer required EMEs and QSEs with 51% or more black ownership to verify and upload BBBEE certificates (BBBEE Commission, 2019).

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[7] For all the B-BBEE Commission annual reports, see https://www.bbbeecommission.co.za/research-reports/

[8] See appendices 1 and 2 for details on the B-BBEE generic scorecard and recognition levels.

[9] All organs of state and public entities, entities listed on the Johannesburg Stock Exchange (JSE), and all Sectoral Education and Training Authorities (SETAs) are required to report their compliance to the BBBEE Act (BEE Commission, 2020a)

[10] EMEs are entities with an annual total revenue of R10 million or less. The threshold for being a Qualifying Small Enterprise ("QSE") is an annual total revenue of between R10 million and R50 million, while that of Large Enterprises is R50 million or more.

[11] See https://www.werksmans.com/wp-content/uploads/2018/11/BBBEE-Codes-Explained.pdf.

[12] In 2019, 411 EMEs, 2 057 QSEs, and 3 350 Large Entities uploaded their B-BBEE certificates.

Overall though, the results in terms of compliance are quite low over the years, with various sectors underperforming in 2019 (BBBEE Commission, 2020a; BBBEE Commission, 2020b). Only 42% of all JSE listed entities, compared with 15% of organs of state and public entities, reported their BEE status in compliance with the Act (BBBEE Commission, 2020a).

Considering ownership of firms, less than one third of firms (constituting about 29% of all submitted certificates) are on average black-owned, although this is an increase from 25% in 2018 and 28% in 2017 (BBBEE Commission, 2020a). Further, when we consider the other four elements other than ownership, we observe slow progress across the board (BBBEE Commission, 2020a). Year-on-year comparisons show poor results, with compliance dropping for three out of the four elements. For instance, the data shows that the average management control points (as a percentage of total management control points) decreased from 45% in 2018 to 39% in 2019, suggesting retrogression in terms of inclusion at the management level, despite a slight increase in black ownership over the same period. Enterprise and supplier development also experienced a significant decrease from 60% in 2018 to 51% in 2019, while socio-economic development experienced a decrease from 71% in 2018 to 68% in 2019. Skills development remained the same at 49% in both years (BBBEE Commission, 2020a).

Empowerment within JSE-listed companies and organs of state & public entities

Although reporting of BEE status for JSE-listed companies is mandatory, only 42% of all listed entities and 15% of organs of state and public entities reported their BEE status in 2019 (BBBEE Commission, 2020a). Further, only just over half (53%) of JSE-listed companies reported to have achieved the target points for priority elements in 2019, dropping from 60% in 2018.

In terms of BBBEE levels achieved by JSE-listed companies, the data firstly shows an increase in non-compliance by both JSE-listed companies (18.01% in 2018 to 25.33% in 2019) and organs of state and public entities (17% in 2018 to 39.53% in 2019) (BBBEE Commission, 2020a). For JSE-listed companies, the percentage of firms rated level 1 to 4 declined slightly from 50.93% in 2018 to 49.33% in 2019, while those rated levels 5 to 8 increased from 26.10% in 2018 to 34% in 2019. Organs of state and public entities rated level 1 to 4 also declined from 45% in 2018 to 32.56% in 2019, and those rated level 5 to 8 declined from 37% in 2018 to 27.91% in 2019. These findings suggest a drop in full compliance by organs of state and public entities, as well as JSE-listed entities.

B-BBEE transactions and empowerment in manufacturing

Similar underperformance is observed in the manufacturing sector as well, when we use the recently published major BBBEE transactions analysis report 2018/2019. This is the first report that compares major BBBEE transactions by DTI codes of good practice and Stats SA classification. As a result, there are no comparative data per Stats SA sectors, including manufacturing, for previous years. The report shows that the manufacturing sector lagged behind all major sectors, such as finance and business services, electricity, gas and water, transport, storage and communication as well construction, in the total value of transactions that were registered in 2018/2019. The available data for 2018/2019, as reported in Table 2, shows the dominance of the finance and business services sector in terms of the total value of transactions registered of about R44,155 billion (BBBEE Commission, 2020b).[13]

[13] The report suggests that the high performance level of finance and business services sector is due to the unique characteristics of the sector's transactions in 2018/2019 and the skewed comparative base registered in 2017/18 (B-BBEE Commission, 2020b).

Table 2: Value creation by Stats SA Sectors in 2018/2019 (R' Billion)

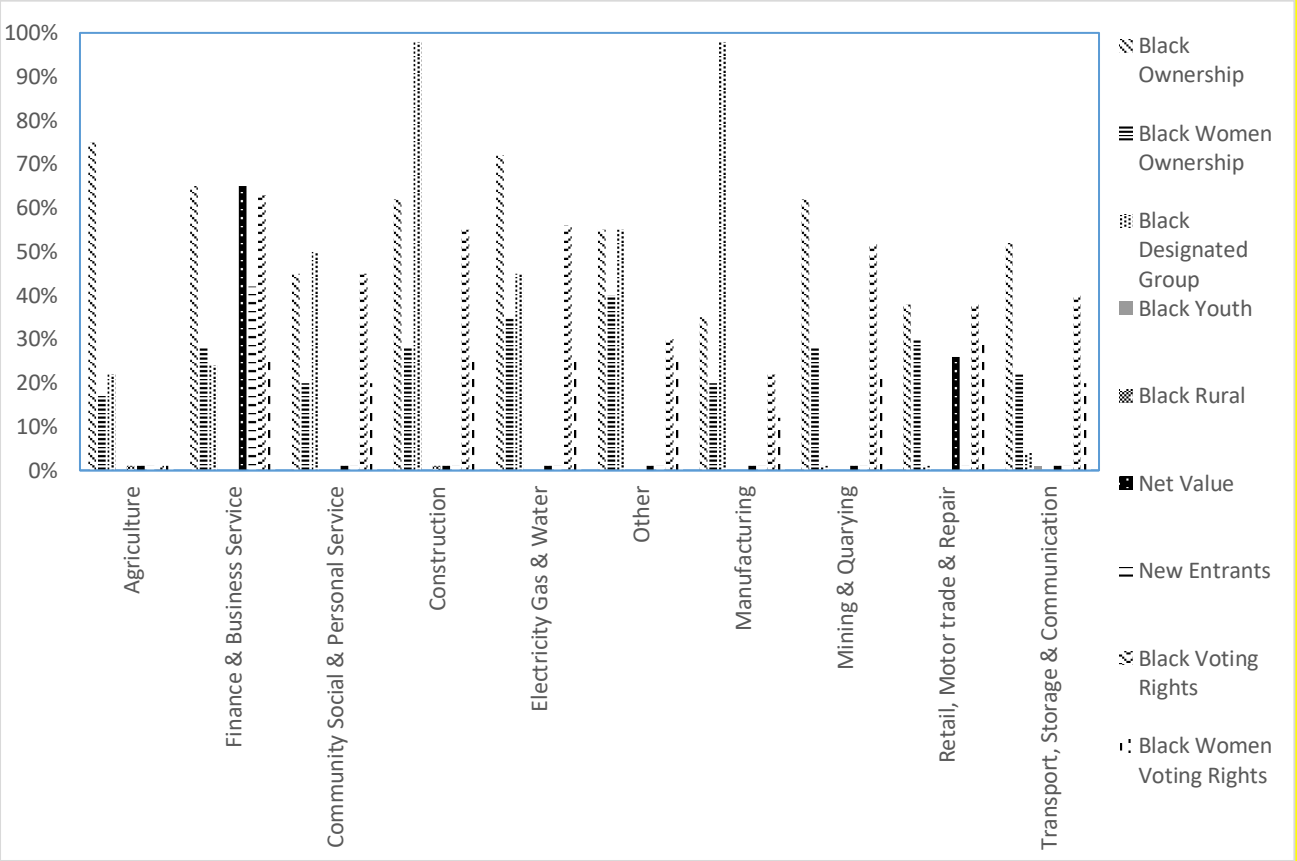
Sector	Amount	Percentage
Agriculture	0 523	0.467
Community, social and personal	0 945	0.844
Construction	2 814	2.514
Electricity, gas and water	36 310	32.438
Finance and business services	44 155	39.446
Manufacturing	1 792	1.601
Mining	0 438	0.391
Other	6 311	5.638
Retail, motor trade and repair	0 204	0.182
Transport, storage and communication	18 446	16.479
Total	111 938	100

Source: BBBEE Commission (2020b)

Notes: There were 95 transactions for 2018/2019, affecting 264 organisations of which 136 companies' empowerment credentials were validated.

Figure 1 shows that the manufacturing sector has the lowest proportion of black-owned firms of about 32% in 2019, compared with sectors such as agriculture, electricity, gas and water, finance, construction and mining that have high ownership levels above 60% (BBBEE Commission, 2020b). While these high-ownership levels are found to have little correlation with management control of firms in these sectors (BBBEE Commission, 2020b), the manufacturing sector in South Africa shows little inclusive transformation in both ownership and management control.

Figure 1: BBBEE ownership levels in 2018/2019 by Stats SA sectors

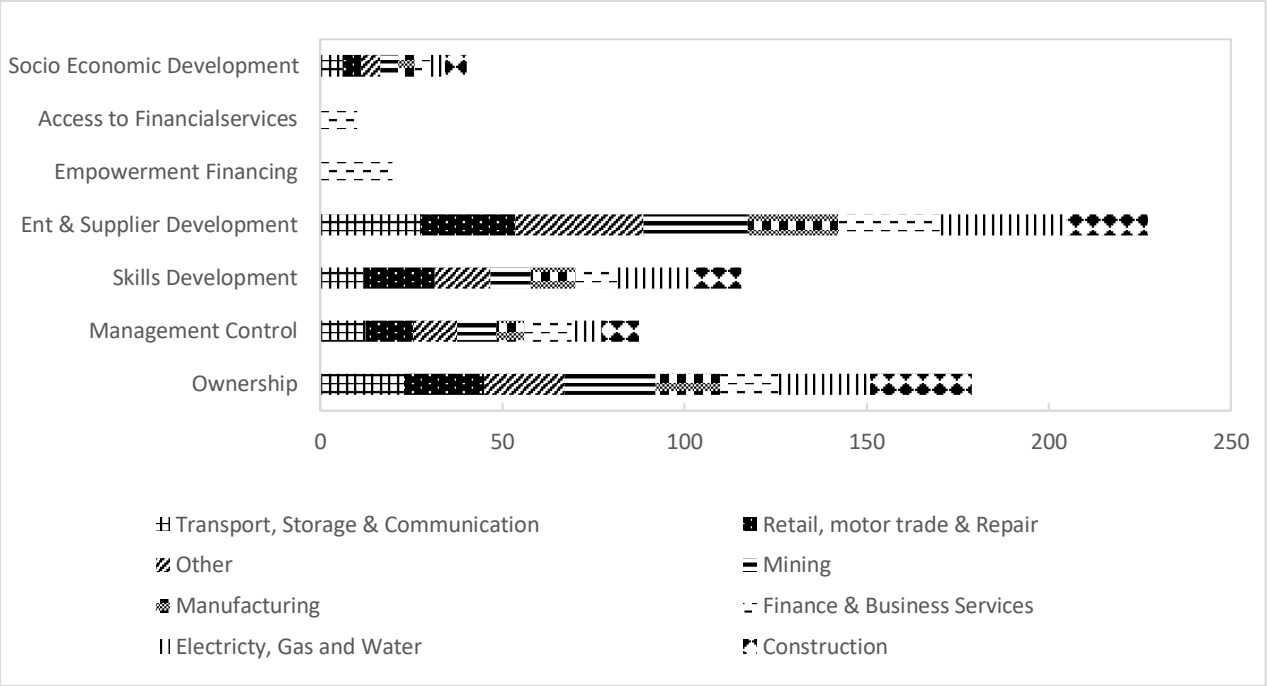


Source: Authors' elaboration based on data in BBBEE Commission (2020b)

Figure 2 shows the performance of sectors across all elements. Considering the manufacturing sector, Figure 2 shows average points of about 17.69 (out of 25) for ownership, 7.77 (out of 15) for management control, 12.4 (out of 20) for skills development, 24.83 (out of 40) for enterprise and supplier development and 4.52 (out of 5) points for socio-economic development.[14] These suggest a higher performance in socio-economic development, ownership, skills development and enterprise and supplier development but underperformance in management control of manufacturing activities (BBBEE Commission, 2020b). In contrast, we observe a higher performance across elements in almost all key sectors. For instance, we see more inclusive transformation in the electricity, gas and water sector with 25 points for ownership, 8.25 for management control, 20.64 for skills development, 34.79 for enterprise and supplier development and 4.99 points for socio-economic development.

[14] See Appendix 1 for BBBEE generic scorecard.

Figure 2: BBBEE performance per each element (for major transactions in 2018/2019) by Stats SA sectors



Source: Authors' elaboration based on data in BBBEE Commission (2020b)

Literature on empowerment in manufacturing

The suggestive evidence, from the foregoing, that the BBBEE policy has not been successful in transforming the economic fortunes of South Africa towards an inclusive society exists in the empirical literature as well. In a qualitative study of 14 black entrepreneurs in Durban, Mudenda (2013) finds a mix of results. On the one hand, the author finds that BEE has resulted in the transformation of some black businesses through the creation of and access to key opportunities. On the other hand, BBBEE is not far-reaching and black entrepreneurs still face barriers to entry into white-dominated sectors, resulting in slow transformation of established sectors (Mudenda, 2013).

Other studies also point to the slow pace of transformation within the manufacturing sector. A study by Olivier and Bracking (2017) examines the role of BEE in empowering large- and medium-sized firms using survey data on 132 manufacturing firms in eThekwini in 2013. They found that only about 26% of manufacturing firms are black-owned. Furthermore, manufacturing firms with a higher BEE level (1 and 2) are smaller in terms of the number of employees and tend to be black-owned (Olivier & Bracking, 2017). The authors also find that firms achieving BEE levels of 1 to 3 are less profitable compared to those in higher BEE levels, though they have benefited more from BEE through new contracts, business opportunities and improvements in credibility. In terms of industrial sub-sectors, firms in industries such as non-metallic minerals, clothing and textiles, and paper and furniture have achieved BEE levels 1-3 status (Olivier & Bracking, 2017). The authors find some growth in management positions by black employees in the manufacturing sector, from 30% in 2003 to 37% in 2013.

There is a complicated relationship between BBBEE and economic outcomes. For instance, on the one hand, an increase in foreign direct investment (FDI) and foreign ownership tends to inhibit BEE in the manufacturing sector in eThekwini, given that foreign-owned firms have little incentive to comply with the Codes of Good Practice (Olivier & Bracking, 2017). On the other hand, FDI is critical to the industrial growth, productivity and competitiveness of firms (World Bank, 2018). This impasse brings into the discussion the relationship between FDI and inclusion, and the critical role government has to play in balancing development goals.

In sum, the evidence based on data from the BBBEE reports and the empirical literature show minimal progress, in some cases, and underperformance, in most cases, across private businesses and in the general transformation agenda in South Africa. The evidence also shows manufacturing to be one of the worst-performing sectors in terms of the priority elements as well as in terms of the rand value of BBBEE transactions registered in 2018/2019.

To encourage compliance with BBBEE elements, preferential procurement policies are employed in government tender evaluations. Preferential public procurement is identified as a critical industrial policy tool to promote and empower MSMEs and black-owned manufacturing enterprises to develop, participate in and integrate value chains (Bolton, 2016; IFC, 2018; Lewis & Gasealahwe, 2017; Mondliwa & Roberts, 2020). The available evidence, however, suggests that the use of public procurement to empower MSMEs is having little net effect on the transformation of black-owned businesses and the economy as a whole (Lewis & Gasealahwe, 2017). Criticisms of the policy indicate that awarding of state contracts under the policy only benefits a few politically connected black businesses and entrepreneurs, resulting in favouritism, corruption, cronyism and state capture, among others (Mudenda, 2013; Olivier & Bracking, 2017; Ponte et al., 2007; World Bank, 2018). It could also make firms reliant on government procurement, making them less competitive and innovative, and could generate inefficiencies in the supply chain (Mohamed & Roberts, 2008; World Bank, 2018).

In summary, the evidence provided above suggests that the BBBEE policy has not delivered significant transformation of the South African manufacturing sector and participation of black industrialists. In fact, the available evidence presented in this section corroborates with the wider literature suggesting that the BBBEE policy has not, so far, led to significant transformation of the manufacturing sector in South Africa (see, for instance, Vilakazi & Ponte; 2020; Mondliwa & Roberts, 2020).

Post-apartheid industrial policies and black empowerment

We argue in this section that the industrial policies required to support the building of capabilities by black-owned firms, and entrants generally, and to stimulate investment and integration of black industrialist and manufacturing firms into key value chains, have been absent. If black firms do not exist, or if they cannot survive, then transformation outcomes will not change over time, especially if incumbent firms are already not complying. Key to this has been a lack of the right forms of funding, but also corresponding tariff and incentive frameworks that have not provided the right support for challengers and/or have entrenched the position of largely white-owned, incumbent firms with market power.

Orthodox economic policies emphasise the role of the market in industrialisation and economic development. However, the experiences of countries like the East Asian tigers between the 1960s and 1980s have placed greater focus on the role of the state in pursuing industrialisation and development. The central idea is that industrialisation does not occur automatically, but that a path to industrialisation must be created by pursuing a broad industrial policy strategy that encompasses other policies, such as development finance, and appropriate levels of competition. "Optimal" competition must be created in order to stimulate investment, but conditionalities must be attached in order to ensure desired investment and capability building (Lee, 2019).

We reflect on two specific areas: i) the role of development finance, DTI incentives, and the tariff regime on capability development in new and emerging manufacturing businesses; and ii) how government has engaged with the power of entrenched firms and the implications of this on value chains and entry of firms in the economy. The analysis in this section draws on a range of experiences from different manufacturing industries.

Implications of industrial policies for empowerment

Financing and incentives

Investments in productive capacity and technological sophistication are key for structural transformation (Team, 2005). Since innovation is incremental and firms need time to learn and build capabilities, public funding plays a

crucial role (Lee, Szapiro & Mao, 2018; Mazzucato, 2013). In South Africa, investments in manufacturing are hampered by high levels of concentration and barriers to entry, which impact on entry of potentially innovative firms. Rivals are important since they bring new products and business models, and spur incumbents to invest in order to improve their own offerings (Vilakazi et al., 2020). Public funding through incentive schemes and development finance are therefore crucial for manufacturing transformation in South Africa.

DTI Incentives: Incentive schemes for industrial policy are key in supporting the entry and expansion of dynamic diversified manufacturing businesses. Since 1994, there have been several programmes, policies, initiatives and incentives directed towards the development of the manufacturing sector. During the 1994 – 2015 period, R57.9 billion (R85 billion in 2015/16) was dedicated towards the promotion and development of the manufacturing sector; about 60% of this was through expenditure and about 40% through tax expenditure (PBO, 2016). Despite this, the composition of manufacturing exports has not changed significantly (see **Error! Reference source not found.** above) and the sector's employment levels have fallen (PBO, 2016).

While there was a range of incentives to promote investment, exports and technological improvements in the 2000 to 2008 period, these incentives targeted the same industries that received support from the apartheid government, and were oriented towards more capital-intensive industries. Therefore, they played little role in changing the structure of the economy (Andreoni, Mondliwa, Roberts & Tregenna, 2021); Black, Craig & Dunne, 2016; Mondliwa & Roberts, 2019;). In the 2008-2018 period, the updated automotive industry incentive programme continued to disproportionately benefit multinational original equipment manufacturers (OEMs) and there was limited linkage building with automotive component sectors. Furthermore, incentives to support recovery from the recession associated with the 2008 global financial crisis, such as the Manufacturing Competitiveness Enhancement Programme (MCEP)[15], also flowed to established firms and financed investments that would have taken place anyway (Beare, Mondliwa, Robb & Roberts, 2014).

There were two significant challenges with the design of the MCEP programme. Firstly, firms had to finance the investment and then claim back from government. This meant that firms that were supported already had access to funding (Andreoni et al., 2021). Secondly, smaller firms found it disproportionately difficult to apply for incentives due to the complexity and bureaucracy of the process, while larger firms with greater access to resources often used consultants to manage the process. This meant that their probability of success increased and, tom some extent, may account for the large firm bias in grants awarded (Beare et al., 2014).

A more recent incentive scheme focusing specifically on black industrialists is the Black Industrialists Scheme (BIS). It was launched in 2016 and aimed to broaden the participation of black industrialists within the manufacturing sector through access to capital and markets. Concessional funding (grant plus debt) is a key feature of the BIS; the DTIC provides a cost-sharing grant of between 30% and 50% of the required investment of the project to a cap of R50 million, with the amount of the contribution based on the combined performance concerning black ownership and economic benefit criteria (Vilakazi & Bosiu, 2021).

There are a few things to note. Firstly, the broad qualifying criteria (scale of the project and potential contribution to the economy) implies a focus on firms that have already overcome the initial learning challenges and are growing and building capabilities towards becoming effective competitors.[16] The scheme, therefore, is targeting black industrialists who can operate as significant challenger firms. Secondly, the claims-based system rewards entrepreneurs that already have access to capital. While this helps to avoid diversification of funds by firms for other

[15] The MCEP was introduced in 2012 in response to low investments in the manufacturing sector following the 2008 recession and was available to all manufacturing industries. In the 2012-2016 period, the MCEP programme was the key action programme under the Industrial Financing pillar of the Industrial Policy Action Plan (IPAP) and its aim was to increase industrial competitiveness through better access to financial capital.

[16] Projects with a minimum investment of R30 million are sought through the scheme.

uses, this is a significant challenge for firms that do not have access to capital. While there are still challenges in terms of access to finance by black industrialists, the design of the scheme and early results show an important shift in thinking about the role of industrial policy in driving inclusion and capability development (Vilakazi & Bosiu, 2021).

Overall, the Department of Trade, Industry and Competition's (DTIC) incentives budget has declined by 19% in real terms between 2012/13 and 2018/19 (Andreoni et al., 2021). This is a significant challenge for entry and expansion of firms and, therefore, to transformation within manufacturing. Furthermore, more generally, the design of incentive schemes has been a challenge. Incentive schemes need to be designed to spur productive changes and support capabilities development, and need to have robust and enforceable conditionalities (Andreoni et al., 2021).

Development finance: A plethora of evidence exists suggesting that young, micro and small firms are the main creators of employment (see, for instance, ILO, 2016; Lewis & Gasealahwe, 2017; SEDA, 2012; World Bank, 2018) and are key drivers of entrepreneurship and inclusive growth (Lewis & Gasealahwe, 2017; SEDA, 2012). Therefore, policies (both government and corporate) that aim to create an enabling environment and empower black-owned manufacturing enterprises to grow are fundamental and key for job creation, industrial growth and an inclusive society.

In South Africa, small to medium businesses struggle to access finance from private financial institutions and the commercial banking sector has been oriented towards funding for consumption rather than investment (Goga, Bosiu & Bell, 2019b; IFC, 2018). Given the failure of markets to provide adequate finance in many countries, development finance institutions (DFIs) or national development banks have stepped in to provide much-needed industrial finance at discounted rates.

In this context, the role of the Industrial Development Corporation (IDC) is crucial in supporting both entry and expansion of new and emerging manufacturing businesses in the economy, and fostering structural transformation and inclusive growth (Goga et al., 2019a). The Korean experience, for instance, highlights the role of finance as a critical policy tool that works together with other policies for productive investments. The nature of finance is critical and, in Korea, this included the provision of loans to SMEs in technology-intensive sectors without requiring much collateral (Lee, 2019).

South Africa's main development finance institution, the IDC, has reinforced the existing industrial structure by continuing to provide funding to upstream resource-based sectors in the metals and chemicals sectors, with funding for diversification and inclusion not featuring as prominently. This is despite the introduction of a more targeted industrial policy through the National Industrial Policy Framework (NIPF) in 2007 and associated Industrial Policy Action Plans (IPAPs) (Goga et al., 2019).

Furthermore, funding by the IDC has been skewed towards bigger businesses – loans have relatively short repayment periods compared to international standards and the IDC's general loan-funding stream does not provide concessional rates. The IDC does have a number of concessional schemes under which it provides concessional finance, although the impact of these has been limited (Goga et al., 2019).

The IDC could do significantly more to provide finance for a larger number of riskier manufacturing investments. Although it is important to assess the potential for firms to be effective competitors (with the offering, scale and expertise required), the IDC should provide long-term finance for the necessary learning and capability development to those that meet the criteria, with the recognition that some will inevitably fail. While it is not possible to predict which manufacturing firms will fail, it is important to support contestation between rivals, as this is part of the process of building capabilities and, therefore, more competitive industries.

Patient capital and concessional rates play a critical role in ensuring that manufacturing MSMEs have sufficient time to build capabilities to compete with established incumbents, particularly in sectors where scale is important. These

are required to help start-ups overcome the challenge of incurring losses in the first few years of operation before they have built up capabilities and become profitable. The overall inability of the IDC to extend sufficient support and concessional support (lower interest rates and longer repayment periods than the private banking sector) is a significant challenge for new entrants and SMEs to becoming effective participants in the manufacturing economy.

This is particularly so since South Africa has a history of entrenched manufacturing businesses, which makes entry at different points of value chains all the more difficult. Thus, in the context of significant concentration in the economy, concessional funding is critical and necessary to level the playing field and ensure that entrants and SMEs not only are sustainably integrated into different stages of value chains in the economy, but also become effective competitors to large incumbent firms.[17,18]

The trade regime: Tariffs are part of a suite of industrial policy instruments that can be used to stimulate investment for development of manufacturing industries, although conditionalities on support are crucial. The tariff reform programme of the 1990s resulted in an extensive and widespread reduction of tariffs. The objective of the programme was to raise competitiveness of the manufacturing sector and to loosen the stranglehold on upstream industries, including basic chemicals and iron and steel (Walwyn, 2019). The steel and chemicals industries are of particular importance to manufacturing in South Africa, as steel and polymers are key input products to a range of diversified downstream manufacturing industries. In South Africa, both steel and polymers have a single dominant local producer (Banda, Tobb, Roberts & Vilakazi, 2015; Zalk, 2014).

In practice, tariff cuts resulted in a weakening of several manufacturing industries, as companies struggled to remain competitive in the face of international competition and a lack of support to build capabilities (Black & Roberts, 2009). Furthermore, in important value chains such as metals and machinery, despite tariff cuts across the board, downstream producers have been more affected. This is partly as a result of the intrinsic nature of industries in the value chain[19], but also because tariff support has been more supportive of upstream steal than downstream diversified industries. For instance, in 2016, the dominant upstream steel producer Arcelor Mittal South Africa (AMSA) was awarded tariff support as a result of the impact of the steel price downturn on the industry. This increased the cost of steel for the downstream fabricating industry, making their products less competitive. Downstream industries have not received the same kind of tariff support (Goga & Mondliwa, 2021).

The tariffs and general support for AMSA have come at the cost of building a more robust and dynamic downstream industry. In essence, while South Africa could have capitalised on significant capabilities in the upstream steel sector, in order to support the entry of new firms for the purpose of structural transformation and broader transformation, it has continued to support upstream firms. The tariff regime has thus worked against structural transformation and broader transformation within the metals-to-machinery value chain. More generally, there needs to be a rebalancing of tariffs within the broader industrial policy system for the purposes of growing manufacturing industries by spurring entry of new and dynamic businesses. This is expected to result in more black businesses and better transformation outcomes.

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17 https://www.competition.org.za/ccred-blog-thinkingaheadsa/2020/4/30/the-nature-of-funding-matters-making-development-finance-work-for-south-africas-smes-in-the-covid-19-crisis.

18 The Development Bank of South Africa (DBSA) primarily funds government infrastructure initiatives and has seen real disbursements in the economy increasing significantly since 1995, with municipalities accounting for the majority of funding. While services to households were the main focus of funding in the period to 2007, more recently the DBSA has focused much more on funding energy projects. Overall, there is significant room for scaling up DBSA's infrastructure investments, but like the IDC, the DBSA generates its own funds (Goga et al., 2019b).

19 Cuts had a limited impact on large integrated carbon steel producers due to "natural" protection arising from the high logistics costs of imported steel (Zalk, 2017)

Engaging with the power of entrenched firms

In the context of significant entrenchment of large incumbent manufacturing businesses in South Africa, government's ability to engage effectively with "big business" has a profound impact on the economy. There is a tension between large firms and development outcomes. The market power that large firms possess can be used to exploit advantages over downstream buyers or upstream suppliers, or to compete unfairly against rivals (Gerber, 2010). Large manufacturing firms thus govern the value chains in which they are present, shaping which firms are able to play within the value chain and outcomes. Their conduct and orientation are biased against inclusion of MSMEs, generally, and black firms, specifically. The data above shows that the average enterprise and supplier development points (as a percentage of total points) decreased from 60% in 2018 to 51% in 2019.

Since 1994, concentration and vertical integration within sectors in South Africa has increased. Large and lead firms have established themselves firmly as leaders in their specific manufacturing sectors. This has enabled them to direct the sector's investment decisions, restrict barriers to entry through strategic mergers and acquisitions and engage in anticompetitive behaviour. They have used a variety of tactics including integration, strategic conduct and lobbying to expand or maintain their market shares and extract rents (Goga, Mondliwa & Roberts, 2020; Buthelezi, Mtani & Mncube, 2019. The conduct of large firms in various sectors has thus impacted on transformation within various manufacturing subsectors through impacting on the entry of businesses and development of capabilities (see Vilakazi et al., 2020, for case studies on various sectors).

Government has failed to engage with the power of these upstream firms for the benefit of entrants and diversified downstream businesses. We provide some examples of this below. In agro-processing, for instance, there has been significant lobbying by the sugar industry. It has a strong legacy of state support and continues to receive extensive protection; it is the only subsector in agriculture that remains tightly regulated post-apartheid. Protection includes tariffs and mechanisms that set the sugarcane price which feeds into prices for downstream industries. This in turn impacts on the inclusion of black industrialists and smaller players in downstream confectionary because sugar is a key input for downstream confectionaries (Dube, das Nair, Nkhonjera & Tempia, 2018).

In two important value chains of metals-to-machinery and chemicals-to-plastics, the large upstream incumbents (AMSA and Sasol) have used their market power to price inputs (steel and polymers) at import parity, to the detriment of downstream industries. Both competition law and policy decisions have failed to deal with the power of these firms. Furthermore, in the steel industry, AMSA has managed to lobby government aggressively for support during downturns. This includes i) access to cheap iron ore (input) without reciprocal mechanisms to pass benefits on to downstream users when Iscor was internationalised in the early 2000s, and ii) tariff support in the agreement between AMSA and government in 2016 (Goga et al., 2020).

In both the metals-to-machinery and chemicals-to-plastics value chains, while there is significant potential for business and employment growth in the more dynamic and robust downstream industries (Beare et al., 2014), government has remained oriented towards the large entrenched upstream firms. The entrenched firms in these value chains have managed to price excessively without sanction and lobby government successfully to support them without conditions that require support to benefit the broader value chain (Goga et al., 2020; Mondliwa & Roberts, 2019).

Government's actions in the metals-to-machinery and chemicals-to-plastics industry show that industrial policy remains biased towards large and entrenched upstream firms. While there is a range of policies for downstream development, the weight of support has been skewed towards entrenched firms and there has been an inability to discipline large entrenched firms effectively (Goga et al., 2020; Mondliwa, Goga & Roberts, 2021). However, the state is fragmented and how government acts (policies, laws and regulations pursued) is also influenced by powerful groups. The state is therefore an arena in which powerful interests are contested.

Conclusion

South Africa's manufacturing sector continues to struggle in terms of increasing manufacturing value added and employment. At the same time, there has been entrenched economic exclusion of black entrepreneurs from the manufacturing sector. Originally caused by apartheid-era policies, the continued exclusion of new and emerging dynamic (black) manufacturing businesses post-apartheid affects the industrial growth and the sustainability of the industrial sector in South Africa. However, several policies have attempted to make corrections for the historical injustice and drive a more inclusive economy in the new South Africa. One such policy is the broad-based black economic empowerment (BBBEE) policy.

This paper examines the black economic empowerment policy within the manufacturing sector by synthesising the available evidence. It considers the role of BBBEE policy in transforming the structure of the manufacturing sector in South Africa. It also examines the impact of various industrial policy tools and measures, such as development finance, incentive schemes and use of tariffs pursued by government to drive "black" manufacturing transformation in South Africa.

Our overall finding suggests that the BBBEE policy has fallen short as an instrument designed to transform manufacturing and empower black industrialists in South Africa. We find that the BBBEE policy has served, in some cases, to obscure the real industrial transformation process in South Africa. We argue that growth in "black" manufacturing is hampered by, among other challenges, high levels of concentration, barriers to entry and lack of access to capital. The persistence of these challenges prevents black entrepreneurs from participating in product markets, thereby maintaining the status quo of highly concentrated markets made up of a few dominant white-owned firms (Vilakazi et al., 2020).

Our analysis of industrial policy tools and measures, though broad brush, is not encouraging. While the evidence suggests that there are a number of tools that have been used to foster entry and capability development of black industrialists, they have fallen short. We find that this is sometimes because they have been captured by other private interests and incumbents to the detriment of downstream producers and better inclusion. As a result, we argue that government, in some cases, has inadvertently played a role in maintaining the status quo by granting support and incentives that protect and benefit incumbents, while undermining competition and inclusion in the manufacturing sector. Furthermore, when considering the various industrial policy tools together, it is clear that there has been little coordination of policy, and that policies pull in different directions.

Transformation policies needs to engage the challenges black industrialists face in the manufacturing sector, and then apply appropriate tools in a coordinated manner to open up markets and support inclusion. This requires better coordination of policies that support coordinated investments along value chains and within clusters (Mondliwa et al., 2021). This also includes tackling abuse of market power by upstream firms, changing regulations to open markets and providing effective support (finance, incentives, tariff support, support for technology development) for capabilities development (Vilakazi et al, 2020).

The BBBEE policy must go beyond pushing for entry into traditional sectors for black industrialists to providing opportunities for the identification and development of new industries and sectors with high growth potential. These policies could be supported by other policies that foster innovation and development of skills, including entrepreneurial capabilities (Lloyd, 2018).

Although the paper presents a review of transformation within manufacturing, further in-depth studies looking at the impact of policies (including BEE, trade and industrial policies) on sectors and sub-sectors (in the context of differences, including different forms of ownership) will provide a much richer understanding of empowerment and transformation in South Africa. The scant nature of data on transformation within the manufacturing sector by Stats SA sectors (only reported in the latest version of the BEE report), and the descriptive nature of the evidence provided in the paper, limits this paper. Given the importance of the manufacturing sector to the sustainable

development agenda of South Africa, there is a need for a robust analysis of data to provide evidence-based policy insights on the effects of BEE on the performance of the manufacturing sector. This may be possible in a future study through the analysis of the *Who Owns Whom data*[20] and data on procurement processes. Our findings do, however, provide critical first-level evidence that synthesises and provides understanding of the effect of BBBEE policy on the manufacturing sector in South Africa.

[20] https://www.whoownswhom.co.za/

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Appendices

Appendix 1

Table 3: BBBEE generic scorecard

Element	Weighting	Code series reference
Ownership	25 points	100
Management control	15 points	200
Skills development	20 points	300
Enterprise and supplier development	40 points	400
Socio-economic development	5 points	500

Source: DTI (2013)

Appendix 2

Table 4: BBBEE recognition levels

BBBEE status	Qualification	BBBEE recognition level
Level one contributor	≥ 100 points on the generic scorecard	135%
Level two contributor	≥ 95 but < 100 points on the generic scorecard	125%
Level three contributor	≥ 90 but <95 points on the generic scorecard	110%
Level four contributor	≥ 80 but <90 points on the generic scorecard	100%
Level five contributor	≥ 75 but <80 points on the generic scorecard	80%
Level six contributor	≥ 70 but <75 points on the generic scorecard	60%
Level seven contributor	≥ 55 but <70 points on the generic scorecard	50%
Level eight contributor	≥ 40 but <55 points on the generic scorecard	10%
Non-compliant contributor	< 40 points on the generic scorecard	0%

Source: DTI (2013)