# Doing Business in South Africa

Today South Africa is one of the world's most sophisticated and most promising emerging markets. A combination of macro-economic and political stability, first class infrastructure and a large market make for an exceptional investment environment.

The many disadvantages to doing business and investing in South Africa which applied during apartheid have been swept away. Instead, the new South Africa is investor friendly with a pent-up entrepreneurial spirit and a wealth of opportunities.

The economic changes and discipline which South Africa has undergone in the past decade have translated into a robust economy which, economists agree, is set for strong growth, despite negative international developments.

Excellent opportunities exist in a variety of sectors. These include tourism (in 2002, South Africa had the fastest growing tourism sector in the world), mining and mineral beneficiation (the country's mineral wealth is legendary), hi-tech industries and communications (one of the fastest growing sectors), manufacturing (manufactured exports have leapt in recent years), agriculture, transport and many other fields.

The costs of doing business in South Africa – labour, land, rental, transportation and general living expenses – all compare favourably to other emerging markets. Plus, as many investors resident in the country, and their executive staff, have discovered, the standard of living, weather and amenities (including golf courses) are second to none.

## Incentives

A range of attractive incentives are offered to potential investors. These include:

- Foreign Investment Grants. Manufacturing and tourism companies (from outside the South African Development Community) are eligible. The grant compensates foreign entrepreneurs for the qualifying costs of moving new machinery and equipment to South Africa. Up to a maximum of R3 million per project is allowed.
- Critical Infrastructure Fund. Large investments in transportation systems, electricity and water distribution, sewerage systems, waste storage, telecommunication networks and fuel supply systems may qualify for funding of 10% to 30% of the development costs.

**Value in Rands of sales of manufactured products for selected manufacturing divisions**

| Manufacturing division | 2000 (in Rands) | 2001 (in Rands) |
|---|---|---|
| Food and food products | 59 693 335 | 67 543 885 |
| Coke and refined petroleum products | 31 823 682 | 37 699 329 |
| Basic chemicals | 21 571 212 | 25 135 080 |
| Other chemical products | 26 327 958 | 29 195 074 |
| Basic iron and steel products | 33 529 317 | 35 607 441 |
| Fabricated metal products | 24 753 734 | 27 341 085 |
| Total machinery and equipment | 19 664 968 | 21 651 027 |
| Total manufacturing* | 448 192 617 | 502 133 244 |

* Total includes all manufacturing divisions.
Source: Stats SA, Manufacturing: Production and Sales

- Strategic Industrial Projects (SIP) incentive package. Allowances, in the form of tax relief, aim to lower the cost of investing in critical industrial projects in South Africa. Proposed projects should be worth R50 million or more. A wide range of manufacturing activities are included, as are various computer-related and research and development activities.
- Skills Support Programme. This is a cash grant for skills development aimed at encouraging investment in training and introducing new advanced skills. Grants may be given to companies engaged in manufacturing, high-value agricultural projects, agro-processing, aquaculture, biotechnology, tourism, information and communication technology, recycling and cultural industries. Up to 50% of the training costs and a maximum of 30% of total salaries of qualifying companies may be granted.

## Spatial Development Initiatives

Spatial Development Initiatives (SDIs) focus high-level resources on areas which have limited economic development and therefore relatively high unemployment, but which also have inherent economic potential.

The SDI programme consists of 11 SDIs and four Industrial Development Zones (IDZs) at varying stages of development. These are located across South Africa and are designed to make the most of local resources, labour and transport facilities (several are in or adjacent to major ports).

One such IDZ currently being created is at Coega in the Eastern Cape province. A deep-water harbour at the centre of this IDZ is being built at a cost of R3,2 billion and is expected to create 10 000 jobs during the construction phase.

IDZs are industrial estates that have duty-free production for exports, provide transport routes, facilities, and services tailored for export-oriented industries. Benefits for investors include exemption from value-added tax (14%) and duty-free import of production-related equipment, raw materials and input for export. Investors may also qualify for incentives such as the SIP.

The 2003 national Budget offered investors several new incentives. These include special depreciation allowances for investments in designated urban areas which will arrest urban decay. Other important new benefits relate to the depreciation of capital equipment.

## Red tape

The South African Government and private sector are committed to facilitating investment in sustainable enterprises in order to raise economic output and employment. An example of the national commitment to achieving this goal is the fact that the Department of Trade and Industry has managed to reduce the time it takes to register a new company or closed corporation from 21 to three days. In 2002, the Department registered close to 30 000 new companies and 107 000 closed corporations.

Logistics experts from the Department's Trade and Investment South Africa assist new investors to get started, ease paperwork and bottlenecks, as well as providing specialised after-care.

Public sector-owned organisations supplying transport and logistics, electricity, postal services, communications and even administrative functions have been corporatised to the point that their levels of customer service are

**Registration of companies**

| Total Registered Entities | 1999 | 2000 | 2001 | 2002 |
|---|---|---|---|---|
| Closed Corporations | 72 265 | 77 000 | 86 396 | 107 300 |
| Public Companies | 438 | 289 | 248 | 221 |
| Private Companies | 26 597 | 29 649 | 27 654 | 29 650 |
| Non Profit (Section 21) | 780 | 980 | 1 344 | 1645 |
| Limited by Guarantee | 0 | 1 | 3 | 0 |
| External Companies | 135 | 117 | 132 | 139 |
| Incorporated (Professionals) | 770 | 840 | 807 | 519 |

Source: Companies and Intellectual Property Registration Office website closely scrutinised. This translates into levels of service which frequently compare with the best in the world.

## Exchange control

Generally, there are no restrictions on the inward or outward transfer of funds of which non-residents are the beneficial owners. Capital invested in South Africa may be freely returned abroad, as can capital and revenue profits, for example, dividends and branch profits. There is generally no limit on the remittance of commissions, director's fees, technical service payments, management fees, or the purchase of technology.

Restrictions still exist with regard to local borrowing by foreign-held companies but these are not onerous and intended simply to ensure that local borrowings are not exploited to remit large-scale profits on minimal capital investments.

## Taxation

Companies are taxed at a rate of 30%. In addition to this, a secondary tax is levied on companies at a rate of 12,5% on all income distributed by way of dividends.

Foreign taxes are credited against South African tax payable on foreign income. Foreign income and taxes are translated into the South African monetary unit, the Rand.

Capital Gains Tax was introduced from 1 October 2001. It forms part of the income tax system and includes capital gains made upon the disposal of assets in taxable income.

Value-added tax (VAT) is levied at a standard rate of 14% on all goods and services subject to certain exemptions, exceptions, deductions and adjustments provided for in the VAT Act.

Transfer duty, estate duty, stamp duty, marketable securities tax, uncertified securities tax, customs duty and excise duty are also levied. Regional Services Councils levy turnover and payroll taxes. However, these taxes are at fairly low rates. Local governments levy rates on the value of fixed property to finance the cost of municipal services.

A formula tax applies to gold-mining companies. Small business corporations (annual turnover of less than R3 million) benefit from a graduated tax rate of 15% on the first R150 000 of taxable income and can write off certain investment expenditure in the year in which it is incurred.

South Africa's financial sector and markets offer world-class service, and outstanding investment opportunities.

## Banking

At the end of December 2001, 53 banks, including 14 branches of foreign banks, and two mutual banks were registered with the Office of the Registrar of Banks. Furthermore, 55 foreign banks had authorised representative offices in South Africa. The banking institutions collectively employed 120 527 workers at 10 437 branches and agencies.

Four major groups dominate the South African banking sector, namely, ABSA Group Limited, Standard Bank Investment Corporation Limited, FirstRand Holdings Limited and Nedcor Limited. These groups maintain extensive branch networks across all nine provinces, and together hold 69,5% of the total assets (R1 047 billion) of the banking sector.

The major banks offer a wide range of services to both individual and corporate customers. Several banks specialise in merchant banking, securities underwriting or other niche areas. Several new banks have been registered and competition has intensified, both among banks and between banks and other financial service-providers

Industry-wide net income after tax rose to 0,7% of total assets in 2001. As a percentage of equity, industry-wide net income after tax decreased from 14% in 1992 to 9,2% in 2001. By the end of 2001, industry-wide net income before taxation had begun to improve, rising to R10,6 billion, compared with R3,1 billion in 1992.

South Africa adheres to the capital-adequacy guidelines for banks issued by the Basel Committee on Banking Supervision, under the auspices of the Bank for International Settlements. In South Africa, the requirement to maintain capital equal to the full ratio of 10% of risk-weighted assets became effective in October 2001.

Many demands are now being made on South African banking institutions to extend their activities in order to accommodate the banking needs of the underprivileged and to provide more funds for housing, export financing, agriculture and small business development.

## Insurance and unit trust companies

In 2000, the total assets of short-term insurers amounted to R48 billion (excluding the Road Accident Fund).

In essence, long-term insurance consists of life, assistance (which includes industrial and funeral), sinking fund, health and disability insurance. Long-term insurance and pension and provident funds are concerned with maximising investment results, and life insurance is dominant. Total assets of long-term insurers were R707 billion in 2000.

In 1998, legislation allowed for the demutualisation of mutual societies into public companies. The two largest mutual insurance companies are Sanlam and Old Mutual. Sanlam demutualised in October 1998, and was listed as a public company on the then Johannesburg Stock Exchange (JSE) in November 1998. Old Mutual demutualised in June 1999 and was listed on the JSE and London Stock Exchange in July 1999.

New Policyholder Protection Rules came into force in 1998. The rules ensure that there is proper disclosure of the financial implications, risks and obligations when undertaking insurance contracts. Full details of commissions and charges are now compulsory.

At the end of 2001, the unit trust industry had net assets valued at R168 billion (excluding intra-industry holdings of assets). Competing with the life insurance

sector, the industry invests in equities, including property units.

## Primary capital market

In 2001/02, a reduced demand for offshore borrowing resulted in a decline in the supply of new public-sector debt securities in the domestic primary bond market. Net redemption of fixed interest securities by public-sector borrowers amounted to R10,2 billion in 2001/02 compared to net issues of R2,5 billion in 2000/01.

The public sector's reduced demand for loanable funds was partly offset by growth in private-sector funding in the primary corporate bond market. In April 2002, the outstanding nominal value of private-sector loan stock stood at R24,5 billion, more than double the value two years previously.

The Government raised R12,4 billion through foreign-currency denominated bonds issued internationally in 2001/02, up from R2 billion in 2000/01. Government opened and completed its offshore borrowing programme for 2002/03 in April 2002, when an amount of R10,7 billion was raised through the issuance of a 10-year global dollar bond.

## Secondary capital market

Bond yields declined steadily since the emerging market crisis in 1998. The general decline in bond yields was supported by, among other things, an improvement in inflation expectations, an easier monetary policy stance and a shrinking supply of government securities. The monthly average yield on long-term government bonds declined by 261 basis points from December 2000 to November 2001 when it reached its lowest level since August 1980.

In December 2001, the general downward movement in bond yields was arrested when inflation expectations changed drastically following the steep depreciation of the exchange rate of the Rand and the monthly average bond yield increased to 12,6% in March 2002 – its highest level since January 2001. The mood in the market, however, has turned more positive with the Rand's steady appreciation against the Dollar and other currencies in late 2002 and early 2003.

Trading activity on the Bond Exchange of South Africa rose by 18% from R10,5 trillion in 2000 to R12,4 trillion in 2001. In December 2001, the nominal value of bonds in issue amounted to R444 billion with a market capitalisation of R471 billion.

## Money markets

South Africa has an advanced money market with a fairly large number of financial institutions participating.

Instruments traded range from traditional ones, such as negotiable certificates of deposit and Treasury bills, to those that only recently became popular, such as forward rate agreements.

Banks are generally kept short of liquidity, ensuring that they have to borrow some funds from the Reserve Bank, which makes the Bank's accommodation rate more effective in influencing money-market interest rates in general.

Banks are accommodated by the Reserve Bank through weekly repurchase transactions. To manage their liquidity needs efficiently, banks are also allowed recourse to their cash-reserve balances. Using so-called contra-accounts, they may on a daily basis borrow against their cash reserve deposits or hold additional cash reserves, as long as the average level of cash reserves during the one-month maintenance period equals or exceeds the minimum cash reserve requirement of 2,5% of their liabilities.

Money-market conditions were relatively stable during the first eight months of 2001 but tightened considerably in subsequent months. The average daily liquidity requirement of the private banks varied between R8,7 billion and R9,8 billion in the months from January to August but increased sharply, reaching R12 billion in December, and R11,3 billion in February 2002.

## The JSE Securities Exchange

The JSE is the largest securities exchange in Africa, with a market capitalisation several times that of all the other African markets combined.

The Exchange completed a major strategic review in March 2000, which identified 31 significant strategic projects to be completed in order to position itself as a world-class regional exchange and as southern Africa's gateway to the world's financial markets. This process, referred to as Gateway 2002, is well under way and is responsible for the many significant changes at the JSE.

On 1 December 2000, a Board of Directors representative of a broad industry interest base was established and a CEO appointed. The Board replaced the old committee structure and the CEO took the place of the executive president.

Portions of the JSE reserves and the accumulated surplus as at 30 November 2000 were capitalised in the form of JSE rights, thus forming a permanent capital base. The JSE is in the process of evaluating the merits of demutualisation and listing.

On 6 August 2001, the JSE acquired the business and assets of the South African Futures Exchange (SAFEX). SAFEX is now incorporated into the JSE as two new divisions – the Financial Derivatives Division, which covers the equity and interest rate futures and options markets, and the Agricultural Products Division, which covers commodities futures and options on maize, sunflowers, soya beans and wheat.

The JSE has led the process of harmonising the listing requirements of the members of the SADC Committee of Stock Exchanges (COSSE). COSSE envisages an integrated real-time national network of securities markets in the region by 2006. The JSE has offered its trading platform to these members, and the Namibia Stock Exchange has been trading on the JSE's trading platform for the past four years.

In 2001, the JSE entered into an alliance with the London Stock Exchange (LSE). As one of the pillars of the alliance, the LSE provides the JSE with core technology, the trading and information dissemination systems.

In addition to the provision of core technology, the alliance allows for reciprocal data distribution, access to the LSE's most liquid stocks on the JSE system, an easier dual listing process for 270 South African companies (without the JSE losing the benefits of their trading volumes), and the possibility of remote membership.

The JSE is keenly focused on product development and innovative ways of meeting the market's needs. The Exchange is particularly focused on products which broaden the investor base and bring greater liquidity and depth to the market. In this regard, the JSE issued and listed the first Exchange Traded Fund (ETF) in South Africa, becoming only the sixth exchange in the world to do so. With the Initial Public Offering (IPO), a total of R2,6 billion was raised, making it the largest IPO to date in South Africa.

The ETF, named SATRIX 40, enables an investor to buy a single JSE-listed security, giving investors the same return as buying shares directly in each company in the JSE's ALSI 40 Index.