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RE: IMPACT OF THE RECENT AND CURRENT INDUSTRIAL ACTION ON THE KZN ECONOMY

The current wave of industrial action started about 14 days ago. The industrial action is currently in its third week with some progress in terms of a possible agreement. It is estimated at this stage that the industrial action will last between 20 to 25 days in total. It is also estimated that about 40 000 employees of Transnet will have participated in some form or way in the industrial action. Transnet has approximately 50 000 employees in total.

The industrial action has mainly focused on port and railway operations. It is stated by the unions that the aim of the industrial action has been to bring port and rail operations to a halt or seriously disrupt these operations. It is doubtful that the industrial action has actually achieved this since port and railway operations have not stopped completely. However, the industrial action has without a doubt seriously diminished port and railway operations throughout the country.

Johan Botha, an economist at Johannesburg-based Standard Bank Group Ltd recently stated that South Africa's economy may lose "billions of rand" if a strike that has shut ports and rail lines and slashed exports of metals, wine and fruit to Europe and Asia, isn't resolved soon. Economist Mike Schussler said: "The Transnet strike probably cost the economy R300 million to R500 million a day. We do not have exact figures, but that is what we think the impact is." Various other economists have predicted that South Africa could

lose as much as R15 billion because of the strike and, couple this with the estimated R30 million's worth of damages caused by strikers, and it's quite clear that the cost of a strike is incredibly pricey.

What is fact is that the current wave of industrial action had an impact on the KZN economy and that the impact is of a negative nature. What is also fact is that the impact is not just on the present but also on the future. We therefore need to look at both the actual output of the economy and the potential¹ output of the economy. For example, the loss of production because of the strike decreases the actual GDP of the province, whilst the loss of investment into the province because of the strike decreases the potential GDP of the province.

Unfortunately the size of the impact on both the actual GDP and potential GDP of the province of KZN is very difficult to determine or quantify. It is not an exercise that can be done in a week or a months' time. It takes massive amounts of time, energy and data to determine the impact of a once-off event on actual and potential GDP and especially if the unit of analysis is a provincial or regional economy.

Port and railway infrastructure and services are very significant from an economic point of view. Such infrastructure and services facilitate the movement of goods and services and labour, i.e., it allows trade to occur. It would be very difficult for trade, both from a domestic and international point of view, to occur without port and railway infrastructure and services. Port and railway infrastructure and services are thus a significant economic enabler.

¹ The highest level of real gross domestic product that could persist for a substantial period without raising the rate of inflation.

From a theoretical point of view there are a number of benefits the citizens and firms of a country or region may enjoy as a result of being able to trade freely with the citizens and firms of another country or region.

- The benefits of specialisation (economies of scale)
- The benefits of competition (economies of efficiency)
- The benefit of choice (consumer surplus)

The point of trade is to delink domestic or region production and consumption and to increase the potential output of the relevant economy.

From a theoretical point of view trade allows domestic or local production not to be limited by domestic or local consumption and thus the rate of economic growth of a country or region doesn't have to be limited by the growth of domestic or local consumption expenditure. Production of goods and services in KZN is not limited by the consumption of goods and services in KZN because of trade. Production or output can therefore be much more than what would be otherwise possible. If trade is to be limited or stopped for whatever reason then the production of goods and services will have to decrease. Production will have to decrease because of the limited domestic or local demand for such products and services. Cuts in production suggest an increase in the number of people unemployed and the closure of businesses.

It is thus possible to put the following theoretical argument forward;

1. Decrease in port and railway infrastructure and services
2. Decrease in trade
3. Decrease in production
4. Increase in unemployment
5. Increase in business closures

The above argument seems to be based on sound economic principles and fundamentals. However, in practical terms it is very difficult to quantify the

argument. There are uncertainties about the size and lag times of the linkages for example. The above argument also only focuses on the present not incorporating the future, i.e., the argument only focuses on actual GDP and not potential GDP.

The transport, storage and communication sector in KZN is a significant sector in that it contributes about 13.60 per cent to the total provincial GDP and the sectors contribution increased by almost 3 per cent since 1996. The total value added in the transport, storage and communication sector in KZN during 2009 was about R35.3bn. The transport, storage and communication sector is the 4th largest sector in the province in terms of its value added. The transport, storage and communication sector employs at present about 154 000 employees; down from a peak of 184 000 employees during the 1st quarter of 2009. The transport, storage and communication sector contributes about 6.74 per cent to the total number of people employed in the province. The KZN transport, storage and communication sector is also the 2nd largest transport, storage and communication sector in SA contributing about 21.67 per cent towards the national transport, storage and communication sector value added (Stats SA and own calculations).

The provincial transport, storage and communication sector is thus a very significant sector. It's difficult to disagree with the argument that the province has an absolute and competitive advantage in the transport, storage and communication sector.

The transport, storage and communication sector is directly impacted by the current wave of industrial action. However, and more significantly, the industrial action is not limited to the transport, storage and communication sector. Other sectors are indirectly impacted. A significant indirect sector is the manufacturing sector because of the significant link between port and railway operations and industrial output.

The manufacturing sector in KZN is a significant sector in that it contributes about 21.66 per cent to the total provincial GDP and the sectors contribution

decreased by almost 3.66 per cent since 1996. The total value added in the manufacturing sector in KZN during 2009 was about R56.2bn. The manufacturing sector is the largest sector in the province in terms of its value added. The manufacturing sector employs at present approximately 407 000 employees; down from a peak of 441 000 during the 1st quarter of 2008. The manufacturing sector contributes about 16.83 per cent to the total number of people employed in the province. The KZN manufacturing sector is also the 3rd largest manufacturing sector in SA, contributing about 21.59 per cent towards the national manufacturing sector value added. It is also fair to say that the province has a competitive advantage in manufacturing (Stats SA and own calculations).

The industrial action thus directly and indirectly impacts on two of the three largest sectors in the provincial economy. It thus cannot fail to have a significant impact on the KZN economy.

Operations at the two harbours (Durban and Richards Bay) have been severely affected. Examples include the following:

- A “build up” of vessels
- Decrease in handling containers
- On-loading of, for example, citrus fruit and wine has stopped completely
- Off-loading of soccer world cup related imports only

The above have the following direct consequences:

- Products ready for exporting must be stored. Non-delivery leading to contracts being terminated. Increased costs of storage. Loss of revenue implications for cash-flow.
- Products needed in the production process not available and thus production “stops”, for example the motor industry
- Transporting of goods has “stopped”. Transport companies incurring significant costs because of the delays and loosing

revenue because of lack of business. Severe cash flow implications.

The above focuses on actual GDP. Potential GDP is also negatively affected, for example:

- Loss of domestic business confidence
- Loss of international confidence in SA
- Loss of competitiveness in the domestic economy
- Increase in country risk

The long-term consequences of the above include the following:

- Loss of domestic and international investment in SA
- Loss of business with SA, i.e., cancellation or non-renewing of contracts, etc
- Increase in cost of borrowing money from international institutions

A quick survey via the different Chambers of Business in the province yielded the following comments:

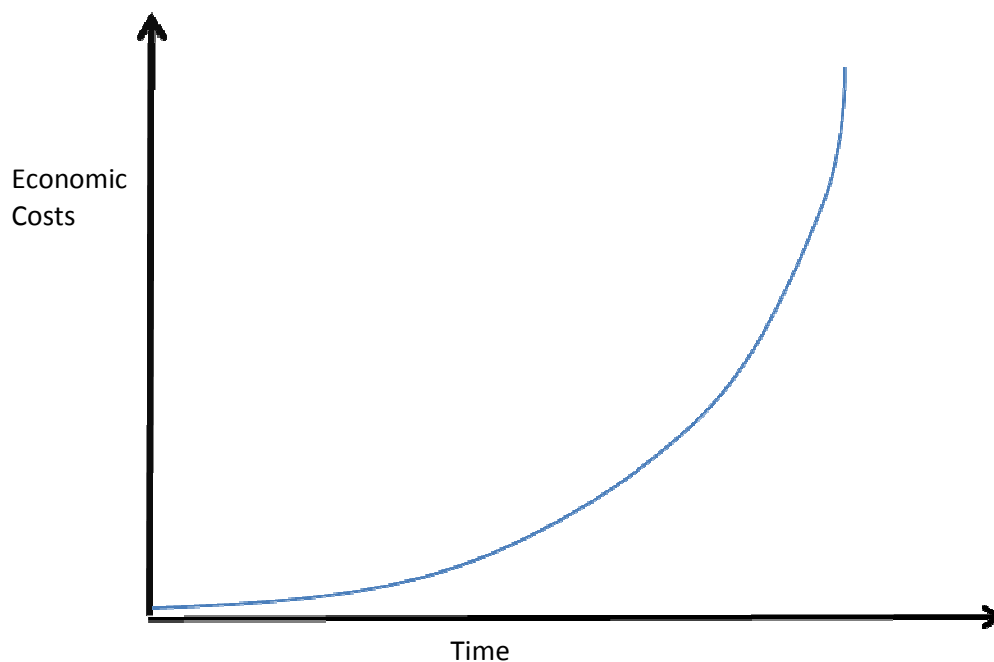
<p>GEI Shipping & Trading cc</p>	<p>The Transnet Strike has a definite negative impact in the economy of our country. Vessels not being able to berth, & in most instances the vessels by-pass the port & discharge cargo in another country.</p> <p>Shippers / Exporters that have confirmed orders are not able to ship their cargo. They are losing a lot of money because importers in other countries, due to the urgency, are importing these products from elsewhere & as a result we also lose money.</p> <p>In the economy we are in at the moment where companies are closing down, thousands of people are losing jobs I strongly feel SATWU & its members are making ridiculous requests. Transnet should give them an ultimatum. If they don't report for work on a given day, they will be dismissed. Then you will see how quick they will end the strike & get back to work.</p>
<p>Clifford Welding</p>	<p>We currently have about 14 x 40ft containers that need to be packed, sales value about R25M.</p>

Systems	<p>Delayed shipment causing delayed receipts is obviously a cash flow and cost of funds issue, but the biggest issue is that it is hampering our production as we cannot commence assembly of our next machines until we can pack and clear these machines from our floor.</p>
Anchor Chemicals	<p>We are awaiting delivery of a container to the value of R866, 556, which was due to dock on 7th May. Material has as yet not been received.</p> <p>We estimate loss of sales this month of R450, 000 due to this material not being available when planned, but this should be recovered in the next month.</p> <p>We cannot estimate or quantify loss of production or re-planning at our customer's end due to the material not being available.</p>
Transnet	<p>Transnet has not been keeping track of the impact of the strike on our business as it is difficult to do. We will only be in a position to understand the impact once the strike is over and we have cleared all the backlogs that have built up. Invariably, all the cargo destined for SA and exports out of the country will still take place.</p>
Britec Laboratories	<p>My business is in Umbogintwini and requires imported products.</p> <p>We have lost sales totalling R100 000 (4%) in the last 2 weeks because of the lack of raw materials</p> <p>Within the park there are a number of logistics companies which have incurred significant losses</p> <p>E.g SATI container yard has lost R2.4 million in turnover.</p>
Independent Economist	<p>It will be difficult to quantify.</p> <p>I visited UEC, the factory producing decoders in Umhlanga, on Tuesday. Their production was close to stopping due to the strike. The same to Toyota in Durban.</p> <p>If you include the impact on the whole manufacturing sector in KZN it will be billions of production lost.</p>
Terry Hudson – www.ports.co.za	<p>While it is difficult to estimate exactly just how much the action is costing the city, several companies reported losing "hundreds of thousands, and possibly millions" a day. The Mediterranean Shipping Company (MSC) alone reported losing between US\$2m and US\$3m a day as its ships remain anchored outside the port.</p>
Dr M Sutcliffe	<p>"There are thousands of businesses in the city that are directly or indirectly linked to the port operation. I would say that about</p>

	30-40 percent of the local economy is based on the port. Because of the sheer size of the port, the largest in Sub-Saharan Africa, Durban has been affected more than any other city,"
Freight 24	<p>We have lost almost a month's turnover which is equivalent to R2,000,000-00.</p> <p>We placed all staff on short-time for the duration of the strike as our business is directly related to the port operation (transport of containerised cargo and warehousing).</p> <p>Our service providers whom we engage lost R1,400,000-00 for the month.</p>

The results suggest fairly significant impacts.

It must also be stated that the longer the industrial action continues the more significant the impact. What is interesting is that the impacts and consequences of such an event seem to follow an exponential function. The impact and consequences in the beginning are not very significant, but as time progresses the impact and consequences increase at an accelerating pace. This is obviously a very dangerous situation because the social and economic loss increases exponentially. The graph below illustrates this phenomenon.



What follows is a very simple and preliminary attempt to quantify the impact of the industrial action. As stated by many economists and commentators it's very difficult to accurately and reliably quantify such economic impacts. Therefore very few actually attempt to do such calculations. Nonetheless, I will attempt to quantify the impact of the industrial action on the provincial economy based on a number of assumptions. The assumptions are however not based on any specific evidence or analysis, but on my perceptions and understanding solely.

The first port of call is to quantify the direct impact, i.e., the loss of production in the transport sector. Transport output is included in the total transport, storage and communication output in the national accounts. My first assumption is that transport accounts for 60 per cent of the total sector output. My second assumption is that output per day is constant. The calculations are indicated in the table below.

2009 Values	Direct Impact
	KZN GDP (Constant 2005 prices)
Transport, storage and communication sector	35,430,031,879
Transport industry (60% of sector output)	21,258,019,127
Transport GDP per day (365 days pa)	58,241,148
Loss due to strike (20 days)	1,164,822,966
Loss as a % of Total Sector Output	3.29%
Sector Contribution to KZN GDP	13.60%
<u>Direct Decrease in Provincial GDP</u>	<u>0.45%</u>

The calculations suggest that the direct loss to the provincial economy is estimated to be about 0.45 per cent of GDP.

The loss of output in the transport industry also has indirect impacts, most significantly in the manufacturing sector. Manufactured products for exports cannot be exported and imported inputs needed cannot be delivered. In both instances manufacturing output either decreases or completely stops. There are however some manufacturing establishments that are not affected by the industrial action because they are not export or import orientated. Thus we only require the GDP of trade manufacturing, i.e., manufacturing establishments that export or import or both. My third assumption is that trade manufacturing accounts for 30 per cent of total manufacturing output. The calculations are indicated in the table below.

2009 Values	Manufacturing Impact
	KZN GDP (Constant 2005 prices)
Manufacturing sector	56,184,135,257
Trade manufacturing industry (30% of sector output)	16,855,240,577
Manufacturing GDP per day (365 days pa)	46,178,741
Loss due to strike (20 days)	923,574,826
Loss as a % of Total Sector	1.64%
Sector Contribution to KZN GDP	21.66%
<u>Indirect Decrease in Provincial GDP</u>	<u>0.36%</u>

The calculations suggest that the indirect loss to the provincial economy is estimated to be about 0.36 per cent of GDP.

The estimated direct and indirect loss to the provincial economy is estimated to be **0.80** per cent of GDP.

It is however very important to note that:

- The calculations are based on certain assumptions

- Some of the losses as calculated can be recovered
- Some of the losses can be either permanent or temporary
- The other sectors of the economy are excluded
- Some of these other sectors can also be affected

The point of the above is to make it very clear that the loss of 0.80 per cent will not be the actual loss. The actual loss could be more or less depending on the ability to recover the temporary loss of production on the one hand and the size of the impact on the other sectors of the provincial economy on the other hand.

It is also important that the current wave of industrial action be seen in light of a fragile economic recovery phase. The prospects for the provincial economy are reasonably sound but based on the assumption that the “good news” will be much greater than the “bad news”. The national or provincial economy simply doesn't need such events at this point in time.

It is also very important to note that the impact on potential GDP is not quantified at all simply because of the difficulties associated.

Your comments and/or suggestions are most welcome.

Yours truly

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