Interplay between industrial policy, firm strategy and market power: metals industries in South Africa

3rd ACER week
Dar es Salaam

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Deindustrialisation in South Africa
- share of manufacturing in the economy
<table>
<thead>
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<tbody>
<tr>
<td>Manufacturing</td>
<td>6.4%</td>
<td>1.2%</td>
</tr>
<tr>
<td>Basic iron and steel</td>
<td>9.7%</td>
<td>2.0%</td>
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<tr>
<td>Basic non-ferrous metals</td>
<td>7.3%</td>
<td>0.1%</td>
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<tr>
<td>Metal products</td>
<td>2.7%</td>
<td>1.5%</td>
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<tr>
<td>Machinery and equipment</td>
<td>3.8%</td>
<td>2.7%</td>
</tr>
</tbody>
</table>
Employment

Basic iron and steel
Basic non-ferrous metals
Metal products excluding machinery
Machinery and equipment
Revealed comparative advantage relative net exports: \((X-M)/(X+M)\)
Basic iron & steel

• Apartheid legacy and its implications:
  • Highly concentrated and state-supported upstream production (capital-intensive)
  • Weak support for downstream
• Liberalisation, post-apartheid
• Critical review of four main areas of engagement:
  • Privatisation and government support
  • Restructuring of Iscor and bringing in MNC owner
  • Addressing market power and anti-competitive conduct
  • Minerals and energy policy as impacts on steel
Government’s role

• Substantial past support for upstream steel industry:
  • Internationally competitive with large net exports, historically very low production costs (iron ore, energy)
  • BUT: benefits not flowing to downstream industry
• Privatisation at end of 1980s

Liberalisation and restructuring

• Bringing in Mittal as MNC steel co – to upgrade techno capabilities (Business Assistance Agreement)
  • Information advantages on the side of the firm evident in returns to multinational (BAA, price for Saldanha Steel)
• Market power → local prices on flat steel approx. 60% higher than export prices
• Moral suasion and ‘developmental steel pricing’
Competition law?
• Law adopted in line with international ‘best practice’, and independent institutions
• Extensive attention on the steel sector
• Steel excessive pricing case: import parity pricing
• Legal treatment of historic state support and special costs advantages? ‘objective’ notional long-run competitive equilibrium ignored historical legacy
• Cartels and other restrictive arrangements

Minerals endowment?
• Cheap iron ore, coal not reflected in local steel price
  • Mining licences provide for non-discrimination against local buyers, including of products derived from minerals
• MPRDA: empowered owners allied to major mining companies
• Intense contestation over rents available from access to rights
Operating Cost – HRC

HRC operating cost US$/t FOB – Q1/04

Source: Metal Bulletin Research
Foundry industry and scrap metal

- Scrap metal main input for foundries → competitiveness of cast components
- Many countries intervene to ensure scrap supply to local industries
- Now evident has been:
  - Local cartel of sellers
  - Local cartel of main buyers (primary steel)
- Implication?
  - Other buyers than primary steel, without bargaining power, getting exploited
- Other possible policies: Export tax
Some conclusions?

• Failure of policy regime to achieve goals
• Failure to effectively engage with power of businesses
• Competition policy?
  • assessment set in narrow legal terrain, ‘technical’ assessment
• Industrial policy?
  • ‘in the small’, not changing firms’ incentives and conduct
  • favouring large firms in actions, incentives; but by-pass any conditions
• Both could be stronger and used as complementary tools
  • Tests for excessive pricing? Competition law as part of wider regulatory regime
  • Stronger industrial policy levers used
• Little effective support for more labour-intensive, downstream industries - more dispersed and with less lobbying power
Effective industrial policy levers?

Upstream discipline and support?
- Competition
- Energy
- Mining inputs
- Procurement
- Trade policy
- Development finance

But all in different departments and institutions!

- Need effective discipline/regulation and/or competition between regional producers
Effective industrial policy levers for downstream industry?

- Finance & support presupposes competitive foundations
- Development finance, technology, procurement
- Potential exists, and substantial trade deficit
- Clusters: bringing together training, finance, infrastructure, testing and R&D facilities
- Regional industrial policy required
  - Cross-country building of capabilities
  - Regional integration and trade driven by industrial policy
  - More effective competition at regional level
Metal products exports, by market

- Metal Product Exports Rest of Africa (18.6)
- Metal Exports Rest of the World (7.3)