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Geekonomics

Frank Flatters and Matthew Stern

THE future of the on-again, off-again, on-again aluminium smelter in the Eastern Cape hangs in the balance following the announcement that US giant Alcoa has made a hostile bid for its Canadian rival Alcan. This when our officials were close to convincing Alcan to go ahead with the project, which was first mooted by the French firm Pechiney before it was taken over by Alcan.

Why are we so concerned about a French, then Canadian, now-maybe-American aluminium plant? Because without it the government’s flagship industrial development zone (IDZ) at Coega looks decidedly empty.

The Coega project consists of two components — a deep-water port on the Coega River and an adjacent 12000ha industrial development zone (IDZ). It is the country’s largest infrastructure project since 1994, with an estimated cost so far of about R8bn — R3,1bn for the new port, R2bn for the IDZ and R2,1bn by Eskom to upgrade power supply. All funding has come from the government.

Coega claims it has secured 10 investment deals worth more than R21bn. We can find no complete listing of these projects on the Coega website or in their annual report, but through past press releases we have pieced together the following portfolio:

Two local companies plan to relocate existing facilities from elsewhere in the Eastern Cape to Coega. Dynamic Commodities, the only company to have begun operations in the IDZ, is an ice-cream manufacturer and exporter. We do not know the size of their investment. Cerebos, a local salt manufacturer, plans to follow suit at a cost of R85m. There will be some expansion to these facilities but this hardly counts as greenfield investment.

Five new investments are reportedly planned for this year. They include a R70m biomass fuel-pellets project, a R50m automotive component operation, a pilot project farming giant shrimps for export, a R50m concrete products operation, and a logistics facility. As far as we can establish, none has actually taken place.

By far the biggest investment announced to date is a R1,1bn chlorine manufacturing facility, to be commissioned in 2009. The same company “plans” to invest a further R5,7bn in a desalination plant, presumably on the back of a cosy off-take arrangement with the local government. There is also talk of a R1,1bn stainless-steel mill.

The history of (non) investment at Coega also includes some that have come and gone with no investment at all, such as a Belgian textile mill that, despite great media fanfare and substantial sweeteners from government, never pitched up. How many of these other projects will suffer the same fate?

At best, the nine “secured” investments amount to R3bn, less than the total amount of physical and electrical infrastructure sunk into the project. So the “success” of Coega remains contingent on a single, extremely elusive and very costly aluminium smelter.

It is for this reason that the government has thrown all that it can — and far more than it should — to secure this anchor investment. The trade and industry department dug loopholes in the criteria of its own investment incentives to ensure that the smelter qualified for maximum tax benefits. A highly subsidised electricity pricing dispensation has been offered to the project, which will require as much electricity as a city, at a cost that has not been made public. Finally, Alcan will provide only 25 % to 40% of total equity, with the government (through Coega and the IDC) and other local investors expected to provide the bulk of the funds.

How much larger than this will be Alcan’s revenue share as a result of deals for management, technology licensing and other fees? What guarantee is there that Alcan will not take its cheap electricity allotment and sell it back to electricity-starved South Africans at exorbitant commercial prices while it delays (or never starts) construction of its smelter? Sounds fanciful, but this is what Alcan is reported to have done to its own people in the Canadian province of British Columbia.

In any event, Alcan looks likely to be swallowed by Alcoa and this will further delay decisions on this project. With very generous incentives already on offer, who knows what more Alcoa will be able to swindle out of government to make this investment happen.

Coega’s initial goal was to encourage private development of a resource-, energy- and capital-intensive mineral processing facility. While this might not have contributed much to employment or general industrial development, the cost to the government would have been small. The decision to develop the zone at public expense, and with the addition of very generous income-tax and other incentives, changed the balance, and raises serious questions about the country’s industrial development priorities.

Is the R8bn that has been invested so far the most effective use of government resources to promote more labour-intensive growth? Even treating these as sunk costs, what is the justification for pouring more of SA’s scarce energy resources, at heavily subsidised prices, into an investment with little other purpose than to save face for those responsible for Coega?

ll Matthew Stern and Frank Flatters are from Development Network Africa, a private economic and development consulting firm (geeks@dnafrica.com).