Incentives for the manufacturing sector: what South Africa can learn from Malaysia and Singapore

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Abstract

The expansion of the manufacturing sector is one of the South African government's focus areas for economic growth and employment creation. The research on which this article is based identified additional incentives, applicable to the manufacturing sector, which the South African government could introduce to encourage investors to choose the South African manufacturing sector as a desired investment destination. The incentives provided to manufacturing companies by the governments of Malaysia and Singapore and those provided by the South African government are compared in order to examine the similarities and differences between these incentives. In the light of these findings, recommendations are made for additional incentives in South Africa to promote investment in South African manufacturing companies and reduce some of the barriers that prevent local and foreign investment in the country.

Keywords

Investment incentives, incentives, investment, promote investment, economic growth, manufacturing sector

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1. INTRODUCTION

South Africa has an unemployment rate of 33.4%, according to the broad definition of unemployment, which includes the number of people who are available for work but not looking for work (Statistics South Africa 2012a:v). It is a primary policy objective of government to reduce this rate significantly and to create five million jobs in the next ten years (Government Communication and Information System (GCIS) 2010:8). In order to achieve this objective, economic growth needs to take place. During 2011 the South African government identified six sectors which it believes would assist extensively in the provision of this much-needed growth and employment creation. The manufacturing sector is one of these sectors (GCIS 2010:10). In support of the government's targeting of the manufacturing sector as a source of growth and employment, the Minister of Finance also announced in his 2011 budget speech that the government is focused on increasing labour-intensive activities in the manufacturing sector (South African Revenue Service 2011a:8).

The manufacturing sector is already playing a vital role in the South African economy. This sector contributed 15% to GDP in 2010, which made it the second-largest contributing sector in the South African economy. The finance, real estate and business services sector is the only sector that is contributing more to GDP than the manufacturing sector (Statistics South Africa 2012b:6). The manufacturing sector also contributed 22.2% of the total tax assessed by the South African Revenue Service for companies reporting positive taxable income in 2009 (most recent information available at the time the research was done). The financial intermediation, insurance, real estate and business services sector was the only one with assessed taxes that were greater than those of the manufacturing sector (South African Revenue Service 2011b:110). The manufacturing sector is the fourth-largest employer and absorbed about 14% of the total employed population in 2011 (Statistics South Africa 2012c:27). It is clear that the manufacturing sector is contributing extensively to the South African economy.

Throughout history, the manufacturing sector has been considered as being at the forefront of an economy that is advancing to higher levels of innovation and efficiency. Manufactured products can be traded easily and profits from the manufacturing sector have an influence on other sectors, resulting in the balanced development of the economy as a whole (Department of Science and Technology 2004:6). The expansion of manufacturing in South Africa will promote economic growth and employment, which will ultimately lead to an economically stronger nation (Rodrik 2006:22). This growth could be achieved by increased investment in the manufacturing sector, by both local and foreign investors (Schneider 2000:413), provided that investors are not discouraged by political volatility. Increased investment in the manufacturing sector is thus required to facilitate increased production capacity, which will contribute to the growth of the manufacturing sector (Department of Communications 2009:12-13). This increase in manufacturing capacity is dependent upon, among other things, government's ability to encourage increased investment (Woolfrey 2010). The government is well aware of the need to improve capital investment in the South African manufacturing sector. According to the Minister of Trade and Industry, investment and training are vital in upgrading the manufacturing sector (SAinfo 2010). President Zuma also announced in 2011 that R20-billion would be set aside in the form of tax-break incentives for the manufacturing sector with the intention of promoting investments, expansions and upgrades (Nkosi 2011).

The South African government has introduced various investment incentives in the form of tax and financial incentives to facilitate the growth of certain industries and to promote local and

foreign investment in South Africa (Department of Trade and Industry (DTI) 2011d). Recently, much attention has specifically been focused on new incentives for the manufacturing sector (such as the Industrial Policy Projects (South Africa 1962, sec. 12I), the Automotive Production and Development Programme (GCIS 2008) and the Enterprise Investment Programme (DTI 2012b). This leads to the question of whether there are more incentives that could be initiated to facilitate increased investment in the manufacturing sector. The purpose of the research reported in this article was to compare the incentives available to the manufacturing sector in South Africa with those available in Malaysia and Singapore. The criteria for selecting these countries are discussed in a separate section below. Through this comparison, incentives applicable to the manufacturing sector, which could be considered for introduction in South Africa, were identified. These incentives could play a vital role in attracting more investment in the manufacturing sector, thus promoting growth in the South African economy.

2. LITERATURE REVIEW

Investment is influenced by several factors. According to Tuomi (2009:117), these factors can be classified into three categories, namely country endowments (the beneficial attributes and elements of a country, such as a large population, geographical location or natural resources), the investment climate of the country (its political and economic stability, availability of infrastructure and quality of labour) and incentive schemes (such as tax exemption and cash grants).

Considering these factors in the South African context, the country appears to be an attractive investment location. Its well-situated geographical location and six deep-sea harbours make the country ideal for international export. South Africa is one of the world's largest producers of gold and platinum and has several natural resources, such as minerals and ores, timber and agricultural products (Maxwell 2007:1-2; Industrial Development Corporation 1997:8; South Africa Web 2012; DTI 2012c:1). South Africa also has an internationally oriented economy. Companies can make use of a large financial support structure, which includes a network of merchant banks and financial service specialists. The cost of doing business in South Africa is similar to that of other emerging countries (Asafo-Adjei 2007:92-94; DTI 2012c:1; Maxwell 2007:1).

However, South Africa faces some obstacles to attracting investment, such as a lack of skilled workers, corruption and a high prevalence of crime. Other negative factors that may influence companies against choosing to invest in South Africa could include inefficient government bureaucracy, extensive labour legislation and inadequate supply of infrastructure (World Economic Forum 2010:302).

Incentives are usually among the relatively few measures that can be introduced to minimise the effects of these investment obstacles and to improve the attractiveness of a country as an investment location. Incentives are also one of the few identifiable signs of a country's change in attitude towards foreign and local investment (Organisation for Economic Cooperation and Development 2001:10). Although research regarding the use of incentives to encourage investment is inconclusive, various incentives have been found to influence investment decisions, and incentives are frequently used by both developed and developing economies (Barbour 2005:8). It is recognised that incentives are not the determining factor for investment decisions and that other negative features of the country may not be overcome by the existence of incentives. The scope of this research was not to determine the effectiveness of incentives,

but to investigate whether this investment promotion tool could be utilised even further. Incentives remain one of the main factors that influence the investment decision (Tuomi 2009:117) and the South African government is indeed actively using incentives to promote the country as a preferred investment destination in its efforts to attract investment to the country (Department of National Treasury 2008b:23)

Incentives can either encourage investment generally or attract investment in selected sectors or geographical areas (Organisation for Economic Cooperation and Development 2001:10). They can also play a legitimate role in encouraging specific types of investments that generate particular benefits for the economy, for instance projects that utilise advanced technologies to improve the host country's technical knowledge, or projects located in less-developed regions of a country, which could help to uplift and expand those regions (Galenson 1984:2-3; Nathan-MSI Group 2004:3-1 to 3-2).

South Africa's incentive regime compares favourably with international best practice (Barbour 2005:vi). Fiscal incentives in the form of specific deductions and capital allowances are contained in the Income Tax Act (58 of 1962). These incentives effectively reduce the investor's tax liability, while the purpose of the financial incentives provided by the Department of Trade and Industry (a division of government) is to encourage direct investment. This is done by providing the investor with upfront funds to set up business activities or reimbursing the investor for expenses already incurred in respect of a new business enterprise (DTI 2012d).

There are numerous types of incentives, each with unique features. For comparison purposes, this study classifies incentives into three main categories, namely incentives that promote specific investment (as defined later on), incentives that encourage investment in capital assets and incentives that reduce the company's fiscal burden.

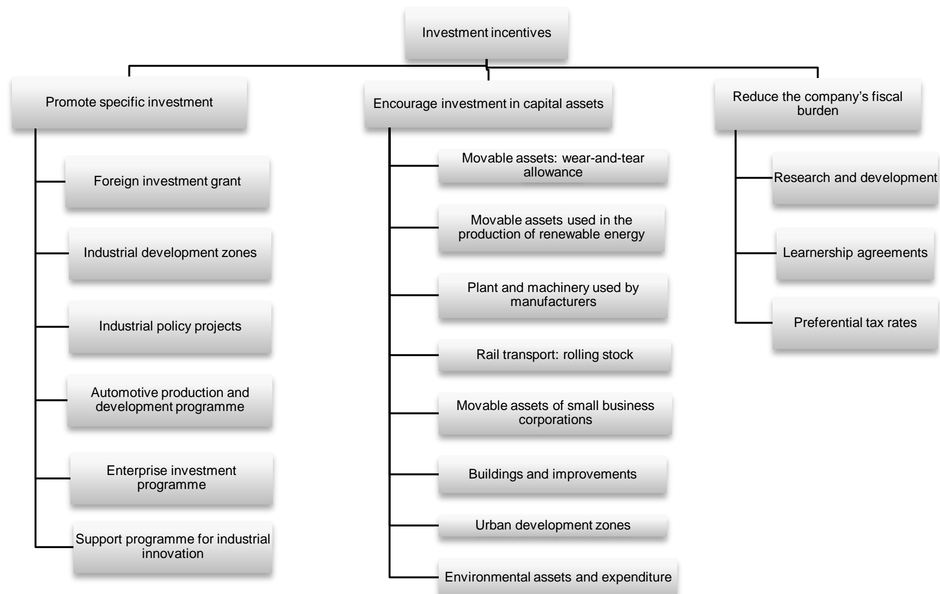

FIGURE 1: Incentives available to manufacturers in South Africa

Source: Wentzel (2010:95)

Incentives that are currently available to the manufacturing sector (either specifically or as part of incentives generally available to all industries) are summarised in FIGURE 1 under the three main categories of incentives as listed above.

It is evident from FIGURE 1 that many incentives are available to South African manufacturers. However, to attract increased investment to the South African manufacturing sector, additional incentives may have to be introduced. By studying investment incentive measures that are provided by other countries, recommendations can be made for the initiation of further incentives.

3. SELECTION OF COUNTRIES AND RESEARCH METHODOLOGY

A comparison was done between the incentives available in South Africa and those available in two foreign countries. Since this research focused specifically on incentives for manufacturing enterprises, the selection method used in determining the foreign countries made use of information that would ensure the comparability of the manufacturing sectors. For this reason, the selection of the two countries was based on three criteria, namely the performance of the manufacturing sector of each country with reference to manufacturing value added, the gross domestic product (GDP) per capita and the geographical location.

The 2011 World Development Indicators report (World Bank 2011:202) provides data on the amount of value added (in US dollars) by the manufacturing sector of most countries in 2009 (the most recent data available at the time the research was done). Manufacturing value added refers to "the sum of gross output less the value of intermediate inputs used in production" (World Bank 2011:205). According to this reports, the amount of manufacturing value added by South Africa during 2009 was the equivalent of $39 014 million. Since South Africa needs to increase its manufacturing activities and in order to learn from countries with higher manufacturing performances than its own, it was decided to identify countries with manufacturing value added values ranging from $6 million below to $12 million above South Africa's value added. Therefore the data range above South Africa's value is higher than the data range below South Africa's value. Seven countries, namely the Czech Republic, Denmark, Finland, Ireland, Malaysia, Saudi Arabia and Singapore, met these criteria.

Although these seven countries can be compared with South Africa because the manufacturing value added by each of these countries is similar to that of South Africa, they differ vastly in several other aspects, such as the level of economic development, which could distort the outcome of the comparison. For this reason the GDP per capita at nominal values of these countries was also taken into account for selection purposes. This indicator represents each country's economic output in relation to the size of its population and therefore reveals the comparability of the countries' economies (Kaul & Tomaselli-Moschovitis 2009; Pinstripe 2009).

The GDP per capita of countries in 2009 was obtained from the International Monetary Fund (2009). Of the seven countries mentioned earlier, only Malaysia's GDP per capita ($7 469) was similar to that of South Africa ($5 635). The other six countries' GDP per capita ranges between $14 871 and $55 942, as they have more advanced economies. It follows that South Africa can be compared to Malaysia, as both these countries have a similar level of economic development and manufacturing value added.

While it would be useful to compare the incentives offered by countries that are similar to South Africa in several respects, it would also be beneficial to compare the incentives offered by South

Africa to those offered by a government with a more advanced economy. This could assist in gaining an understanding of what South Africa's approach should be for future growth. Of the advanced economies among the seven countries listed above, Singapore was selected because of its proximity to Malaysia. No country in the same geographical area as South Africa was identified as being comparable in terms of the criteria used for selection. The fact that Malaysia and Singapore are situated in the same geographical region of Southeast Asia and that both of these countries' economies are primarily dependent on manufacturing (Encyclopedia of the Nations 2010; Department of Statistics Singapore 2012) was regarded as providing sufficient reason for comparing them to South Africa.

Malaysia and Singapore are both attractive investment destinations, as both countries' economies are open for international trade (International Export Support 2009; Monetary Authority of Singapore 2012). Malaysia is located in Southeast Asia and it has a population of over 28 million (World Bank 2012a). The manufacturing sector is a major source of the country's economy and at the end of January 2006 this sector contributed 31% of Malaysia's GDP (Associated Chambers of Commerce and Industry of India 2006). The country's focus on technological development is a huge advantage for manufacturers in Malaysia because it offers a cost-competitive location with modern-day technology for investors based in the country. Furthermore, due to Malaysia's easy global access via several air and shipping routes and its favourable business environment, the country is an attractive location for trade and investment and has become one of the world's most preferred destinations for investors wishing to set up offshore manufacturing operations. This is substantiated by the fact that more than 5 000 foreign companies from over 40 countries have established and expanded their businesses in Malaysia (Bernardi, Franschini & Shope 2006:218; Malaysian Industrial Development Authority (MIDA) 2012b).

Singapore is also situated in Southeast Asia and has a population of almost five million. It is a highly developed country for global trade and in 2012 it was ranked the world's easiest place to do business (World Bank 2012b), as well as the third preferred country for foreign trade and investment (Singapore Economic Development Board 2012). In view of its well-established infrastructure and sensible pro-business tax policy (Singapore Press Release 2012), Singapore is a highly desirable location for the establishment of new business. Consequently, over 7 000 multinational corporations have established their business operations in this country (Ministry of Manpower 2012; Monetary Authority of Singapore 2012).

While both Malaysia and Singapore are attractive destinations for investment in manufacturing, they have initiated different incentives to attract more investment in an attempt to encourage economic growth. Singapore was one of the first Southeast Asian countries to offer incentives in 1960 (Baumüller 2009:8-9) and in 2007 it was recognised as the country providing the most attractive incentives in the world (Singapore Economic Development Board 2007a). Malaysia also started to initiate generous incentives in the late 1960s and focused extensively on the relocation of manufacturing activities to Asia in the 1980s (Baumüller 2009:9). Baumüller's (2009:13) research into the impact of incentives in Southeast Asia revealed that incentives have been a major contributing factor in attracting foreign direct investment to Singapore and Malaysia, resulting in the stimulation of economic development and export growth.

The study made use of a literature review. This involved the collection, analysis and interpretation of relevant published information. The information was obtained from books, articles (both secondary sources) and legislation (primary source) (such as South Africa's Income Tax Act, Malaysia's Income Tax Act, Malaysia's Promotion of Investment Act, Singapore's

Income Tax Act and Singapore's Economic Expansion Incentives Act). Information was also obtained from electronic sources in accessing the official websites of government entities (such as the South African Department of Trade and Industry, the Inland Revenue Board of Malaysia, the Malaysian Industrial Development Authority and the Inland Revenue Authority of Singapore).

4. COMPARISON OF INCENTIVES THAT PROMOTE SPECIFIC INVESTMENTS

This section compares and highlights the similarities and differences between the incentives offered by South Africa and those offered by Malaysia and Singapore. This article focuses only on the first incentive category (as outlined in FIGURE 1), namely incentives that promote specific investments. These incentives encourage and facilitate the incorporation of new manufacturing companies and the expansion of existing ones in specific industries or geographical areas that will benefit the country's economy.

TABLE 1 lists the incentives offered by all three countries to promote specific investments in the manufacturing sector. This indicates similar incentives offered by more than one country, as well as unique incentives offered by only one country. The classification of the comparison indication disclosed in the last column of TABLE 1 (class) is explained as follows:

A = Incentives offered by South Africa, Malaysia and Singapore

B = Incentives offered by South Africa and Malaysia only

C = Incentives offered by one country only

D = Incentives offered by Malaysia and Singapore only

TABLE 1: Comparison of manufacturing incentives offered by South Africa, Malaysia and Singapore to promote specific investment

SOUTH AFRICA	*MALAYSIA*	*SINGAPORE*	*CLASS*
Industrial Development Zones	Industrial Development Zones	Industrial Development Zones	A
Support Programme for Industrial Innovation	Support Programme for Industrial Innovation	Support Programme for Industrial Innovation	A
Reinvestment and development incentive: (Enterprise investment program expand)	Reinvestment and development incentive	Reinvestment and development incentive	A
Strategic projects (Industrial policy projects)	Strategic projects	-	B
Relocation of manufacturing activities (Foreign investment grant)	Relocation of manufacturing activities	-	B
Automotive Production and Development	Automotive Production and Development	-	B

Small-scale companies' incentive	Small-scale companies' incentive	-	B
Enterprise Investment Programme (new)	-	-	C
-	Industrial linkage programme	-	C
-	Production of specialised machinery and equipment	-	C
-	Resource based industries' incentive	-	C
-	-	Start-up companies' incentive	C
-	Tax holiday – pioneer status	Tax holiday – pioneer status	D
-	Investment tax allowance	Investment tax allowance	D

Source: Authors' compilation

The comparison between the three countries revealed that, in terms of the objective, several incentives are similar. On closer scrutiny, however, it becomes clear that in most instances the deduction amount, allowance rate or other assistance offered by these three countries per incentive varies, which would have an impact on the benefit a manufacturing company would receive. The discussion of the results from the comparison between these incentives considers only the benefit offered to the manufacturer, and does not examine any other requirements that need to be met in order to make use of these incentives or limitations that apply.

4.1 Incentives offered by South Africa, Malaysia and Singapore (class A)

South Africa, Malaysia and Singapore have three incentives in common. The similarities and differences between the incentives offered by the three countries are discussed in detail below.

4.1.1 Industrial development zones

All three countries have similar industrial development zones, where manufacturers may import raw material, machinery and assets free of customs duty and there is no need for South Africa to enhance its incentive design (South African Revenue Service 2012); MIDA 2012c; Inland Revenue Authority of Singapore 2012a).

4.1.2 Support programme for industrial innovation

Incentives are provided to companies in South Africa, Malaysia and Singapore to encourage the use of new and emerging technologies to develop innovative and competitive products or processes (industrial innovation). In South Africa, a grant of 50% to 85% of the development costs incurred in such a project is offered to manufacturing companies (DTI 2012a). In Malaysia, a company involved in the production of promoted products with emerging technologies, such as computers, may enjoy a 100% income tax exemption for five years, if it has pioneer status (corporations that participate in a promoted activity or produce a promoted product).

Alternatively, such a company may claim an investment tax allowance of 60% on capital expenditure for five years (Malaysia 1986, sec. 1(c),s2(c)). In Singapore, innovation is encouraged by means of a grant in the form of co-funding of capital expenditure incurred by the manufacturing company, based on the level of support needed (Nanyang Technological University 2012:[1]).

South Africa and Singapore are similar in that they provide the same type of incentive, namely a cash grant, to increase any manufacturing sector's innovation capacity. Malaysia, however, prefers to offer tax exemption or a generous tax deduction, but these benefits are applicable to certain manufacturing companies only. It is interesting to note that South Africa measures up to an advanced economy, namely that of Singapore, with regard to this specific incentive, as it grants a cash benefit, which immediately provides assistance to the manufacturer, instead of allowing a tax deduction. It is therefore concluded that the incentive offered by South Africa is similar to that offered by Singapore and in line with that offered by Malaysia, and this incentive does not need to be amended.

4.1.3 Reinvestment and development incentive

In order to expand the manufacturing sector and encourage local and foreign investment, the South African government offers a grant of 15% to 30% of capital investment costs incurred with respect to establishing new operations or expanding existing ones. This grant is payable over a period of up to three years (DTI 2012b:4). A Malaysian company may claim a 60% reinvestment allowance for a period of 15 years (Malaysia 1967, sec. 133A), while companies in Singapore enjoy the benefit of a reduced corporate tax rate of 5% on profits above a predetermined base for a further ten years (Singapore 1967, sec. 19J(5), 19K). Another incentive offered by Singapore to manufacturing companies that invest more than S$10 million in equipment and machinery to increase productivity is the tax exemption of increased profits, after the expansion, for a period of up to ten years (Bell 2012:[2-3]).

The incentives offered by all three countries to encourage reinvestment in the manufacturing sector differ vastly. South Africa provides a cash grant over three years, Malaysia permits the deduction of a tax allowance for 15 years, and Singapore provides a lower tax rate or tax exemption of certain profits for ten years. As with the incentive discussed in the previous paragraph, South Africa prefers to provide a cash grant to reimburse capital expenditure incurred by a manufacturing company. Although a cash benefit would be more effective in encouraging new manufacturers, in particular, to incur this type of investment cost (Boadway & Shah 1992:97; South African Institute of Chartered Accountants 2009:9), there is clearly some scope for South Africa to explore the possibility of providing different or additional types of incentives to achieve its aim of expanding the manufacturing sector.

One of the above-mentioned incentives offered by Singapore could play a valuable role specifically in expanding existing manufacturing activities and could also be of great value to the manufacturer. This incentive provides income tax exemption of *increased* profits that occur as a result of the expansion of manufacturing activities. An incentive like this would ensure that the capital investment actually increases the productivity and profitability of the manufacturing sector, because the benefit to the manufacturer is directly linked to performance. However, there would be an additional administrative burden to determine the amount of increased profits, and the South African government would initially also not receive any tax revenue from the increased profits. The impact of these negative factors can be reduced by the fact that the country's economy would benefit from the growth in the manufacturing

sector (Thirlwall 2002:40) and that the tax revenue would increase after the exemption period had elapsed. It is recommended that the implementation of such an incentive be considered.

4.2 Incentives offered by South Africa and Malaysia only (class B)

There are four incentives that are offered by South Africa and Malaysia, but not by Singapore. These incentives are probably more relevant to emerging and developing economies such as South Africa and Malaysia. There are no incentives in common between South Africa and Singapore only, possibly because Singapore is an advanced economy. This could be indicative of different investment approaches or strategies.

4.2.1 Strategic projects

Both South Africa and Malaysia provide an incentive for strategic projects relating to an intensive investment in particular industries that could have a significant impact on the economy of the country. A South African manufacturing company may claim an additional allowance of 35% or 55% of the cost of manufacturing assets, depending on the qualifying status of the project (South Africa 1962, sec. 12I(2),(3)). Malaysia provides full tax exemption for five years to a strategic project with pioneer status, or an investment tax allowance of 100% on the capital expenditure incurred within a period of five years (Malaysia Manufacturers Directory 2012:[10]). Furthermore, Malaysia provides an allowance of 60% to 100% of capital expenditure incurred by manufacturing companies in specific industries to increase its productivity (Malaysia 1986, sec. 3).

Although Malaysia seems to offer greater incentives to manufacturers for strategic projects, South Africa does provide a significant deduction rate for capital expenses, which is in addition to the existing income tax deduction for manufacturing plant and machinery. If the higher of the two allowance rates in respect of strategic projects, namely 55%, is added to the allowance rate of new plant and machinery in the year of acquisition, namely 40% (South Africa 1962, sec. 12C), a deduction of just below 100% is permitted. This allowance rate is almost the same as that offered by Malaysia and therefore no adjustment to the current South African incentive is recommended.

4.2.2 Relocation of manufacturing activities

South Africa provides a grant of 15% of the transportation costs incurred to relocate new plant and machinery into the country from abroad (DTI 2012b:19–20), whereas Malaysia provides an income tax exemption for five years or an investment tax allowance of 100% for five years to existing local manufacturing companies that transfer their business to promoted areas in the country (MIDA 2012a:[5]).

South Africa's objective is to encourage foreign direct investment in the country's manufacturing sector, while Malaysia's aim is to increase local investment in specific regions in the country. This could explain why the design of the incentives is different. The South African government could explore granting an additional allowance on capital investment in order to provide a tax benefit to a manufacturer for relocating its existing business to regions where increased investment in manufacturing activities is required.

4.2.3 Automotive production and development

South Africa has an extensive incentive programme for the automotive industry, which entails the following benefits: import duty reduced to 25%, no import duty on 20% of components used for local assembly, an import duty credit of 55% based on production value added and a grant of 20% of productive assets (DTI 2012e). Malaysia grants a 100% tax exemption for five years or a 60% investment tax allowance for five years to companies that manufacture automotive components (MIDA 2012a:[8]).

South Africa has a far more intricate design for this incentive than Malaysia, which is apparent from the four types of benefits offered to South African manufacturers. The focus of South Africa's incentive falls mainly on reducing or exempting import duty, whereas Malaysia's incentive does not refer to this. Furthermore, South Africa provides a cash grant, whereas Malaysia offers a tax exemption or tax deduction. Due to the fact that South Africa's automotive incentive was reviewed and reinvented in 2008 (Business Day 2008), it is argued that no immediate adjustment to the South African incentive design be considered.

4.2.4 Small-scale companies' incentive

Small business corporations in South Africa may deduct the full purchase cost of manufacturing machinery in the year of acquisition. An allowance of 50% in year 1, 30% in year 2 and 20% in year 3 may be claimed in respect of other capital assets (South Africa 1962, sec. 12E(1),(1A)(b)). Malaysia offers a tax exemption for five years or an investment tax allowance of 60% for five years to small-scale companies. Furthermore, an accelerated capital allowance of 100% may be claimed by these companies when they reinvest in plant and machinery during the 2009 and 2010 years of assessment (MIDA 2012a:[6],[10]).

Although the designs of these incentives offered by the two countries are different, the benefits of South Africa's incentives for small business corporations appear to be comparable to those provided by Malaysia. Since South Africa allows a full deduction of the cost of manufacturing assets, there would be no reason to consider initiating an accelerated allowance, as Malaysia did.

4.3 Incentives offered by one country only (class C)

Malaysia offers three incentives to manufacturing companies which are not available to manufacturers in Singapore or South Africa, and Singapore and South Africa each have one manufacturing incentive that is not offered by either of the other two countries. South Africa's incentives are discussed first, followed by those offered by Malaysia and Singapore.

4.3.1 South Africa: Enterprise Investment Programme

The Enterprise Investment Programme encourages new and increased investment in the manufacturing sector by providing a grant that is linked to the total capital investment cost (DTI 2012b:4). The part of this incentive that relates to increased investment to expand existing manufacturing activities was discussed above (reinvestment and development incentive), as Malaysia and Singapore also have a similar incentive. These two countries do not, however, offer an incentive to encourage *new* manufacturing activities in general. Most of the incentives aimed at the manufacturing sectors of Malaysia and Singapore focus exclusively on manufacturing activities relating to specific products or regions (as determined for companies with pioneer

status). South Africa's Enterprise Investment Programme incentive is therefore unique, compared with the incentive in the other two countries, as all new manufacturing companies benefit from the incentive offered to them. Possibly, an incentive like this has been introduced by South Africa only because the South African government recognises that investment by all manufacturers, existing and new, will make a vital contribution to the growth of the economy (Department of National Treasury 2008a:5).

4.3.2 Malaysia: Industrial Linkage Programme

The Industrial Linkage Programme provides an incentive to vendors who manufacture their own goods in an industrial linkages programme, if these goods are classified as promoted products, such as plastic products, iron and steel, machinery, machinery components and electronic products. The benefit enjoyed by these manufacturers is a 100% tax exemption for five years or an investment tax allowance of 60%. This benefit is increased if vendors are able to achieve world-class standards in terms of the price, quality and capacity of their manufactured products (Malaysia 1986, sec. 1(d)).

4.3.3 Malaysia: Production of specialised machinery and equipment

Another Malaysian incentive is offered to new manufacturers of specialised machinery and equipment, such as plastic injection and extrusion machinery, robotics, factory automation equipment and machinery for specific industries. These companies may qualify for a 100% tax exemption for ten years or a 100% investment tax allowance. A reduced benefit is offered to existing locally owned companies that expand or automate their existing activities in the manufacturing of specialised machinery and equipment (MIDA 2012a:[10]).

4.3.4 Malaysia: Resource-based industries' incentive

A resource-based incentive is offered when local companies incur capital expenditure for the expansion of their activities in the manufacturing of rubber, palm oil and wood-based products that are of export potential. These products are some of Malaysia's natural resources which the country uses extensively for manufacturing purposes. The incentive provides a tax exemption of 100% for five years or an investment tax allowance of 100% (MIDA 2012a:[10]).

All three of the above-mentioned Malaysian incentives encourage manufacturers to produce or use specific items. The focus is either on promoted products such as iron and steel, specialised machinery such as robotics, or natural resources such as rubber. As mentioned earlier, South African incentives focus specifically on the manufacturing of automotive products and the use of other products or resources have been not been identified for incentive purposes. It is submitted that the South African government could consider introducing similar incentives as discussed above to increase the production of specific products or the use of specific natural resources that are crucial to the economy.

The design of incentives like these should be considered carefully. The benefit offered by each of the incentives initiated by Malaysia only is either a partial or full tax exemption or an investment tax allowance on the capital expenditure. The tax exemption of profits, otherwise known as a tax holiday, is not currently offered in South Africa, although this incentive has been available in the past in an effort to promote investment in the manufacturing sector (the tax holiday scheme in terms of Section 37H of the Income tax Act). If South Africa would consider

following the example of Malaysia in providing a tax holiday to manufacturing companies, then the possible impact of such an incentive should be examined first.

Although tax holidays are useful in signalling a welcoming attitude of the country towards local and foreign investment and are generally introduced to enable the country to remain competitive with neighbouring countries, this type of incentive is extremely costly and not so effective in influencing the decisions of investors. Furthermore, only profitable companies can benefit from a tax holiday, and not much assistance would thus be available to start-up companies (Wells, Allen, Morisset and Pirnia 2001:41-43, 45).

Therefore, given South Africa's circumstances, the deduction of a tax allowance on the capital expenditure is proposed instead of a tax holiday. In an effort to motivate manufacturers to engage in the manufacturing of the specified product or resource or to expand existing manufacturing activities in this field, a significant deduction over a short period would be preferable.

4.3.5 Singapore: Start-up companies' incentive

Singapore permits a start-up incentive which assists new companies by offering a tax exemption on part of their chargeable income for the first three years of production resulting in a reduced tax liability (Inland Revenue Authority of Singapore 2012b). This enables these new companies to accumulate their cash flow and profits in the first few years in order to become more profitable and to re-invest in operations. Previously, South Africa offered a similar incentive to small business corporations, but it was withdrawn due to the introduction of other incentive measures. In terms of the withdrawn provision, small business corporations in South Africa could claim a double deduction, limited to R20 000, of expenditure and losses actually incurred by them in the tax year in which they commenced trading. This deduction resulted in a decrease in the taxable income and consequently a lower tax liability (Department of National Treasury 2003:53).

It is clear that South Africa is aware of and has explored the use of an incentive like the one currently offered by Singapore to start-up companies, although South Africa applied this incentive only to small business corporations. This incentive could be reintroduced in an effort to encourage new manufacturing companies to commence business. As discussed above, a tax exemption or tax holiday would probably not be a feasible option, but a double deduction of certain expenses or losses, as previously offered by South Africa, could be of assistance to South African start-up companies.

4.4 Incentives offered by Malaysia and Singapore only (class D)

The last category reflects on the two incentives offered by Malaysia and Singapore, but not by South Africa. It should be considered whether one or more of these two incentives could be implemented by South Africa in an effort to enhance the country's competitive advantage in attracting local and foreign manufacturers.

4.4.1 Tax holiday (pioneer status) and investment tax allowance

A partial or full tax holiday or an investment tax allowance is granted to manufacturing companies that specifically produce preferred products, otherwise known as companies with pioneer status. A company may only apply for one of these two incentives and the decision to

grant them is based on the company's estimated profitability and the amount of capital expenditure required for the project. The tax holiday in Malaysia provides partial exemption from paying income tax (Malaysia 1986, sec. 1(a)), while Singapore grants full tax exemption (Singapore 1967, sec. 6, 13). Malaysia offers an investment tax allowance of 60% of the capital expenditure relating to qualifying projects incurred within five years (Malaysia 1986, sec. 2(a)), whereas Singapore offers an investment tax allowance of up to 100% of capital expenditure incurred within five years (Singapore 1967, sec. 68).

These incentives focus specifically on encouraging investment in the manufacture of specific products such as pharmaceuticals, wood, rubber and steel in the case of Malaysia, and high-technology products in the case of Singapore. Further benefits are also provided for companies with pioneer status that invest in a specific region of Malaysia, in order to encourage investment in a particular geographical area. It is clear that the aim of all these incentives is to promote the production of specific items that are significant to each of these countries.

As mentioned in the section above relating to the three incentives provided by Malaysia only, South Africa might consider an investment tax allowance incentive if the production of specific products needs to be promoted in the future, but at present, the introduction of a tax exemption or tax holiday is not recommended.

5. CONCLUSION AND RECOMMENDATIONS

The South African government has identified the manufacturing sector as a sector which it believes would assist extensively in the provision of much-needed growth and employment creation in the country. The aim of this article was to compare the incentives available to the manufacturing sector in South Africa with those available in Malaysia and Singapore, in order to identify additional incentives that could be considered for introduction in South Africa to attract more investment in the manufacturing sector. South Africa faces some obstacles to attracting investment, such as a high unemployment rate and a lack of skilled workers. Incentives are usually among the relatively few measures that can be introduced to minimise the effects of these investment barriers and they are continually used by both developed and developing economies to attract investment.

It is recognised that the research reported in this article only considered incentives. It was not intended to be a study of other measures and factors which could play a role in investment and also does not cover the many and diverse factors that affect the investment decision. Although incentives may not override negative attributes of a country, various incentives have been found to influence investment decisions. The scope of this research was not to determine the effectiveness of incentives, but to investigate whether this investment promotion tool could be utilised even further. This research also only considered incentives that are directly applicable to the manufacturing sector, and not all existing incentives.

For the comparison purposes of this research, incentives were classified into three main categories, namely incentives that promote specific investment, incentives that encourage investment in capital assets and incentives that reduce the company's fiscal burden. The first incentive category, namely incentives that promote specific investment, was addressed in this article. The other two incentive categories will be discussed in a separate article. The comparison between the incentives offered by South Africa, Malaysia and Singapore which promote specific investment revealed that all three countries have several incentives in

common, although closer inspection confirmed that the design and benefits of these incentives for manufacturers differ in most cases. There are also a number of incentives that are offered either by Malaysia or Singapore, or both countries, but not by South Africa.

The results of the analysis of the comparison suggest that incentives relating to the following be considered for introduction:

- Manufacturing of specific products or the use of specific natural resources: a significant deduction over a short period (such as two years) of capital expenditure, by means of an accelerated wear-and-tear allowance
- Start-up manufacturing companies: a partial exemption of profits or a double deduction of a limited amount of expenses or losses in the first two to three years
- Relocation to a preferred geographical area: an additional allowance on capital investment incurred by manufacturing companies to relocate their business
- Increased profits of manufacturing companies: a partial or full exemption of increased profits resulting from a significant amount of increased capital investment for a limited period

These recommended incentives are expected to contribute to the much-needed growth of the manufacturing sector and ultimately to South Africa's economic development. It is acknowledged that the South African government cannot merely introduce incentives without careful consideration of all aspects involved and their impact on the economy. In order to achieve the desired outcome, the unique design of each incentive should also be carefully considered. Further research could focus on evaluating whether existing incentives have an effect on South Africa's economic activity and whether the new or revised incentives, as proposed in this article, would be practical and effective in the country's unique circumstances. It is expected that the introduction of the additional incentives would enable the manufacturing sector to grow and to be at the forefront of South Africa's economic growth and employment creation.

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