BUSINESS CLIMATE SURVEY 2014

EU TRADE AND INVESTMENT IN SOUTH AFRICA

Business Climate Survey 2014: EU Trade and Investment in South Africa was researched and compiled by Tutwa Consulting and published by Imani Development South Africa.

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This Business Climate Survey is based on responses to a questionnaire circulated to some 1 500 companies and responded by 153 EU-connected companies during the second part of 2014. It is meant to provide an analytical tool to understand trends affecting foreign direct investment sentiment in South Africa at the time the survey was conducted. The findings and views expressed herein should not be construed as representing the stance of the European Union or its member states in respect on any of the matters discussed.

NOTE
Due to rounding, numbers presented throughout this survey may not add up precisely to 100 per cent.
R = South African Rand.

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FOREWORD

The European Union (EU), as a bloc, remains the largest foreign investor in the South African market. The EU and South Africa are long-standing, and remain significant, partners in key areas of policy, trade, investment and social reform.

It is perhaps most desirable that in supporting the aspirations of the South African government and its people, represented in the National Development Plan, that EU companies – in addition to providing jobs and community support – actively contribute substantively to the evolving debate that underpins the long-term, sophisticated relationship between both partners.

Against this backdrop, in late 2014, a total of 153 EU companies, operating in South Africa, participated in this Business Climate Survey – under the auspices of EU–SA Business Links – a precursor to the newly launched EU Chamber of Commerce and Industry of Southern Africa.

The survey, which represents a snapshot in time, measures the views of EU companies on the South African business and investment landscape. It measures the experiences of respondents on a cross-section of aspects relating to the business environment – at that time – and seeks to contribute to the broad objective of improved communication and advocacy between the EU business community and South African stakeholders.

The survey shows that, in general, EU investors remain committed to South Africa. The majority of respondents state that they would recommend South Africa as an investment destination. Nevertheless, there are a number of common concerns within the EU investor community on various aspects of the business and investment climate. This would include recent constraints such as the current electricity situation, which only escalated after the survey was concluded.

There is, therefore, need for continued dialogue on interventions to improve the business environment and improve competitiveness. The survey will undoubtedly provide a basis for continuing advocacy work, which will be taken forward by the newly established EU Chamber of Commerce and Industry.

Stefan Sakoschek
Executive Chairman
EU Chamber of Commerce and Industry of Southern Africa

EXECUTIVE SUMMARY

This report presents the findings from the second survey of European Union (EU) trade and investment with South Africa (SA). Compared to the first survey, the 2012 *White Book on EU Trade and Investment in SA* (hereafter referred to as the *White Book*), a new survey method was used which saw an increase in the number of EU companies responding and gave a larger dataset to work with. The overall aim was to identify the degree of EU firms' satisfaction or dissatisfaction with the South African business climate, to survey particular aspects of the business climate and to identify emerging trends and concerns among respondents.

Aggregating and analysing the respondents' profiles helped to identify underlying general patterns and to interpret the findings. Respondents were categorised according to their country of origin, the size of the company, the duration of activities in South Africa, and the main industry in which they did business. When looking at the respondents' profiles and economic contributions the following is apparent:

» Approximately 10 per cent of the 1 500 companies to which the survey was sent responded; 153 in total.
» Most respondents were from smaller EU economies.
» Ninety per cent of the respondents are classified as small and medium sized enterprises (SMEs) by number of employees, of which more than half of the respondents increased their staff in the past three years.
» A third of respondents reported turnovers of over R100 million from their South African operations and two thirds reported an increase in turnover in the past three years.
» One third of firms had been in South Africa for 20 years or more, predating the advent of democratic governance, and a further 25 per cent of firms for between 11 and 20 years.
» EU respondent firms conducted business across a wide range of industries in SA, particularly in Gauteng province. The largest group is categorised as being in the services industry.

When interpreting the results of the survey, it is known that the majority of respondents represent SME firms from smaller EU countries, with medium sized turnovers, drawing on substantial experience in South Africa, and operating in various industries.

In 2014, the overall satisfaction of EU firms with the South African business climate was decidedly mixed: more than twice as many firms were dissatisfied than were satisfied with it. This represents a sharp deterioration on the mostly positive perceptions recorded in 2012. In 2004 the majority of respondents experienced a decline in the business climate over the past year and held the opinion that it would remain unchanged for the next year; compared to the 2012 survey when more than three quarters of respondents thought the business climate would improve. Social unrest and political instability emerged as the major concerns amongst the sample group.

On the plus side, and in contrast to their negative opinion of the South African business climate, the overwhelming majority of respondents said they would recommend South Africa as a business location.

The principal barriers to doing business remained largely the same across the two surveys, but this is hardly surprising, as they constitute microeconomic and socio-political problems that had not been resolved since the previous survey. Specific barriers to doing business in South Africa were identified and are shown in the figure overleaf, in decreasing order of severity.[1]

From the reported barriers it appears that EU firms see substantial obstacles to conducting business in South Africa. The perception is that the situation will continue to deteriorate, reinforcing the impression that South Africa's microeconomic policies and restrictions present a mixed picture for foreign investors. However, as can be expected from these types of surveys, positive assessments are probably underrepresented. South Africa has a very sound macroeconomic environment and a strong financial sector in which investors find some solace. This is reflected in the survey results.

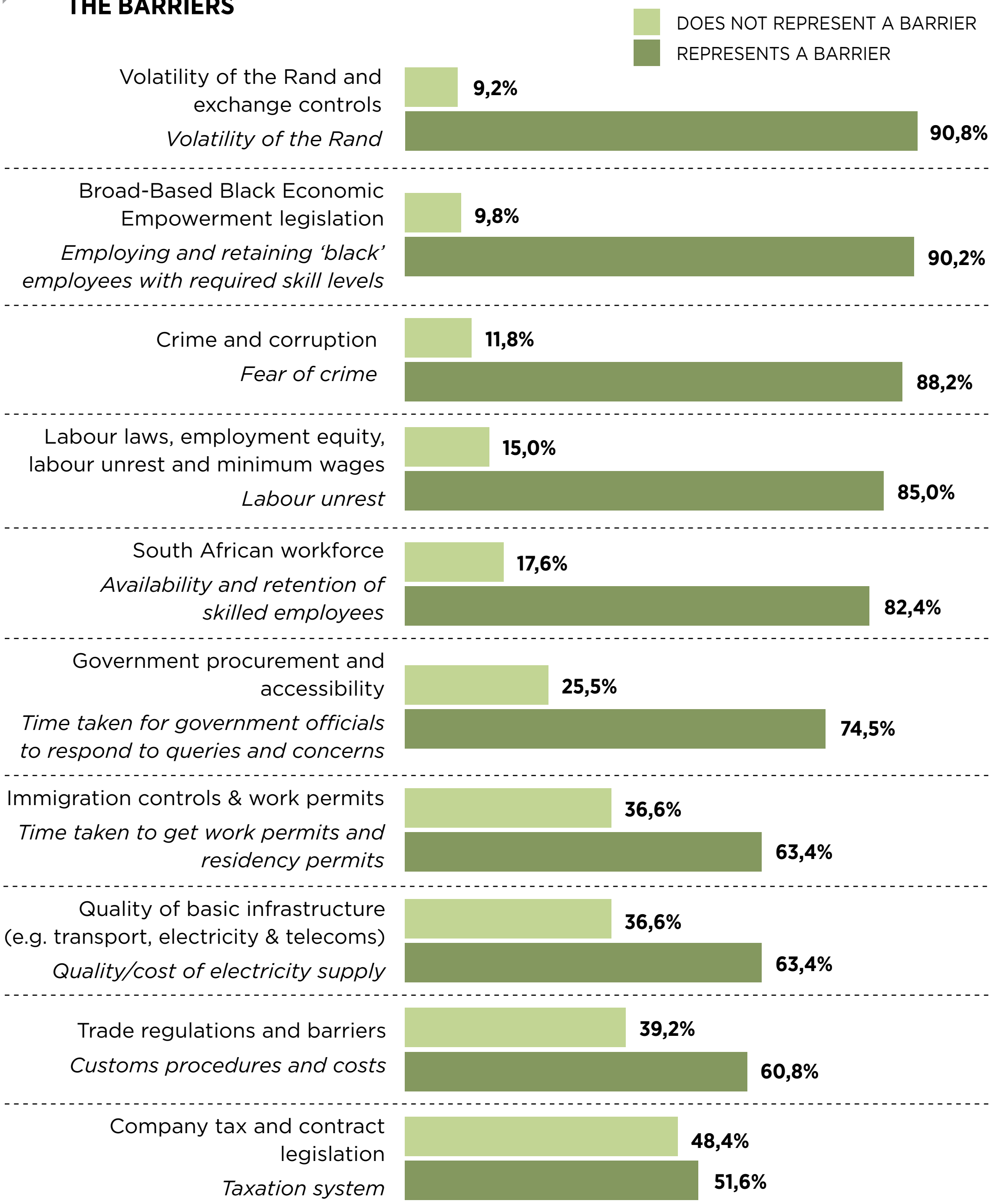
The supplementary insights from statistical analysis show that large EU-based companies with high turnovers, operating for a longer time in South Africa, are more pessimistic concerning the possibility of the South African business climate improving. Since the results show that they are more active with regard to investment in skills and assistance to South African businesses, this is a cause for concern. Respondents with a large stake in the South African economy are more optimistic about the future business climate but this only holds true for companies not operating in the primary sector. This correlates with the perceived threats and barriers to doing business, of which land reforms and nationalisation are seen as particular threats for companies operating in the primary sector.

In a broader context, and based on surveys measuring similar indicators, the views expressed by respondents are likely to be shared among the wider business community. By comparing the results found in this report to the Global Competitiveness Index (GCI) of the *Global Competitiveness Report 2014–2015* and the *Doing Business 2014* reports we established that concerns relating to the South African workforce and labour market are equally held, as are concerns over crime and corruption, government procurement, and the quality of infrastructure.

What is also apparent when looking at the broader context is that compared to a select basket of South Africa's emerging market peers, the South African business climate shows more improvement than decline in the specific barriers to doing business we chose for this analysis. Of the 24 indicators used to compare country level competitiveness, South Africa has increased in ranking in 17 of them in the past year. This being said, South Africa more consistently ranks in the bottom half of the selected group of countries and ranks highest in only four of the 24 indicators.

1 It is important to note the survey was conducted in September and October 2014. Since then new visa regulations have been implemented, and Eskom implemented a more intensive load-shedding programme. Consequently, it is possible that these two issues would feature higher on the list should the survey be implemented now.

BARRIERS TO DOING BUSINESS AND THE GREATEST CONCERN REGARDING THE BARRIERS



Although South Africa is perceived as having a deteriorating business climate and that respondents face growing microeconomic barriers to conducting business, it is still a desirable investment destination when compared to emerging market peers. The majority of respondents are experiencing, and foresee, growth in both turnover and number of staff. However, the persistence of barriers to conducting business, as measured in the 2012 EU investment survey, the GCI and the *Doing Business 2014* report, is likely to drive down EU investor's confidence in the South African business climate relative to South Africa's African peers.

1 BACKGROUND

Over 2 000 EU companies operate in South Africa, many of them in the manufacturing and services sectors, generating hundreds of thousands of jobs and billions of Rands in export revenue. However, stocks of invested capital from the EU have decreased over the past three years for which EU data is available[2], highlighting specific elements of concern among EU investors, notably small and medium size companies.

Consequently, in August 2014, the EU Chambers of Commerce distributed an online questionnaire among approximately 1 500 EU-based firms that conduct business in South Africa. Its purpose was to establish, broadly, the degree to which their member firms were satisfied or dissatisfied with the business climate and particular aspects of the business environment in South Africa. It was also intended to identify emerging trends in relation to satisfaction or dissatisfaction with the business climate.

The report is not the first analysis of the perceptions that EU-based firms have of the South African business climate. In 2012, a *White Book on EU Trade and Investment in SA* was published.[3] The 2012 report followed a survey methodology via face-to-face interviews. The current survey was conducted online, via a web portal. These different methodologies have their respective advantages, with the former offering greater qualitative insight and the latter greater quantitative insight. Whereas in the 2012 *White Book*, 88 firms responded, this time about 10 per cent of all EU-based companies, 153 altogether, replied to the questionnaire. This larger number yielded more robust results and enabled the researchers to establish a number of statistical relationships between the respondents' characteristics, such as size, country of origin, sector, and time period of operations in South Africa, and the responses. A dataset for calculating these correlations regarding the present and expected business climate in South Africa was accordingly created.[4] In this report we first present the direct responses, and then interpret the results using the dataset.

Overall, the answers to the 2014 questionnaire indicate that the respondents' satisfaction with the South African business climate was mixed.[5] The picture changes slightly when looking at expectations, with a small majority expecting deterioration versus improvement, and no respondent expects an improved situation. Nonetheless, a substantial majority of respondents consider continuing to do business in South Africa, or recommend doing business in South Africa.

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2 According to Eurostat figures overall stocks of EU sourced foreign direct investment (FDI) in South Africa were as follows: €75,4 billion in 2010, €55 billion in 2011 and €58 billion in 2012. By contrast outward FDI stocks from the EU worldwide increased in this period.

3 *White Book on EU Trade and Investment in SA*, Genesis Analytics (Pty) Ltd, Johannesburg, 2012.

4 This final dataset was created by Tutwa Consulting and is available on request.

5 The 2012 survey did not measure perceptions of the South African business climate.

Detailed results are reported in section 3. These results stand in contrast to those presented in the 2012 *White Book*, where around 75 per cent of respondents indicated that they were satisfied with overall South African business conditions, and expressed optimism that things would improve. While the two results are not strictly comparable, they do seem to indicate deterioration in EU companies' perceptions of the South African business environment.

Some care is necessary, since it could be argued that the questionnaire has attracted, in particular, respondents that have taken an opportunity to air their frustration; this caveat is backed by the contradiction between the assessment of the business climate and the recommendations to invest in South Africa.

With respect to the principal barriers to business, the picture has not changed dramatically in comparison with the first *White Book*. In the 2012 report the five core obstacles to conducting business from the perspective of EU-based firms were identified in order of decreasing severity:

1. Workforce skills and education;
2. Broad-Based Black Economic Empowerment (BBBEE) legislation;
3. Government bureaucracy;
4. Corruption; and
5. Currency volatility.

In comparison, this year's survey identifies the following five groups of barriers to conducting business in South Africa, in order of decreasing severity:

1. Volatility of the Rand and exchange controls;
2. BBBEE legislation;
3. Crime and corruption;
4. Labour relations, labour quality and cost; and
5. Government procurement and accessibility.

While the two methodologies are not directly comparable, since questions were posed differently and issues grouped together in different ways, there is evidently substantial continuity between the two sets of results. The most striking observations are the following: the movement of currency issues to the top of the list of concerns; continued concern over BBBEE legislation, corruption, and government bureaucracy, particularly government procurement; and ongoing concerns over the workforce. The results specific to this year's survey are discussed in detail in section 4.

The report is structured as follows. Section 2 aggregates respondents' profiles according to their responses, and establishes some broad details of their South African footprints. Section 3 presents their broad perceptions of South Africa's business climate, using both qualitative and quantitative insights. Section 4 reviews their perceptions of specific barriers to conducting business in South Africa. In addition to reporting the results in detail, in section 5 we report on the statistical analyses conducted to complement the empirical overview. In section 6 we contrast the results with South Africa's aggregate performance in select international business environment surveys in comparison with selected emerging market peers. This allows the survey results to be viewed in a wider international context, rather than in isolation. Based on the preceding analysis, in section 7 we outline broad policy recommendations for further improving the business climate for EU-based companies in South Africa.

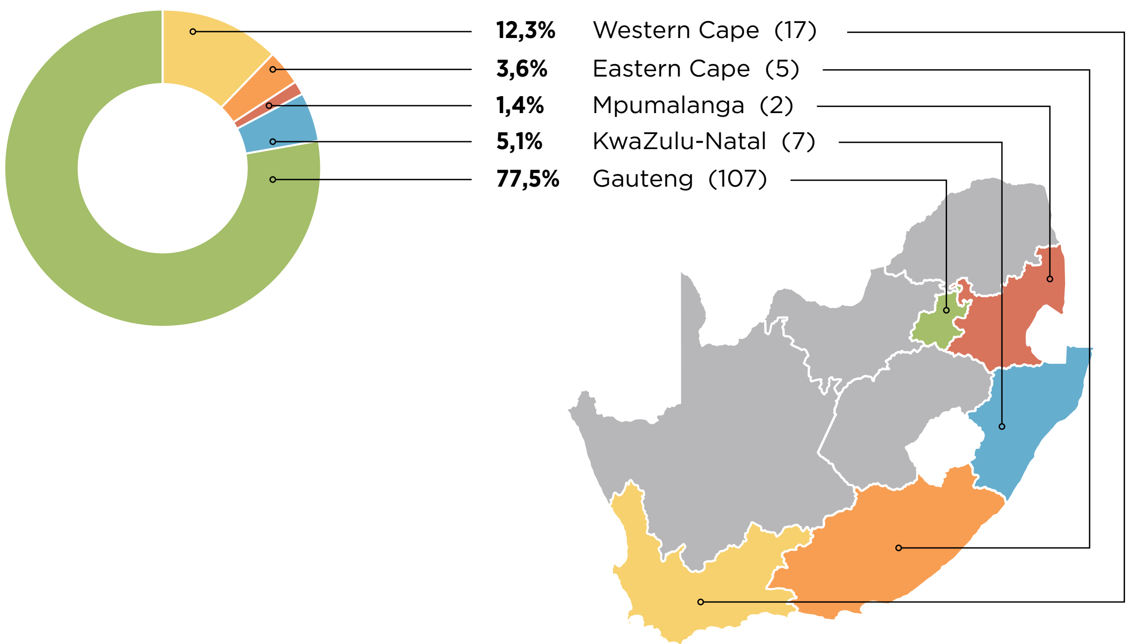
2 RESPONDENTS' PROFILES AND ECONOMIC CONTRIBUTION

In total, 153 companies replied to the questionnaire. This number gives enough information on the one hand, but does not allow for a sophisticated statistical breakdown on the other hand, since the number of companies from certain sectors or EU member countries is too small to run statistically significant country or sector regressions. Therefore, to supplement the results, we conducted the statistical analysis presented in section 5.

2.1 RESULTS

A proper interpretation of the survey results requires a closer look at particular features of the respondents. The respondents were mainly in the higher management of the respective companies. For 140 of the 153 EU-based companies, replies were from the following: the owner (22), senior management (84), or middle management (34). This indicates that the questionnaire was taken seriously, and that the resulting data are reliable and trustworthy.

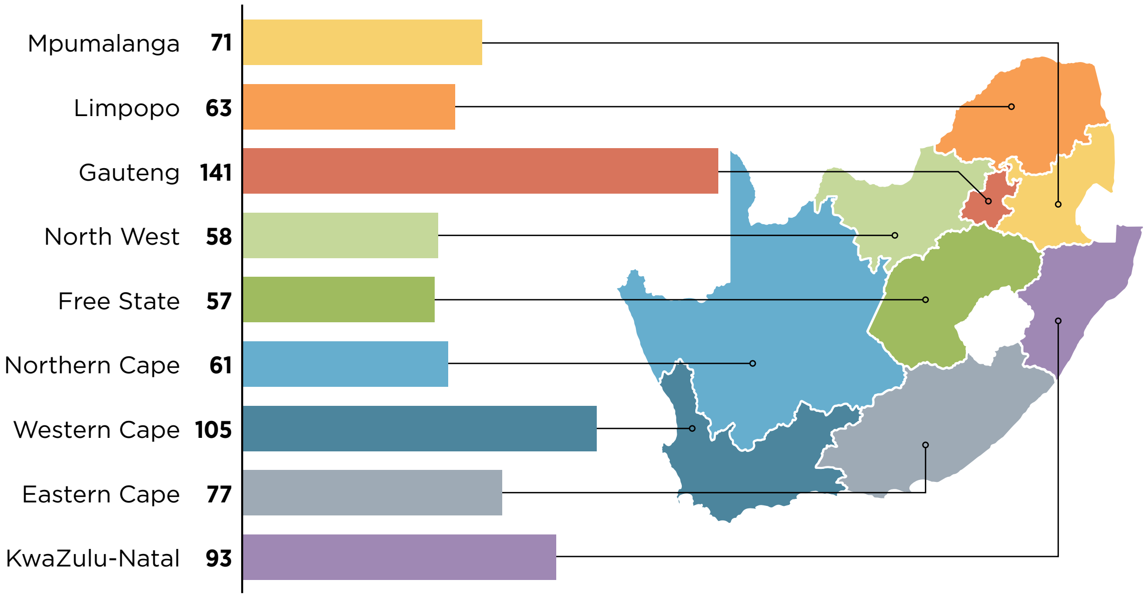
FIGURE 1 PROVINCIAL LOCATIONS OF THE HEAD OFFICES IN SOUTH AFRICA



NOTE: Due to rounding, numbers presented throughout this survey may not add up precisely to 100 per cent

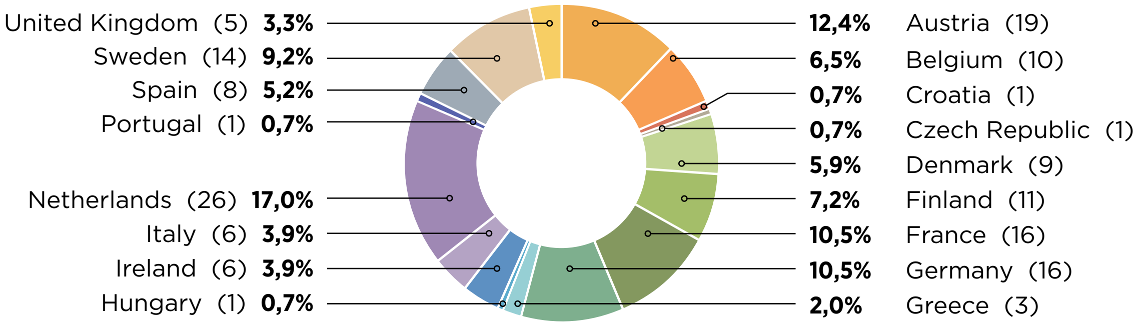
Regionally, most companies do business in Gauteng and the Western Cape, as shown in Figure 1. The head offices of 107 of 138 companies are in Gauteng (15 of the 153 companies are not legally incorporated in South Africa). Whereas headquarters are distributed among 5 provinces, Figure 2 shows that some companies conduct business in other provinces as well, although the three main commercial centres, Gauteng, KwaZulu-Natal and Western Cape, feature more prominently.

FIGURE 2 PROVINCES WHERE EU-BASED COMPANIES OPERATED



Four features mostly characterise the responding EU-based companies: **country of origin**, **size of the company**, **duration of activities** in South Africa, and the **main industry** in which they do business. Analysing the structure of respondents may help to identify general patterns and thus to interpret the findings appropriately. In addition, information about the perceptions of certain groups of respondents may help the South African government to focus on the core issues required to improve the business climate.

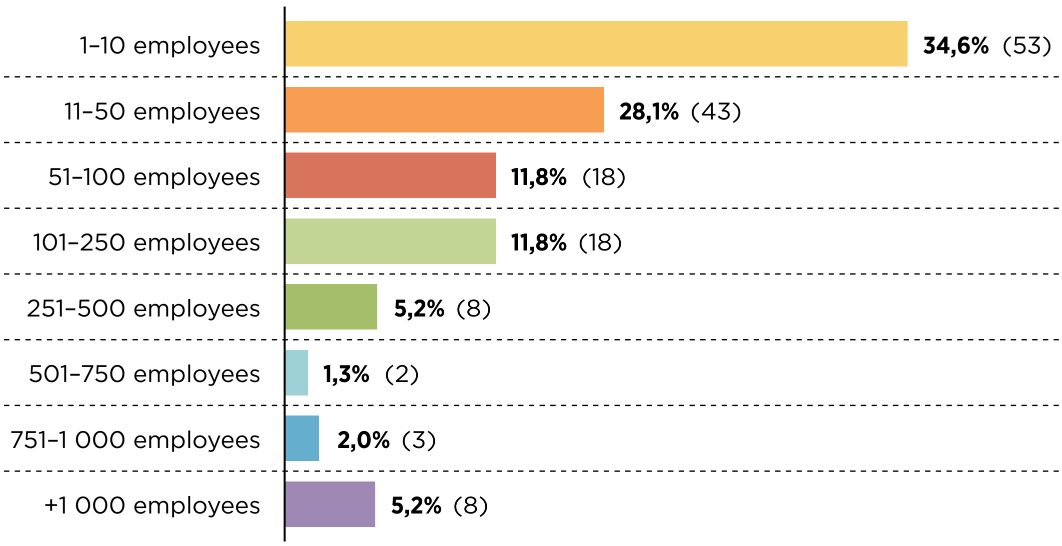
FIGURE 3 RESPONDENTS' STATED GEOGRAPHICAL ORIGINS



Regarding the country of origin, companies with a parent enterprise in a large EU member country, as measured in terms of total gross domestic product, may feel relatively confident since they may believe that the South African government will take their business environment concerns more seriously. In this light, Figure 3 shows that the majority of the respondents are from smaller EU member countries. Of the larger EU countries, 16 companies from each of Germany and France have responded, six from Italy, and five from the United Kingdom. Of companies from smaller countries, 26 from the Netherlands responded, 19 from Austria and 14 from Sweden.

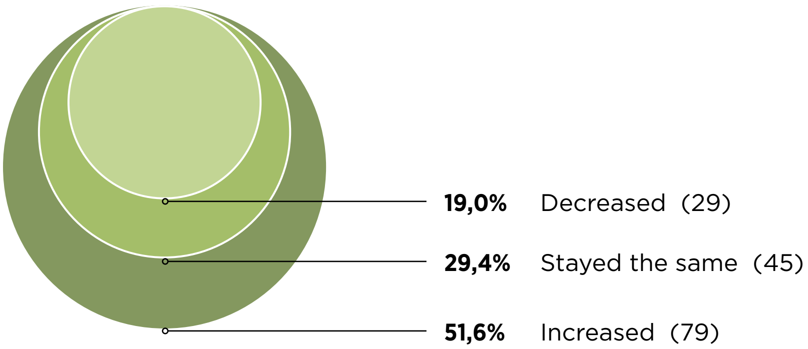
Figure 4 shows that three quarters of the respondents employ fewer than 100 staff, a third employ fewer than 11, and 13 companies have more than 500 employees.

FIGURE 4 SIZE OF SA OPERATIONS IN TERMS OF PERMANENT EMPLOYEES



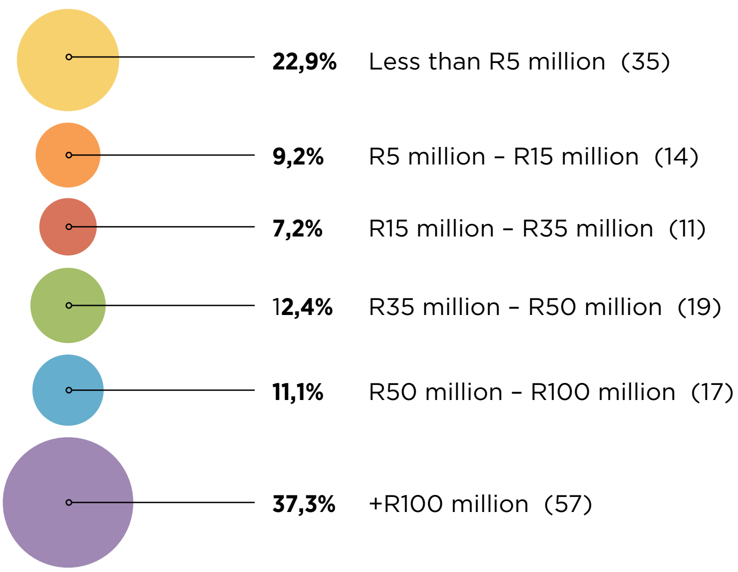
Larger companies might feel they can cope better with the issues identified in the survey than smaller ones. In general, it is easier for large firms to deal with regulation than is the case for small firms. The relevant indicators used in the survey are the recent changes in the number of employees and recent changes in turnover. Nonetheless, despite being SMEs, on average the respondents hired more staff in the past three years. Figure 5 shows that half of the respondents increased staff, whereas only a fifth reduced personnel.

FIGURE 5 CHANGES IN THE STAFF COMPLEMENTS OF PERMANENT EMPLOYEES OVER THE PAST THREE YEARS



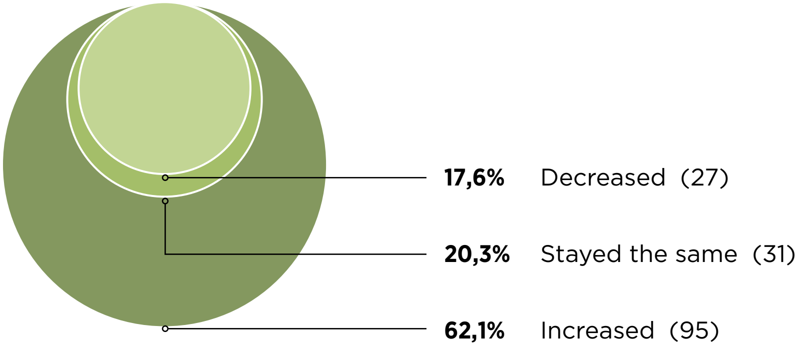
As for turnover, the results are comparable but distinct. Figure 6 shows that slightly more than a third of respondent companies derived annual turnover of more than R100 million from their South African operations.

FIGURE 6 TOTAL TURNOVER FROM BUSINESS/TRADE ACTIVITIES IN OR WITH SOUTH AFRICA IN THE PREVIOUS FINANCIAL YEAR



On the other hand, a fifth of the companies earned less than R5 million in turnover. This indicates that some companies had high turnover with small staff complements.[6] Comparing the numbers for employees (Figure 4) with those for turnover (Figure 6) reveals that about a third of the companies employed between one and 10 workers, whereas 37,3 per cent of companies were in the highest turnover category. In other words a simple majority had a high turnover, whereas a simple majority employed 1–10 people.

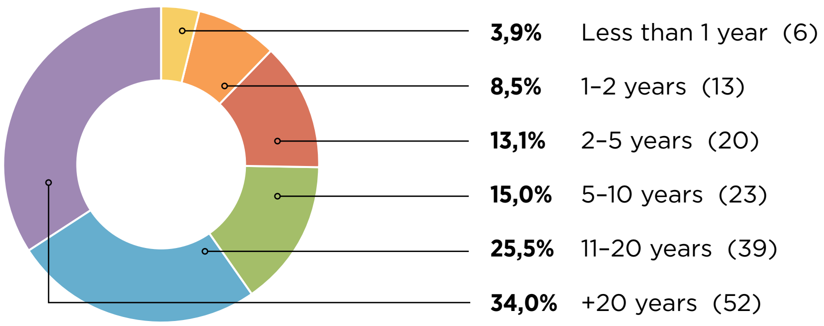
FIGURE 7 CHANGES IN TURNOVER FROM BUSINESS/TRADE ACTIVITIES IN OR WITH SOUTH AFRICA OVER THE PREVIOUS THREE YEARS



While the average annual turnover was rather small, Figure 7 shows that it had grown in the past three years for close to two thirds of the companies. A fifth of the respondents reported lower turnovers.

It may be assumed that the longer a firm is in the country, the better it can adjust to the business environment. On the other hand, it is possible that a well-established firm will be concerned about the situation, in particular when the management observes deterioration in the business climate. Unfortunately, regarding the duration of activities in South Africa, no clear findings emerged.

FIGURE 8 DURATION OF RESPONDENT COMPANIES BUSINESS ACTIVITIES IN SA

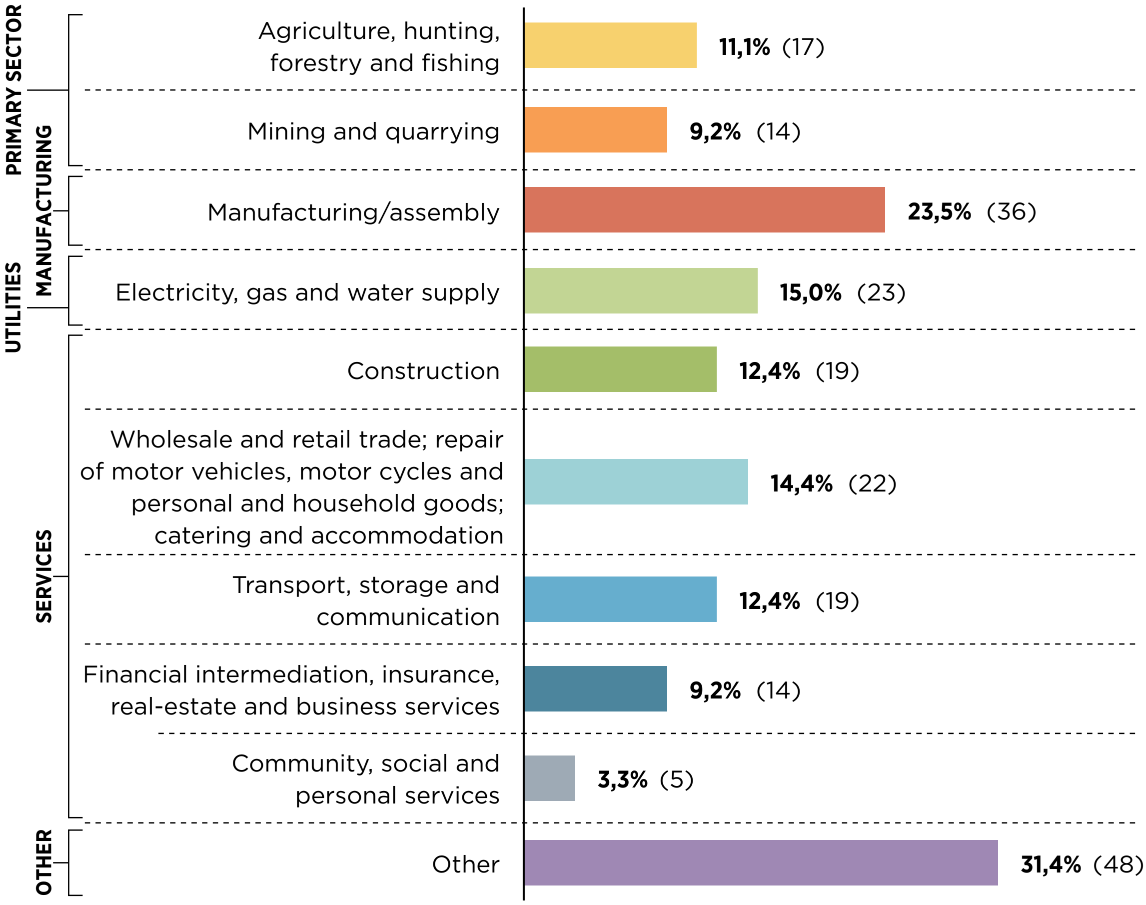


6 Unfortunately, the data did not allow for calculating a statistically robust relationship between turnover and size of the company (measured as number of employees). Therefore, we can only guess about this relationship.

Figure 8 shows that a majority of respondent companies had gathered substantial experience of operating in the country. One third (52) of the firms had been in South Africa for 20 years or more; about a quarter (39) have been present between 11 and 20 years; and 15 per cent (23) have been in the country for more than five years but fewer than 11 years. Only 39 firms had operated for five years or less, of which six firms had been present for less than one year. Overall, one may assume that those firms with more experience in South Africa will have developed some sort of resilience towards unique South African problems.

The main industry of the responding companies sheds some light on their economic situation, and influences their perceptions of the local business climate. Firms in thriving sectors might perceive the business environment more optimistically than those in declining industries. Problems may also occur in sectors that are politically difficult, such as farming and mining. In addition, difficult labour relations may cause problems in certain sectors.

FIGURE 9 INDUSTRY SECTORS OF EU COMPANIES OPERATING IN SOUTH AFRICA



Here we find some respondents indicating that their companies were active in several industries, accounting for the fact that the number of responses (217) exceeds the number of overall survey respondents (153). Figure 9 shows that 31 companies did business in the primary sector (categories 1 and 2); 36 in manufacturing; 23 in utilities, 79 in the services sector (categories 5–9), and the remaining 48 firms specified the ‘other’ category.

2.2 SUMMARY OBSERVATIONS

The overall impression that emerges from this part of the analysis is one of companies from relatively small EU economies, operating mostly in South Africa’s economic heartlands, with relatively small workforces but medium-sized from the turnover perspective, and mostly expanding on both fronts, drawing on relatively substantial experience of the South African business environment in terms of longevity in the country, and covering a fairly even spread of economic activity.

However, first impressions need to be tempered by closer inspection. In section 5 we pick up the four characteristics analysed here, through conducting a statistical analysis of the firms’ features and their responses, and we interpret this against the background of the rather critical survey responses displayed in the following two sections.

3 PERSPECTIVES ON SOUTH AFRICA'S BUSINESS CLIMATE

Here we report on the general survey results pertaining to questions regarding respondents' views on the general business climate, now and in the past, their expectations for the immediate future, and their stance towards recommending South Africa as a location for business.

FIGURE 10 SATISFACTION WITH THE OVERALL BUSINESS CLIMATE IN SOUTH AFRICA

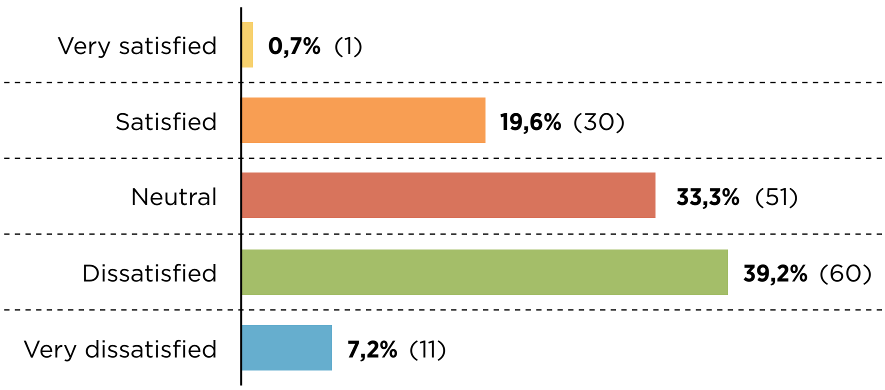


Figure 10 shows that more than twice as many firms were dissatisfied than were satisfied with the overall business climate. This stands in contrast to the 2012 *White Book* exercise in which 73 per cent of respondents indicated their satisfaction with the overall business climate.

Figure 11 shows that only about 8 per cent of respondents saw a better business environment than a year before, and whereas 60 per cent had experienced a worsening of the business climate, roughly a third of the companies had not seen a change.

Similarly, the expectations firms had with regard to whether the future business climate would improve or deteriorate confirm respondents' apparent pessimism.

FIGURE 11 CHANGES IN THE BUSINESS CLIMATE IN SOUTH AFRICA IN THE PREVIOUS 12 MONTHS

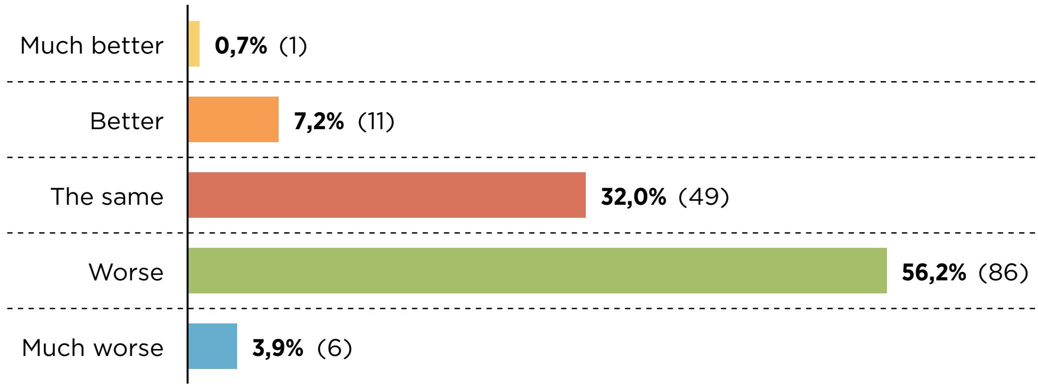
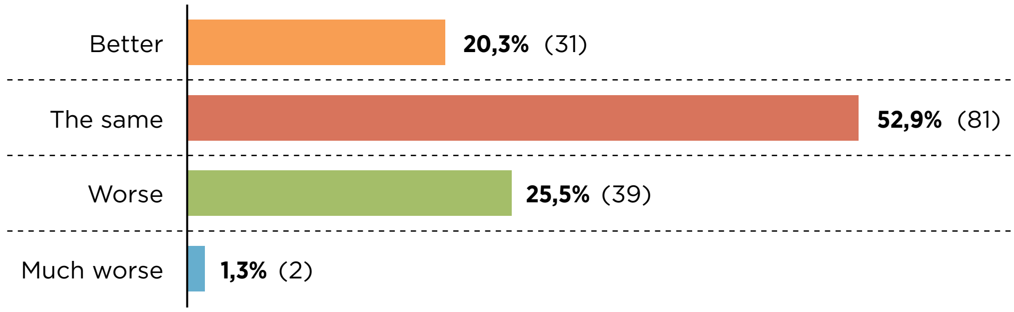


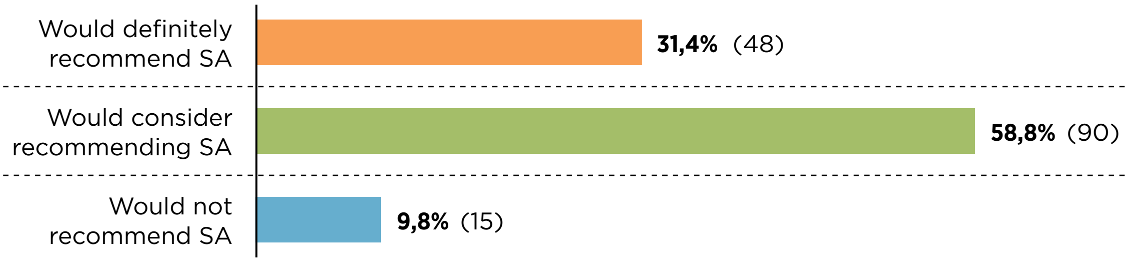
Figure 12 shows that 31 companies saw a brighter future for their business, while 41 companies expected a worsening climate in the coming year. Half of the respondents did not expect any change to the business climate in the South African economy. In the 2012 *White Book* survey, more than three quarters of respondents expected the business climate to improve; clearly expectations had deteriorated since then.

FIGURE 12 EXPECTATIONS OF THE BUSINESS CLIMATE IN SOUTH AFRICA OVER THE NEXT 12 MONTHS



Notwithstanding these critical results, Figure 13 shows that the great majority of the respondents potentially would recommend South Africa as a business location; slightly less than 10 per cent would not give such a recommendation. About a third of these firms would definitely recommend South Africa for doing business.

FIGURE 13 RECOMMENDING SOUTH AFRICA TO ANOTHER EU COMPANY AS A PLACE TO DO BUSINESS



In light of the picture that emerged from section 2 of firms with small but growing physical footprints, relatively high and growing turnovers, and that had generally been in South Africa for a fairly long time, these results are interesting, but contradictory. In the absence of conducting personal interviews with the respondents, we can only speculate as to the reasons for this evident contradiction. For example, perhaps people were sceptical about the short term, but saw worthwhile longer-term opportunities. Perhaps those who had been here for a while had developed coping mechanisms, while the new entrants faced a steeper learning curve, which they were prepared to work through.

In the next section we review survey responses regarding specific barriers, or perceived barriers, to conducting business in South Africa.

4 PERSPECTIVES ON SPECIFIC BARRIERS TO DOING BUSINESS

4.1 THE GENERAL PICTURE

Respondents were asked to give their perceptions of specific barriers to doing business in South Africa.

FIGURE 14 RANKING OF BARRIERS TO CONDUCTING BUSINESS IN SOUTH AFRICA

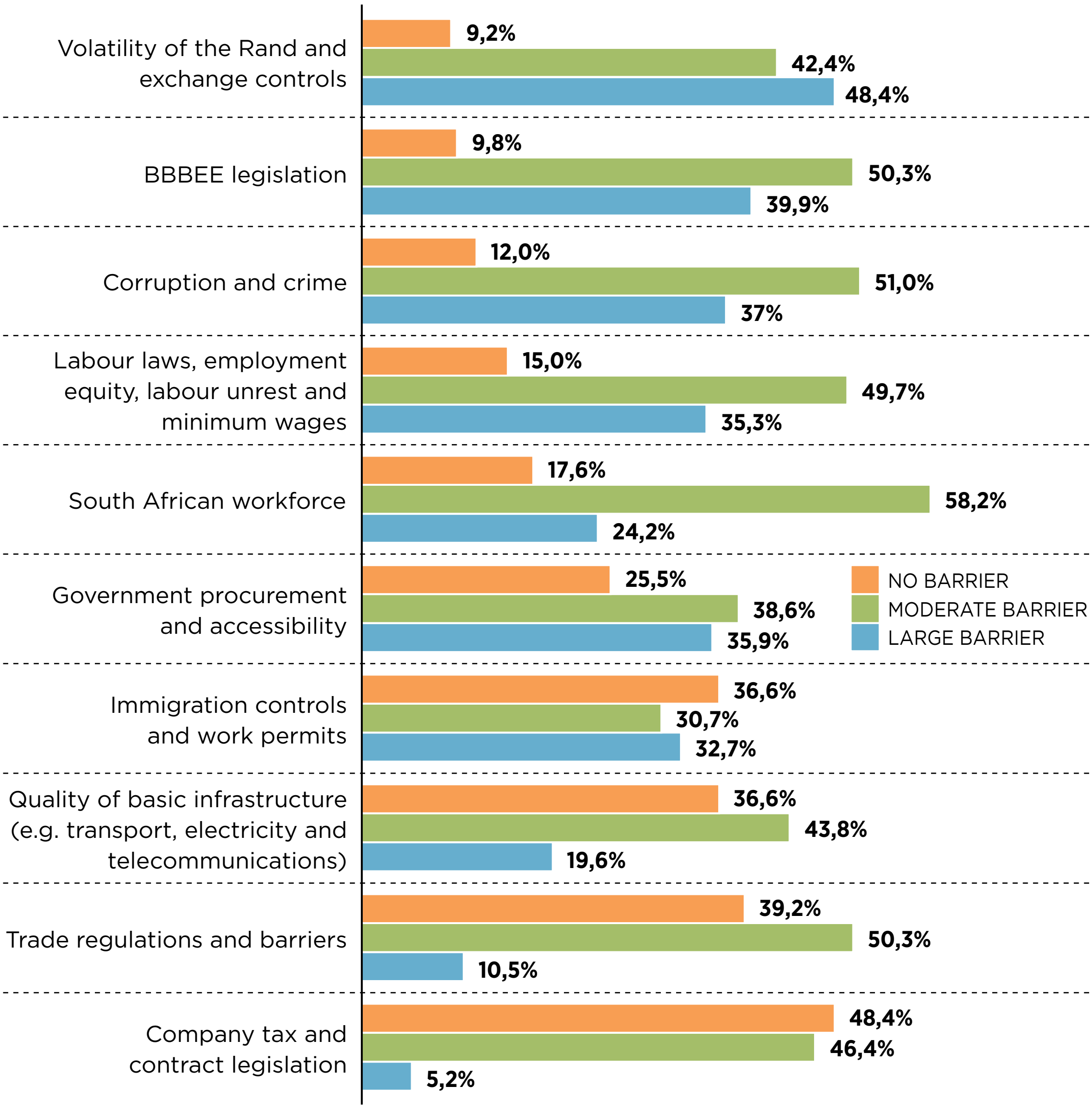


Figure 14 depicts the identified barriers, from those perceived as the largest to the smallest, taken from the firms' responses to the questionnaire. Taking moderate and large barriers together, more than 80 per cent of respondents experienced the following as the main barriers to conducting business in South Africa: the exchange rate of the Rand; concerns over BBBEE; corruption and crime; deteriorating labour relations; and poor labour skills. Immigration controls and work permits were identified as a large barrier by a third of respondents, whereas government procurement and accessibility, the quality of basic infrastructure, and trade regulations were experienced as specific barriers to doing business in South Africa by 60 per cent or more of the respondents. The questionnaire also gave respondents the opportunity to express their concerns over the main barriers to business; this is discussed in section 4.3.

As indicated earlier, these results are consistent with the outcomes of the 2012 *White Book*, where the South African workforce, BBBEE, government bureaucracy, corruption and the volatility of the Rand were mentioned as the most urgent barriers to business.

4.2 SEVERITY OF BARRIERS IN DETAIL

The companies were asked to give detailed explanations of where they identified barriers to conducting business in South Africa. We discuss these below.

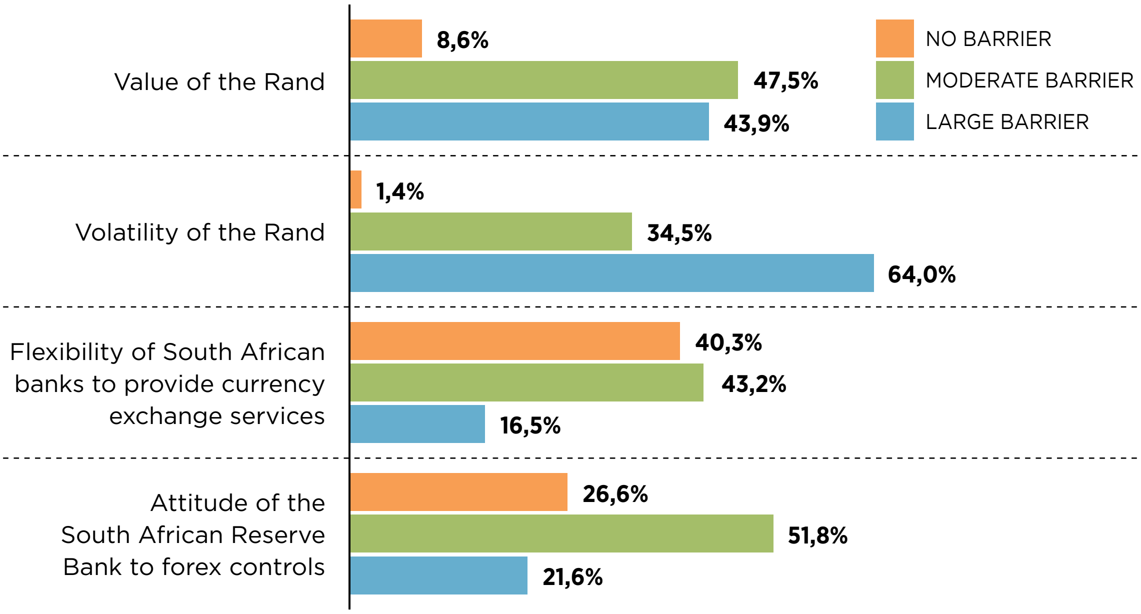
1. Currency problems.
2. Broad-Based Black Economic Empowerment.
3. Corruption and crime.
4. Labour relations and workforce.
5. Government procurement and accessibility.
6. Immigration controls and work permits.
7. Quality of basic infrastructure.
8. Trade regulations and barriers.
9. Regulation and taxation.

4.2.1 CURRENCY PROBLEMS

Figure 15 shows that the main barrier to conducting business in South Africa, as identified by respondents, is the value and volatility of the Rand, particularly volatility. Three quarters of respondents do not expect changes in the future, although one fifth thought things might get worse. Exchange controls and access to foreign currency were mainly perceived as moderate barriers.

In this context, more than 40 per cent of all respondents mentioned that the flexibility of South African banks to provide currency exchange services does not constitute a barrier to doing business in the South African economy. This finding is in line with the view reported in the 2012 *White Book*, namely that South Africa's well-developed financial system mitigates the challenges that the volatility of the Rand poses to EU-based companies.

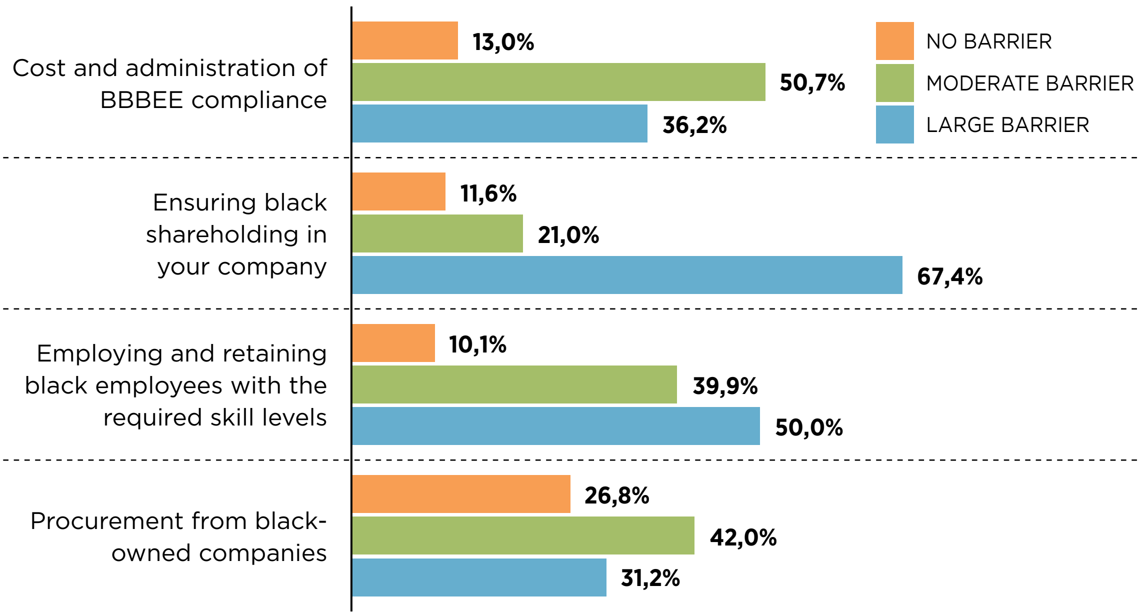
FIGURE 15 VOLATILITY OF THE RAND AND EXCHANGE CONTROLS



4.2.2 BROAD-BASED BLACK ECONOMIC EMPOWERMENT

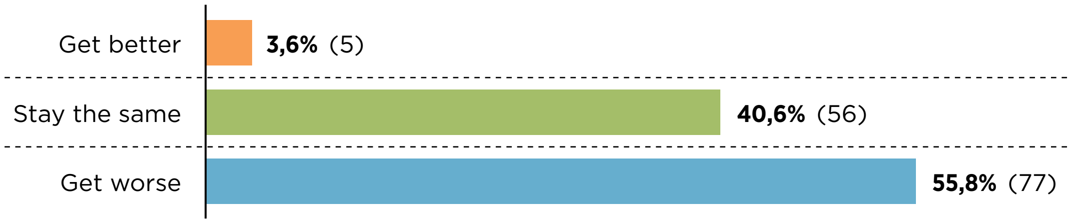
Approximately 80 per cent of respondents will be affected by BBBEE legislation, since the legislation will apply to companies with a turnover greater than R5 million (see Figure 6).

FIGURE 16 BROAD-BASED BLACK ECONOMIC EMPOWERMENT LEGISLATION



Of the various elements of this perceived barrier, Figure 16 shows that the least problematic of the barriers is clearly procurement from black-owned companies, although close to one third of the respondents considered it a large barrier. Since SMEs were the dominant stratum amongst the respondents, this is nonetheless a surprising finding, given the search costs involved in securing black-owned partners from which to source. Perhaps not surprisingly, yielding shareholdings to black partners was identified as the largest single barrier, and employing and retaining skilled black labour came second. The cost and administrative problems of compliance with BBBEE legislation, which was rated to be the most problematic dimension from the standpoint of EU-based companies in the 2012 *White Book*, also featured as a significant barrier in 2014.

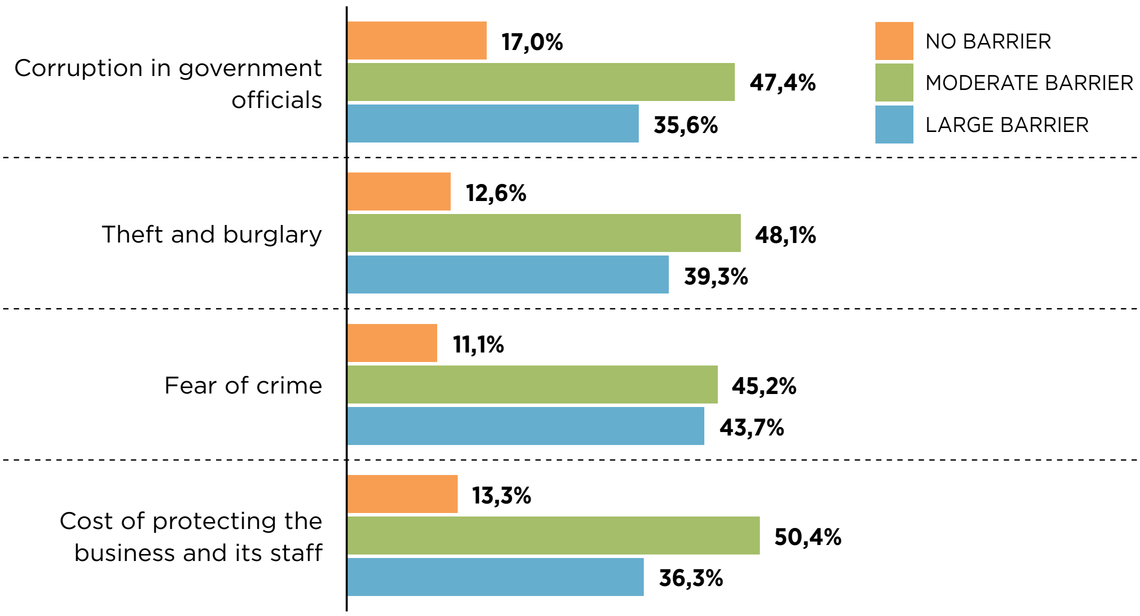
FIGURE 17 CHANGE EXPECTED IN BBBEE LEGISLATION IN THE NEXT 12 MONTHS



Furthermore, as Figure 17 shows, a majority of respondents consider that the BBBEE legislative environment will become more difficult in the next 12 months.

4.2.3 CORRUPTION AND CRIME

FIGURE 18 CORRUPTION AND CRIME

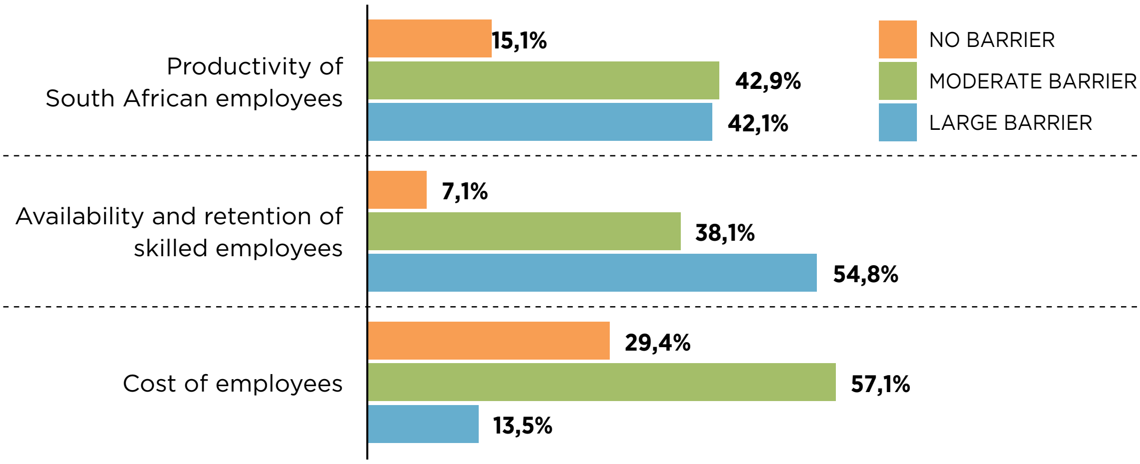


Corruption and crime both present problems for respondents. Figure 18 shows that less than 20 per cent of the respondents do not see problems at all; but more than 80 per cent regard corruption, theft and burglary, fear of crime, and the associated costs of protecting the business and staff as moderate to large barriers for business. Roughly two thirds of the respondents to this question do not expect changes, only six expect improvements, and 42 companies see deterioration in the future. This finding in principle is in line with the results in the 2012 *White Book*, in which the majority of respondents expressed the perception of a deteriorating government procurement climate and worsening corruption.

4.2.4 LABOUR RELATIONS AND WORKFORCE

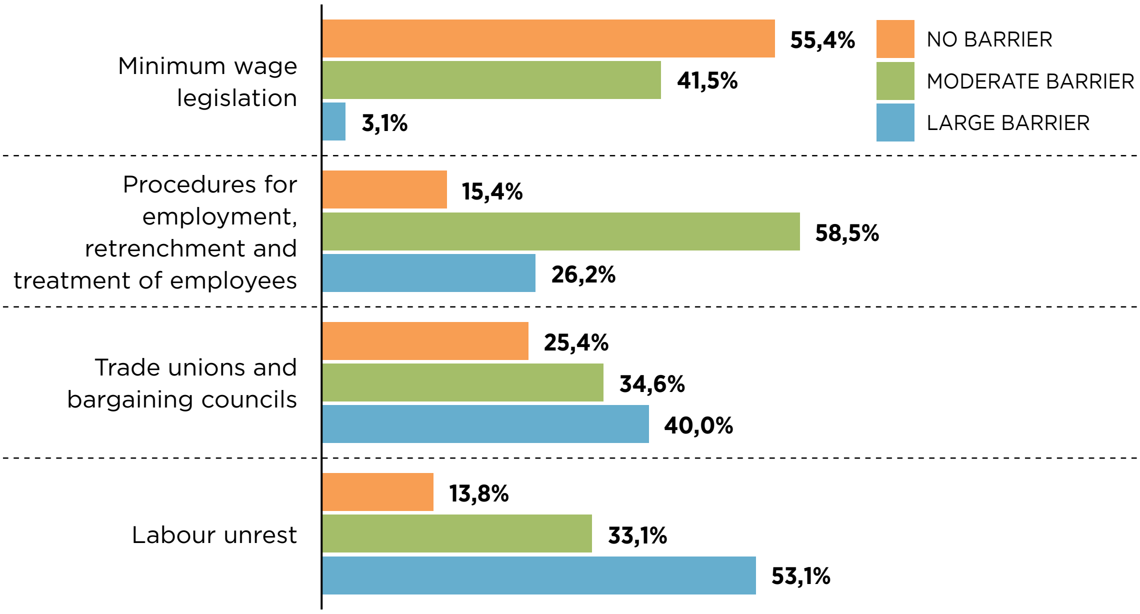
An interesting finding in light of the public debate on the subject is that cost of employees, while experienced by the majority of respondents as a moderate barrier, matters least of the three barriers measured (see Figure 19).

FIGURE 19 SOUTH AFRICAN WORKFORCE AS A BARRIER



This finding contradicts the assessment reported in the 2012 *White Book*, that EU-based companies then rated the increasingly high labour costs as a specific barrier to doing business in South Africa. In 2014 low productivity of workers was seen as more of a problem, with over 42 per cent of the companies regarding it as being a large barrier, and another 42 per cent as a moderate barrier. The biggest obstacle for respondents' business was the availability and retention of skilled labour. The majority of companies did not expect changes in the next year. Almost a third expected the situation to worsen rather than improve.

FIGURE 20 LABOUR RELATIONS AND LABOUR COSTS



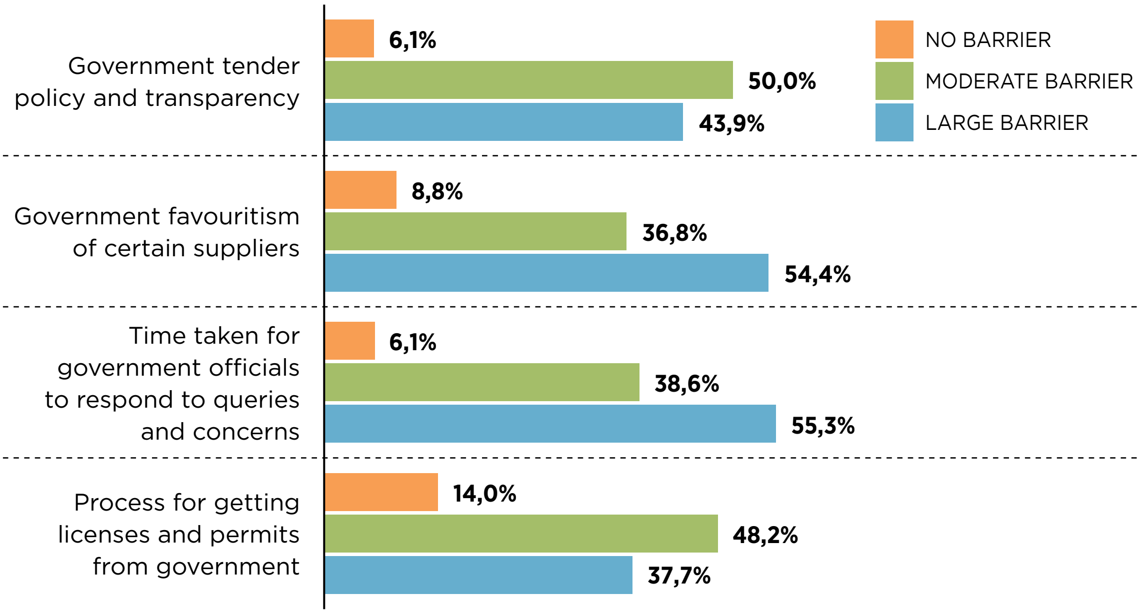
These results are in line with perceptions of labour relations. Figure 20 shows that minimum wage legislation was not perceived as a barrier to business by the majority of firms, although a substantial minority of 41 per cent saw it as a moderate barrier. However, procedures for employment, retrenchment and treatment of employees were regarded by a majority of respondents as being a moderate barrier, whereas trade unions, bargaining councils, and labour unrest were seen by more respondents as large barriers.

Furthermore, overall expectations for labour laws, employment equity, labour unrest, and minimum wages are somewhat pessimistic, with 41 per cent of respondents indicating these issues would deteriorate, albeit 52 per cent indicated they would stay the same.

4.2.5 GOVERNMENT PROCUREMENT AND ACCESSIBILITY

Similar to the evaluation of public procurement processes in the 2012 *White Book*, Figure 21 shows that those companies that registered difficulties with respect to government procurement were again concerned primarily with procedures.

FIGURE 21 GOVERNMENT PROCUREMENT AND ACCESSIBILITY AS BARRIERS



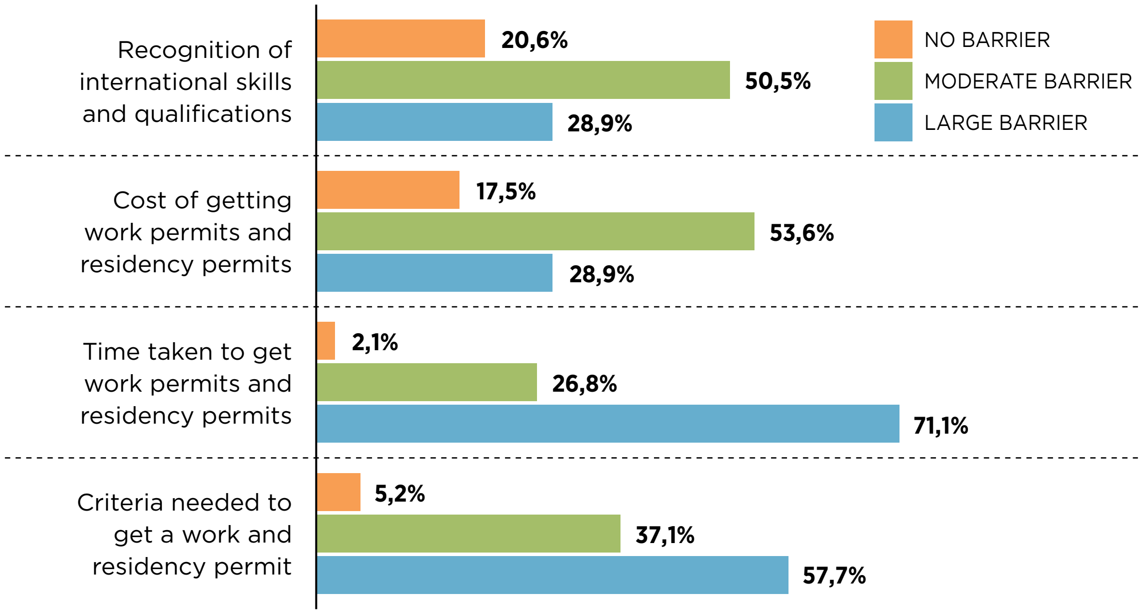
The time taken by government officials to respond was particularly problematic for these companies, as was favouritism towards certain suppliers in decisions of government officials. Government tender policy and transparency were also perceived as substantial barriers, whereas the processes for obtaining licenses and permits, while only fourth in terms of being large barriers, were nonetheless problematic for respondents. Again, two thirds of respondents did not expect changes, although 30 per cent were pessimistic.

4.2.6 IMMIGRATION CONTROLS AND WORK PERMITS

EU-based companies investing in South Africa often need to bring in skilled employees from their home country or other countries. This requires smooth handling of immigration and work permits.

Figure 22 shows that most respondents had some concerns about immigration procedures, an outlier being the time needed to get work and residence permits which over 70 per cent of respondents regarded as being a large barrier to conducting business. Close to 60 per cent regarded the criteria for obtaining these permits as a large barrier. Furthermore the expectations for the future were pessimistic. Almost half of the companies who answered this question (47 companies) expected a worsening situation, the same number did not expect changes, and only three were optimistic.

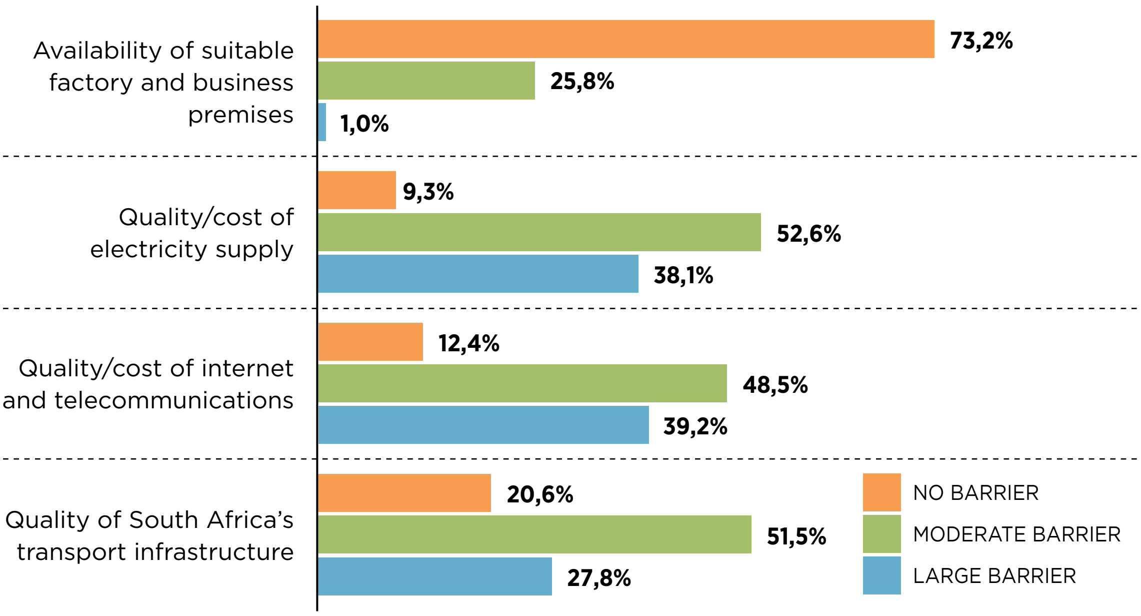
FIGURE 22 IMMIGRATION CONTROLS AND WORK PERMITS AS BARRIERS



4.2.7 QUALITY OF BASIC INFRASTRUCTURE

As has often been reported, infrastructure in South Africa has its deficiencies. Nevertheless, it is among the categories with the lowest number of complaints, as revealed in Figure 23.

FIGURE 23 QUALITY OF BASIC INFRASTRUCTURE AS A BARRIER

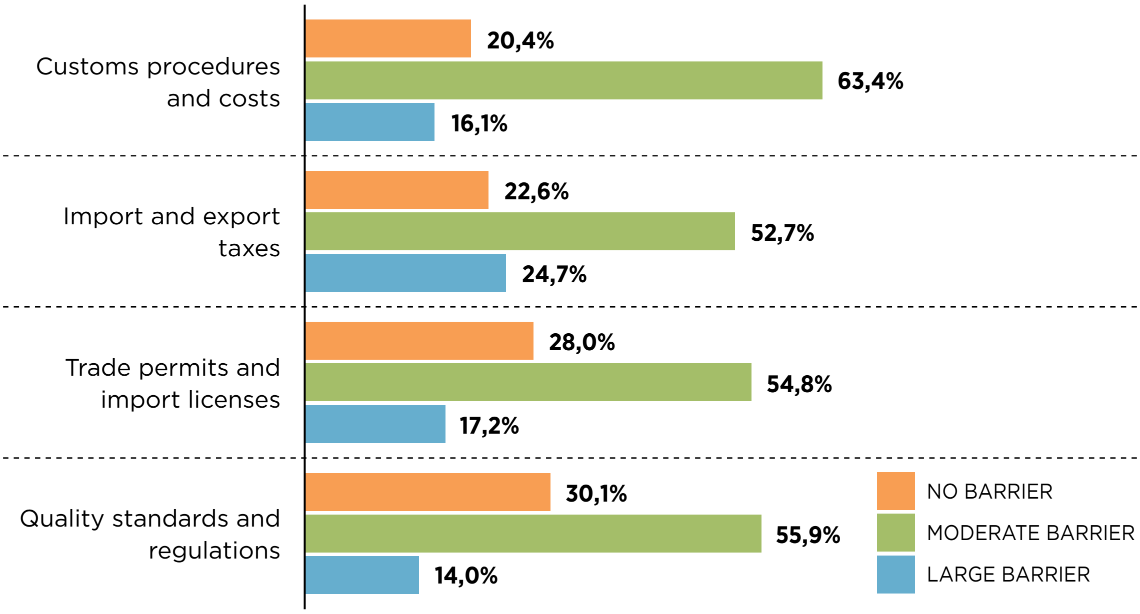


Two-thirds of the respondents to this particular question see barriers in the quality and cost of network services, of whom the majority were concerned about electricity and telecommunications, less so about transportation. By contrast, the availability of suitable business and factory premises was not seen as a barrier. A third of the respondents expected the overall quality of basic infrastructure to decline in the next 12 months, roughly twice as many as those expecting improvements, whereas more than half (50) did not expect changes.

4.2.8 TRADE REGULATIONS AND BARRIERS

Issues with respect to trade regulations were reported as the lowest ranked barrier to conducting business in South Africa in the 2012 *White Book*. In contrast to this view, Figure 24 shows that trade regulations and barriers, while not currently seen as constituting major barriers, do constitute moderate barriers.

FIGURE 24 TRADE REGULATIONS AS BARRIERS



Combining the moderate with the large barrier scores, each of the areas covered in the survey scores above 70 per cent, or slightly below in the case of quality standards and regulations. Furthermore, more than 90 per cent of respondents expected the situation to remain the same in the next year. Evidently there were not too many problems in this sphere, a good finding for a relatively open economy.

4.2.9 REGULATION AND TAXATION

The perception of bureaucratic and tax requirements was even less critical.

FIGURE 25 COMPANY TAX AND CONTRACT LEGISLATION AS BARRIERS

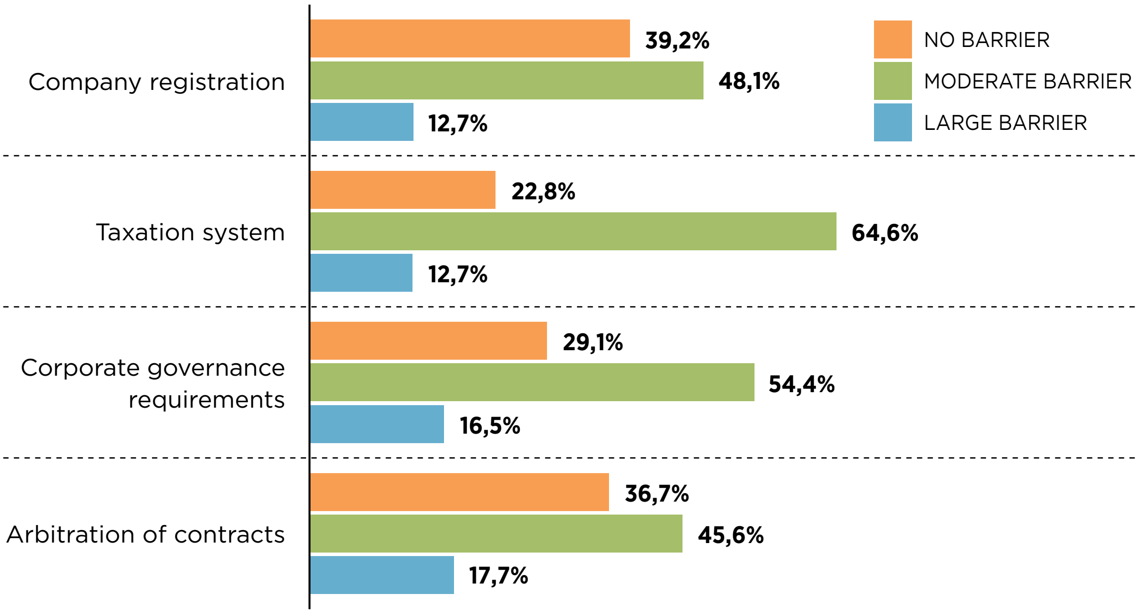


Figure 25 shows that most respondents saw some moderate barriers, but the 'no barrier' score outweighs the large barriers score by a substantial margin in each category. By the same token 87 per cent of respondents did not expect there to be changes in the next 12 months.

4.3 INSIGHTS FROM QUALITATIVE RESPONSES[7]

There are quite a few positive remarks, including good infrastructure, and references to well-educated staff, dynamic and entrepreneurial business partners, and resilient South Africans who are able to deal with apparent government disorder and underperformance. One respondent concluded, 'the potential is huge'.

7 Because the questionnaire gave respondents the opportunity to freely express their concerns over the main barriers to business, some comments reflected the current mood of the respondent and were not drafted very carefully, so they should not be accorded too much weight. Furthermore, in surveys of this kind aspects that are going well often pass unnoticed or are associated with the respondents' own success in business. As a consequence, positive assessments are generally underrepresented, while respondents dissatisfied with the present situation often have a greater inclination to reply to such questionnaires.

When it came to critical remarks, most responses related to perceptions of corruption, deteriorating labour relations, poor labour skills, and concerns over the BBBEE legislative environment. This outcome reflected the quantitative results of the questionnaire, as discussed earlier in this section, and indicated that these were serious concerns.

Strikes were mentioned as one of the major problems. One respondent wrote: ‘Strikes, strikes and more strikes’ as the main obstacle to doing business in South Africa. One respondent qualified this by noting that while the incidence of strikes was high, in international comparative perspective it was not the number of strikes per se that stood out, rather the violence associated with them. In addition, there was frequent mention of infrastructure problems such as energy shortages, and declining investment protection due to the South African government’s decision to terminate or not renew investment protection agreements with EU members in 2013. However, these comments were not reflected in the quantitative results.

Dissatisfaction with governmental entities was of great concern to some respondents. For example, one noted ‘a lack of real commitment from the South African government to promote small business and facilitate strong relations with global companies’.

Some answers highlighted the aforementioned frustration that firms had with regard to the present business climate in the South African economy: ‘Dealing with state owned companies has become more and more cumbersome over time; decision making processes are taking very long; preparedness to pay for services, and to pay on time, is very low’.

As for the future, fears such as the following were expressed: ‘Cancellation of Bilateral Investment Treaties, looming nationalisations including land expropriation proposals and general lack of clear direction of government’.

4.4 SUMMARY OBSERVATIONS

Overall, it is clear the EU respondent firms saw substantial obstacles to conducting business in South Africa, and their aggregate perception was that the situation would not improve in the next 12 months, and was more likely to deteriorate. In this aggregate picture, traditional areas of South African strength, notably tax and trade regulations, remained positive factors, while traditional areas of concern, picked up in the 2012 *White Book* and in many other surveys, remained problematic. Thus the familiar story of South Africa’s economic environment was confirmed in this survey: macroeconomic policies and outcomes were reasonably sound while microeconomic policies and regulations presented a mixed, and on the whole a deteriorating, picture.

Next we subject the aggregate data, as presented in this section, to some statistical tests in order to refine and deepen the analysis.

5 SUPPLEMENTARY INSIGHTS FROM STATISTICAL ANALYSIS

The preceding sections provided the results of the survey responses. Confining the analysis of survey responses only to general averaged values would imply that every responding EU-based company that raised a concern would contribute to the results to the same extent as each of the other respondents. However, the degree to which, for instance, specific barriers to doing business (see section 4) are regarded as impediments may vary widely across different types of EU-based companies. Accordingly, the following supplementary insights from statistical analysis indicate further systematic patterns in the survey responses, using the four general features that characterise the responding EU-based companies, as discussed in section 3: the **country of origin**, the **size of the company**, the **duration of activities** in South Africa, and the **main industry** of the responding companies. Thus the analysis helps to identify specific room for improvements to the business climate that different kinds of EU-based companies face in the South African economy.

5.1 METHODOLOGY

The statistical analysis employs six alternative variables as proxies for the four general features. These six variables represent key features that typify an EU-based company. The set of features is composed of the alternative variables of **share**, **size**, **turnover**, **years**, **sector**, and **income**. The choice of these variables pertains to the respondents' profiles regarding their commitment to the South African economy as indicated by their responses to the questionnaire (see section 3). Further technical details are provided in Annexure 8.1.

The present empirical analysis first constructs a new variable, **share**, to gauge the general feature **country of origin**. The resulting variable captures respondent companies that have either a relatively small or a relatively large market share compared to other respondent EU countries of origin in the sample, while the market share is simply calculated as the number of the respondent firms by country of origin relative to the total number of 153 respondents (i.e. the average relative market share). Here, large means equal to or greater than the average relative market share, while small is always less than the related average market share of an EU country of origin.

Regarding the **size of the company**, the second new variable, **size**, refers to the number of employees in a respondent company. In this respect, the present complementary study distinguishes between fewer than or equal to staff of 100 employees and more than 100 employees in a firm. In addition, the general feature **size of the company** is gauged by the third alternative variable, **turnover**, distinguishing between relatively low turnover of up to R15 million, medium turnover ranging from R15 million to R100 million, and relatively high turnover greater than R100 million.

This study also uses the fourth new variable, **years**, pertaining to the **duration of activities** in South Africa. This alternative variable distinguishes between respondent companies operating less than two years (short-term period), two to 10 years (medium-term period), or more than 10 years (long-term period) in the South African economy.

Regarding the **main industry** of the responding companies, the statistical analysis employs the fifth new variable, **sector**, capturing respondent companies that stem from the primary, secondary, or tertiary economic sector. In addition, the related sixth new variable, **income**, indicates whether the majority of a respondent company's income in South Africa is from counterparties in the business sector, or not.

Next we employ these six alternative variables to further examine the general survey results presented in sections 3 and 4, and to add further information on systematic patterns across answers to the questionnaire (see Annexure 8.2 for further technical explanations).

5.2 RESULTS

The subsequent reporting of supplementary insights from the statistical analysis refers to significant correlations between general survey answers and selected types of EU-based companies. This procedure ultimately allows for extending and validating insights from the overview of general results in sections 3 and 4. Most notably, the analysis helps to pinpoint policy recommendations for further improving the business climate for EU-based firms in South Africa (see section 7).

5.2.1 RESPONDENT FIRMS AND THE GENERAL BUSINESS CLIMATE IN SOUTH AFRICA

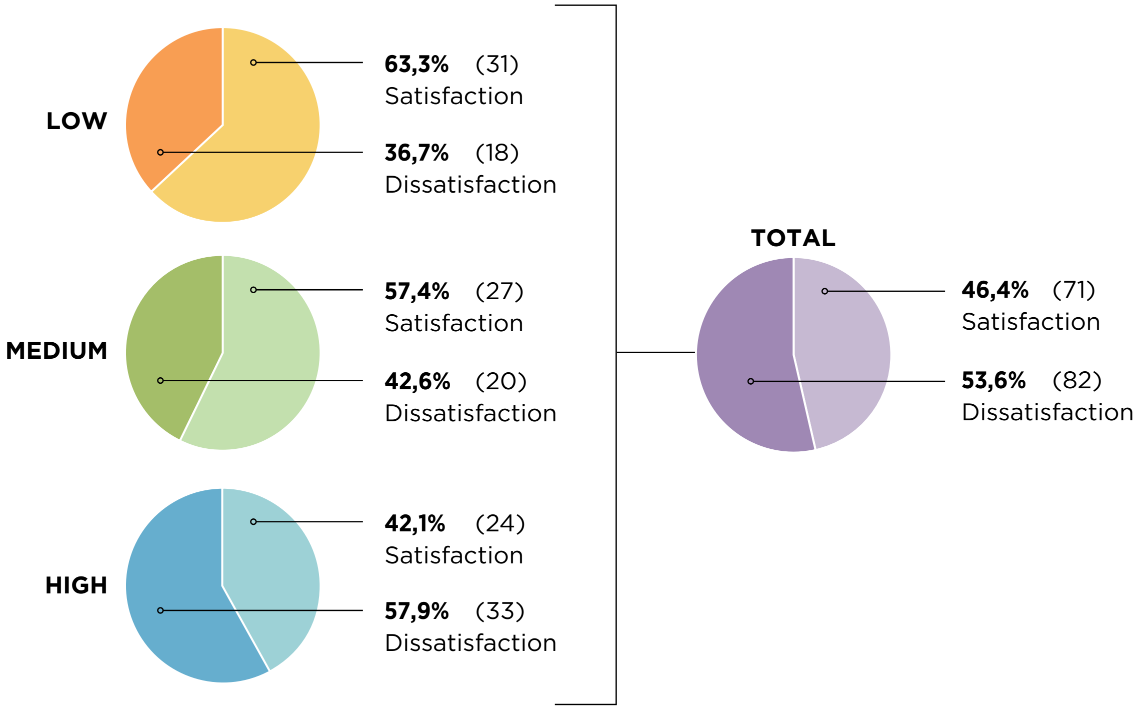
The perspectives on South Africa's business climate have already been portrayed in section 3. The present section analyses the perception of the business climate in South Africa in relation to the typology of respondent companies set out in section 5.1.

Regarding the duration of activities in South Africa, the more years a respondent company has been doing business in South Africa, the lower the probability that these firms are satisfied with the overall business climate in South Africa. Furthermore, there is evidence that the more years a respondent company has been conducting business in South Africa, the higher the probability that such firms are dissatisfied with the current business climate in South Africa compared to 12 months ago. Finally, the more years a respondent company has been doing business in South Africa, the higher the probability that such company expects the business climate to deteriorate.

In light of these findings, it could be argued that the likelihood of dissatisfaction with a relatively poor – and in the opinion of many respondents – deteriorating business climate increases with the length of time such firms have been operating in the South African economy.

The size of business also affects firms' assessment of the South African business climate. In particular, the statistical analysis shows that the higher an EU-based company's turnover is, the lower the probability that these firms are satisfied with the overall South African business climate.

FIGURE 26 ASSESSMENT OF CURRENT BUSINESS CLIMATE BY TURNOVER



In more detail, it can be seen that while 31 firms representing about 63,3 per cent of EU-based companies with a low turnover (up to R15 million) are satisfied with the current business climate in South Africa, the majority of firms with a high turnover greater than R100 million (i.e. 33 firms or 57,9 per cent of all EU-based companies with a high turnover) are dissatisfied with the current business climate. Larger firms are either less satisfied or more willing to express their dissatisfaction.

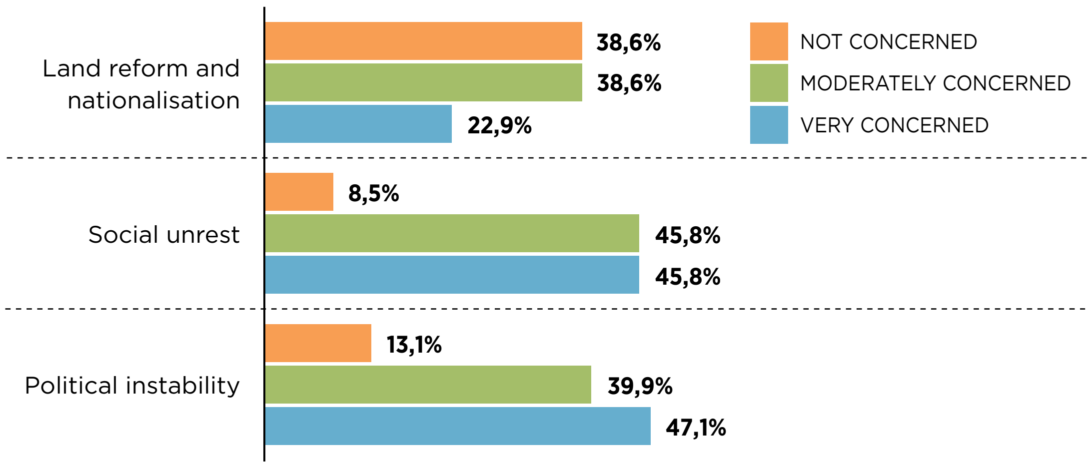
The statistical analysis indicates that the probability of a firm expecting the business climate in South Africa to get better increases if the respondent company's country of origin has a relatively large share in the sample, except when the main industry of the responding companies represents the primary sector of the South African economy.

To summarise, large respondent companies with high turnovers that have been operating for a considerable time in South Africa are relatively pessimistic concerning the possibility for the South African business climate to improve. However, being part of a discernible community of nation-specific respondent companies counteracts such assessments of both the present and the expected business climate in South Africa, whereby those from EU countries with a larger market presence, except in the primary sector, are relatively more optimistic. Overall, however, and as noted in section 3 (see Figure 10), respondent companies are more dissatisfied than satisfied with the South African business climate.

5.2.2 BARRIERS AND THREATS TO DOING BUSINESS

The ranking and discussion of barriers to conducting business in the South African economy was presented in section 4. The statistical analysis examines whether all, or only particular types, of EU-based companies are concerned with these barriers and, in addition, we also consider the threats to doing business in the South Africa economy as identified in the questionnaire.

FIGURE 27 DEGREE OF CONCERN ABOUT THREATS TO DOING BUSINESS IN SOUTH AFRICA



The general survey results portend that threats related to both social unrest and political instability affect all EU-based companies regardless of the general features characterising such firms (see Figure 27). However, the statistical analysis results indicate that the threat of land reform and nationalisation is of greatest concern, in particular to the main industry of the responding companies represented by the primary sector.

The statistical analysis also shows that the first five ranked categories of barriers to doing business, as reported in section 4, affect all types of EU-based companies to the same extent. This validates the findings that the volatility of the Rand and exchange controls, concerns over

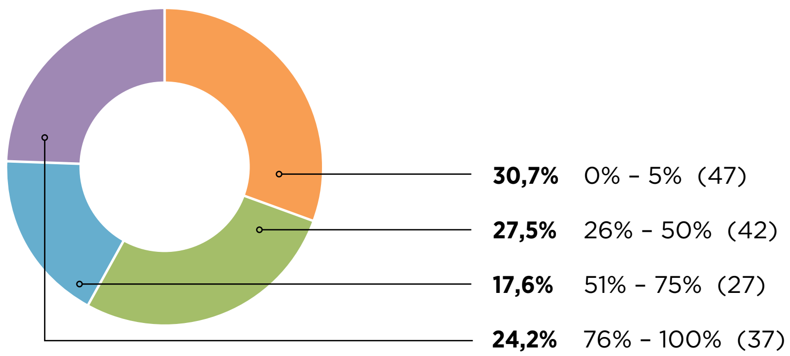
BBBEE, corruption and crime, deteriorating labour relations, and poor labour skills are either moderate, or large barriers to conducting business, from the viewpoint of any type of EU-based company. In addition, the statistical analysis indicates that issues related to government procurement and accessibility are experienced as barriers to doing business in South Africa if the EU-based company stems from the secondary sector. The secondary sector is also particularly concerned with trade regulation and barriers. Not surprisingly, these issues also significantly correlate with the years an EU-based company has been doing business in South Africa. By the same token, the related general feature duration of activities also increases the probability that the quality of basic infrastructure has been experienced as a barrier to doing business in South Africa.

To summarise, threats related to social unrest and political instability, as well as numerous barriers to doing business in South Africa, are of general and great concern to any EU-based company. According to our estimates, the findings can be interpreted as the main reasons for the EU-based companies' dissatisfaction with the business climate in South Africa. Although there most probably is a bias in terms of overrepresented dissatisfaction, there is robust information regarding the issues that are of greater concern to all, or to selected EU-based companies in the South African economy. This evidence bears important lessons for policymaking in South Africa.

5.2.3 LABOUR RELATIONS

In this section, the statistical analysis considers labour relations between the EU-based companies and their workforce. The corresponding general results of the survey are presented in Figure 28; it is evident that respondent companies were engaged in training to varying degrees, although just less than one third of the companies did not appear to provide much training.

FIGURE 28 PROVIDING SKILLS TRAINING TO THE SOUTH AFRICAN WORKFORCE OVER THE PREVIOUS 12 MONTHS



The statistical analysis shows that the probability of having provided the firm's South African workforce with skills training during the previous 12 months increased if the EU-based company's country of origin had a relatively large market share in the South African economy, compared to other EU-based companies' countries of origin. In addition, the years an EU-based company had been doing business in South Africa and the turnover of such companies positively correlated with the probability of having provided an increasing share of the firm's South African workforce with skills training during the previous 12 months. At the same time, however, the statistical analysis also demonstrates that the probability of having provided a greater share of the company's South African workforce with skills training during the previous 12 months decreased if the EU-based company was from the secondary sector, while this probability increased in the case of the tertiary sector.

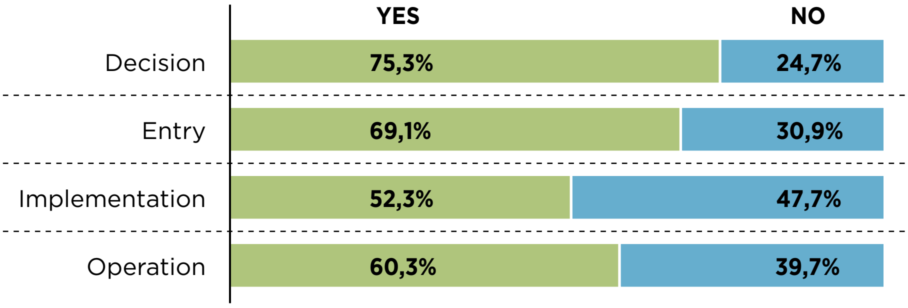
These results are intuitively plausible. Longer duration of activities in South Africa and greater size of company – as also hallmarked by the market share gauging an EU-based company's country of origin – tended to increase investment into human capital, everything else being equal. The stakes for firms that were well-established rose and labour relations intensified. In particular, the skills needed by EU-based companies operating in South Africa were not high in the secondary sector, while the tertiary sector contributed considerably to skills training. In line with these findings, one may argue that newly established EU-based SMEs in South Africa tend, to a relatively lesser extent, to contribute to skills training of the South African workforce.

5.2.4 SUPPORT IN ESTABLISHING THE OPERATION

According to the general survey, about 83 per cent of all EU-based companies said they had assisted other South African businesses. The question arises as to which types of EU-based companies tend to contribute most to the probability of providing support to other South African firms. It may well be assumed that European firms can provide support either directly or via indirect spillovers. In particular, the statistical analysis indicates that the probability of having provided support to other South African businesses increased if the EU-based company's country of origin had a relatively large market share in the South African economy (i.e. compared to other EU countries) and if the EU-based company was of large size (i.e. the number of employees was greater than 100).

We proceed by analysing the support that EU-based firms received from South African based organisations. Each form of support that an EU-based company may have received at different stages of its investment cycle (decision stage, entry stage, implementation stage, and operation stage), is correlated with the typology characterising EU-based companies as described in section 5.1.

FIGURE 29 SUPPORT FROM SOUTH AFRICAN BASED ORGANISATIONS DURING THE INVESTMENT CYCLE



In general, the survey results indicate that EU-based companies received support at all stages, with an emphasis on early stages of the investment cycle (see Figure 29).

Regarding the decision stage, support in the form of information on procedures and regulations for doing business in South Africa were frequently mentioned, as well as corporate taxation procedures and incentives. EU-based companies also reported if they received support in facilitating company registration, permits, and licenses, as well as being introduced to legal, accounting and other professional services. These firms also frequently mentioned finding key staff and suitable sites as specific forms of support received during the implementation stage. Finally, at the operational stage, EU-based companies received information on finance and complaint resolution issues. Regarding the statistical analysis, the specific finding was that the probability of receiving support at the entry stage increased if the customer group providing the EU-based company with the majority of its income in South Africa was from business in contrast to non-business or residual income. In addition, it would appear that the marginal probability of receiving support at the implementation as well as at the operational stage was positively correlated with an EU-based company's turnover.

Apparently, South African based organisations supported EU-based firms that invested in South Africa. There was seemingly a bias in granting support to EU-based companies, which mainly pertained to the size of company and its income share generated in South Africa. This did not automatically imply a bias by the South African government towards size. By contrast, these correlations may well indicate a reverse causality, namely that more support at the implementation or operational stage helped to generate higher turnover. This consideration gets support from the notion that there was no evidence of significant correlations between support at various stages of the investment cycle and size, this time referring to the number of employees in an EU-based company. In any case, the South African government is currently willing to support foreign business and their investment, although this may change once the Promotion and Protection of Investment Bill is enacted.

5.3 SUMMARY OBSERVATIONS

Regarding the **country of origin**, it could be surmised that companies with a parent enterprise in an EU member country that has relatively large physical footprints in the South African economy might feel more confident than companies from EU countries which have a smaller investment in South Africa. They may believe that their government is better placed to influence the South African government to address their business problems, which we call the 'community effect'. Our statistical analysis can neither confirm nor reject this proposition, although it does show that firms from EU member countries with a relatively large market share in the South African economy are more active with regard to investment into both skills and assistance to South African businesses.

Concerning the **size of the business**, in general it might have been expected that it is easier for large firms to deal with regulatory complexity than it is for small firms. In fact, the opposite seems to have been the case; larger firms seemed to be more dissatisfied with the South African business environment than smaller ones. One explanation may lie in the fact that there was no match in aspects of either staff or of turnover. The majority of EU-based firms did not employ many workers, but the majority of firms were at the upper end of the financial turnover scale. Another explanation could be that larger firms, having presumably worked to establish their market presence, were correspondingly more disappointed that the business environment did not match their level of effort in developing the market. Smaller firms, presumably also correlated with relative newness in the market, having recently taken the decision to invest, did so in a context of global financial crisis and as such may have lowered their expectations.

As for the **duration of activities** in South Africa, one may assume that the companies had developed little by little some sort of resilience towards unique South African problems, and accordingly would set their expectations lower. Interestingly, our statistical analysis also revealed the opposite, namely that the longer-established companies were more pessimistic than new entrants. From a policy point of view this suggests that in order to positively sway expectations of the foreign investor community, the South African government could interact more strategically with those that have been long-established in the country.

We earlier expressed the hypothesis that the **main industry** of the responding companies may shed some light on their economic situation. Firms in thriving sectors might perceive the business environment more optimistically than those in declining industries. There is no evidence for this statement; dissatisfaction seems to be widespread and not concentrated in any particular industries.

6 THE BROADER CONTEXT

In order for us to draw relevant conclusions that South African policy makers would find useful, the detailed analysis reported in the previous sections is best viewed through a wider, comparative lens rather than on its own terms. Accordingly, here we consider how South Africa is doing, relative to selected emerging market peers, in respect of several key indicators pertinent to the characteristics of the survey sample group, as measured in widely available, respected international reports. Specifically, we consider issues pertaining to SME regulation and development sourced from the World Bank's *Doing Business 2014* report, and the competitiveness of micro and macroeconomic policies as revealed in the World Economic Forum's *Global Competitiveness Index 2014–15*.

Countries included for comparison, and the high-level rationale for their selection, are South Africa, Kenya, Nigeria (representing regional African gateways), Brazil, Russia, India and China (South Africa's BRIC peers), Mexico, Turkey, and Indonesia (also regional developing country gateways and G20[8] members along with South Africa). While these comparisons offer some insight, it has to be kept in mind that of the countries used for comparison only China and Indonesia are in the same stage of development as South Africa, according to the GCI. This is recognised in the *Doing Business 2014* report, and to normalise results certain indicators are weighted according to the country's development stage, which distorts absolute aggregate rankings.

Simply looking at the index rankings and comparing all the selected states it becomes clear that South Africa, on aggregate, is reasonably competitive and the most business friendly. South Africa ranked 56th of 144 countries, as measured in the *Global Competitiveness Report 2014–2015*, and 41st of 189 countries, as measured in the 2014 *Doing Business* report. However, put into a longer time frame, South Africa has steadily been slipping in both rankings. The highest rank achieved in the past five *Doing Business* reports was in 2010 and 2011, ranking 34th out of 183 countries, and the highest GCI rank in 2011, ranked 50th out of 142 countries. This indicates that the South African business climate had been deteriorating well before the first EU business climate survey in 2012, using the given indicators. Of the selected comparator states, the only ones that beat South Africa in the GCI were China, Russia, Turkey and Indonesia, while South Africa ranked 12 places higher than the second best performer, Mexico, in the *Doing Business 2014* report.

8 The members of the G20 are Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, the Republic of Korea, Mexico, Russia, Saudi Arabia, South Africa, Turkey, the United Kingdom, the United States and the European Union. The G20 group represents about two-thirds of the world's population, 85 per cent of global gross domestic product and over 75 per cent of global trade. Its heads of state meet annually to discuss economic co-ordination.

Looking past the aggregate rankings, one can compare South Africa and the select group of countries on certain perceived barriers to doing business in South Africa, as identified in sections 4 and 5 of the survey, that overlap with the GCI and *Doing Business 2014* reports.

The largest perceived barrier to conducting business in South Africa is the volatility of the Rand and exchange controls, which are not measured in the GCI or *Doing Business 2014* reports; however, in the GCI, respondents did list this as the 11th most problematic factor for doing business in South Africa. This relative lack of priority is interesting in light of our survey results as it seems to indicate a substantial divergence of opinion amongst the two sample groups. The source of this difference could reside, for instance, in the country origins of our survey – perhaps the combination of Euro uncertainty and Rand uncertainty was particularly acute this year – or in timing factors associated with the two surveys.

Of the 10 barriers to doing business in South Africa, three could be categorised under labour market efficiency. BBBEE legislation, the second highest reported barrier, is not measured in either the GCI or *Doing Business 2014* reports, but the efficiency of the labour market is. This includes the South African workforce (productivity, availability of skilled labour and labour cost), and the South African labour market (labour laws, employment equity, labour unrest and minimum wages). Thus relevant comparisons can be made using sub-category indicators from the GCI as shown in Figure 30.

FIGURE 30 GCI 2014 RANKING ON WORKFORCE AND LABOUR MARKET EFFICIENCY

	Labour market efficiency	Pay and productivity	Flexibility of wage determination	Hiring and firing practices	Quality of the education system	Country capacity to retain talent	Extent of staff training
South Africa	113	136	139	143	140	50	**18**
Kenya	**25**	56	69	17	**30**	47	34
Nigeria	40	51	35	**7**	122	92	48
Brazil	109	117	125	135	126	44	44
India	112	69	113	47	45	42	77
China	37	**15**	84	15	52	**31**	46
Russia	45	24	**28**	41	84	103	89
Mexico	121	87	88	103	123	63	74
Turkey	131	81	49	67	89	86	91
Indonesia	110	30	114	32	32	32	24

Bold numbers indicate best performer.
Yellow indicates an increase in ranking, blue a decrease, and green no movement.

Source: Global Competitiveness Index, *Global Competitiveness Report 2014–2015*, World Economic Forum, Geneva, 2014.

EU-based companies' concern over the South African workforce and labour market are clearly not unfounded as South Africa is out ranked in all sub-indicators on labour market efficiency, although South Africa's capacity to retain talent and train staff are two valuable and redeeming qualities.

In our survey, crime and corruption was found to be the third biggest barrier to conducting business in South Africa. The *Doing Business 2014* report does not include crime or corruption, whereas the GCI reports on the perceived frequency of diversion of public funds to companies, individuals, or groups due to corruption, irregular payments and bribes, and the business cost of crime and violence. Closely linked to these indicators are the GCI's indicators for favouritism in decisions of government officials and the burden of government regulations. These, to a comparable degree, cover the concern of government procurement and accessibility, the sixth biggest barrier to conducting business in South Africa. These indicators are shown in Figure 31.

FIGURE 31 GCI 2014 RANKING ON CRIME, CORRUPTION, GOVERNMENT PROCUREMENT AND ACCESSIBILITY

	Diversion of public funds	Irregular payments and bribes	Favouritism in decisions of government officials	Burden of government regulation	Business costs of crime and violence
South Africa	96	**48**	104	120	133
Kenya	83	108	75	48	129
Nigeria	142	135	126	99	130
Brazil	135	89	108	143	124
India	60	93	49	59	98
China	**45**	66	**22**	**19**	**52**
Russia	102	102	87	111	70
Mexico	119	99	99	118	135
Turkey	74	54	59	71	67
Indonesia	63	87	33	23	80

Bold numbers indicate best performer.
Yellow indicates an increase in ranking, blue a decrease, and green no movement.

Source: Global Competitiveness Index, *Global Competitiveness Report 2014–2015*, World Economic Forum, Geneva, 2014.

Looking at the select indicators for corruption and crime, and government procurement and accessibility, EU-based companies' concerns would appear to be validated as South Africa ranks in the bottom three in favouritism in decisions of government officials, burden of government regulation and cost of crime and violence to business. South Africa sits in the middle of the select group in the ‘diversion of public funds’ indicator. However, in the ‘irregular payments and bribes’ sector, South Africa fares far better than its competitors. Perhaps some of these results should be interpreted with caution, since the GCI is based on perceptions. In this regard it is difficult to credit India’s good score for ‘burden of government regulation’, relative to the others in the group, particularly South Africa, and especially in relation to South Africa’s relatively sound *Doing Business 2014* scores.

Quality of basic infrastructure, the eighth highest concern for doing business in South Africa, is extensively covered in the GCI and, to a lesser extent, in the *Doing Business 2014* report. South Africa is ranked 150th of 188 countries in the *Doing Business 2014* report for the number of procedures, and the time and cost it takes to get electricity. The GCI also ranks both quality and cost of electricity supply and access to the Internet, as well as the quality of South Africa’s transport infrastructure. These results are shown in Figure 32.

FIGURE 32 GCI RANKING ON QUALITY OF BASIC INFRASTRUCTURE

	Quality of overall infrastructure	Quality of electricity supply	Fixed broadband Internet subscriptions/ 100 pop.	International Internet bandwidth, kb/s per user	Mobile broadband subscriptions/ 100 pop.
South Africa	59	99	89	126	74
Kenya	65	95	124	53	115
Nigeria	133	141	140	141	96
Brazil	120	89	63	60	39
India	90	103	103	107	114
China	64	**56**	51	120	78
Russia	74	73	**43**	61	**29**
Mexico	69	80	60	79	104
Turkey	**33**	72	59	**40**	62
Indonesia	72	84	101	100	65

Bold numbers indicate best performer.
Yellow indicates an increase in ranking, blue a decrease, and green no movement.

Source: Global Competitiveness Index, *Global Competitiveness Report 2014–2015*, World Economic Forum, Geneva, 2014.

The quality of overall infrastructure is one of South Africa’s highest ranking indicators. However, EU-based companies’ perceptions of quality of basic infrastructure being a barrier to doing business are justified as South Africa compares poorly to the select group in all sub-indicators or falls into the bottom group, with a large margin between the top and bottom groups.

Trade regulations and barriers, the ninth biggest concern for doing business in South Africa, and Company, Tax and Contract Legislation, the 10th biggest concern, are also covered in the GCI and *Doing Business 2014* reports (see Figure 33). The *Doing Business 2014* report comprehensively covers concerns of company, tax and contract legislation (starting a business, paying taxes and enforcing contracts), while the GCI sufficiently addresses concerns on trade regulation and barriers in the sub-indices on goods market efficiency (prevalence of trade barriers, trade tariffs, and burden of customs procedures).

FIGURE 33 GCI/DOING BUSINESS RANKING ON TRADE REGULATIONS AND BARRIERS, AND ON COMPANY, TAX AND CONTRACT LEGISLATION

	Prevalence of trade barriers	Trade tariffs, % duty	Burden of customs procedures	Trading across borders	Starting a business	Paying taxes	Enforcing contracts
South Africa	**23**	76	62	106	64	**24**	80
Kenya	110	98	92	156	134	166	151
Nigeria	42	119	132	158	122	170	136
Brazil	115	118	138	124	123	159	121
India	100	124	75	132	179	158	186
China	54	115	**55**	74	158	120	19
Russia	111	102	95	157	88	56	**10**
Mexico	70	92	70	59	**48**	118	71
Turkey	77	69	83	86	93	71	38
Indonesia	103	**64**	68	**54**	175	137	147

Bold numbers indicate best performer.
Yellow indicates an increase in ranking, blue a decrease, and green no movement.

Source: Global Competitiveness Index, *Global Competitiveness Report 2014–2015*, World Economic Forum, Geneva, 2014.

While respondents may have felt that trade regulations and barriers were a hindrance to doing business in South Africa, the comparisons indicate that South Africa was a relatively favourable country in terms of trade regulations and barriers, ranking highest among competitors in prevalence of trade barriers and in the top three in trade tariffs and burden of customs procedures. The same was true for company, tax and contract legislation, where South Africa consistently ranked in the top five of all indicators in the focus group and ranking first, with a wide margin, in the *Doing Business 2014* paying taxes indicator (see Figure 33).

7 CONCLUSIONS

The present questionnaire is the second attempt to get an impression of the perceptions of EU-based companies about the general business climate in South Africa, as well as perceived specific threats and barriers to doing business in the country. It provides some continuity with the first survey, although the comparison is limited by the latter having used a different form of interview (written instead of personal). The written survey allows for a more detailed analysis, which we conducted in section 5 of the present survey.

As reflected in the preceding sections there are many interesting insights and nuances arising from the results – too many to recap here. Nonetheless, we would highlight five key conclusions.

First, despite some critical views and a somewhat pessimistic outlook for the next 12 months, the majority of companies surveyed recommended doing business in South Africa. This matches the generally favourable perception of South Africa as a business location as expressed in two key international surveys (see section 6): South Africa is in many respects still an attractive investment location, particularly relative to its emerging market peers.

Second, the general business climate is perceived as mixed, as section 3 shows; and compared to the *White Book* 2012 results, the situation seems to have deteriorated substantially. This picture fits with the general decline shown in the country's aggregate rankings in the two international benchmarking surveys discussed in section 6. This picture of steady slippage seems contrary to the South African government's intention to attract foreign direct investment (FDI) in order to grow the economy, create jobs, and reduce inequalities.

Third, one striking result, namely the elevation of concerns over political risk to the top of this survey pool's list, merits particular attention. When perceptions of political risk rise, investors look for commensurately higher returns. However, it is abundantly evident that the South African economy is growing well below potential, so that the risk–reward matrix is becoming less unfavourable. Given the relatively high growth rates evident in sub-Saharan Africa, and correspondingly high returns, the combination of higher risk and lower rewards in South Africa signals potentially declining FDI inflows in the years ahead if left unchecked.

Fourth, EU-based companies see a number of institutional issues and microeconomic policy measures (as identified in section 4), that are perceived as threats and barriers. This becomes more obvious when reading the personal statements of the respondents, a selection of which is given in section 4.3. These creeping problems, left unchecked, disincentivise investors and compound the negative drift in the general business environment.

Finally, there is consistency between the responses to this questionnaire and the international surveys, and a strong continuity over time regarding the main threats and barriers to doing business in South Africa, as the comparisons between the 2012 *White Book* and this report reveal. The respective main barriers to business are similar (in a slightly changed order) in the reports. Consequently, the issues the South African government needs to deal with in order to allay the growing concerns of all investors, not just Europeans, are clear.

8 ANNEXURES

8.1 INPUT FOR CALCULATING CROSS-CORRELATIONS: REFINEMENTS OF RESPONDENTS' CHARACTERISTICS

The calculations of cross-correlations help to re-examine the validity of the general and summarising results of the survey responses. In particular, the corresponding statistical analysis establishes a set of six alternative variables. The statistical analysis employs these variables to gauge four general features of EU-based companies comprising: the **country of origin**, the **size of company**, the **duration of activities** in South Africa, and the **main industry** of the respondent companies (see section 3). In addition, the low number of respondents amounting to a total number of 153 EU-based companies requires aggregation of data for technical reasons.

SHARE

The variable **share** is a new binomial variable representing EU-based companies of a specific country of origin in the EU base. The new variable is assembled from respondents' answers to question 9 of the questionnaire. The outcomes indicate either a relatively large or a relatively small market share compared to the average market share of an EU country of origin conducting business in the South African economy. Here, the average market share is simply the ratio of the number of EU-based companies with identical country of origin and the total number of respondent firms. As a consequence, large means equal to or greater than the average market share, while small is always less than the average market share.

SIZE

The new variable **size** refers to the number of permanent employees in the respondent EU-based companies. The original eight possible answers in question 18 of the questionnaire are collapsed into a binomial variable indicating whether or not the number of employees is greater than 100.

TURNOVER

The new variable **turnover** depicts EU-based companies with a low, medium, or high economic turnover. The original six possible answers in question 20 of the questionnaire are aggregated, meaning that a low turnover amounts to less than R15 million, a medium turnover is in a range between R15 million and R100 million, while a high turnover starts at a level of +R100 million. As a consequence, the new ordinal variable has only three outcomes.

YEARS

The variable **years** refers to the time period respondent EU-based companies have been doing business in the South African economy. The new ordinal variable is composed of three values representing the period of operation in the South African economy: a short-term period (i.e. less than two years), a medium-term period (i.e. a range between two and 10 years), and a long-term period (i.e. more than 10 years). As a consequence, the original six possible answers to question 10 of the questionnaire are collapsed into three ordinal categories.

SECTOR

The variable sector draws on the respondents' answers to the 10 possible categories in question 16 of the questionnaire. The new nominal variable sector is divided by the **primary sector** comprising the answers 01–02, the **secondary sector** merging the answers 03–05, and the **tertiary sector** composed of the remaining answers 06–10.

INCOME

The new variable **income** indicates whether the customer group providing an EU-based company with the majority of its income in South Africa (see question 17 of the questionnaire) is from business or not. As a consequence, the original five possible answers are merged into one binomial variable. Here, 112 EU-based companies receive the majority of their income from other South African businesses, while 41 firms mainly rely on income from other sources.

8.2 CLUSTERING ANSWERS TO SELECTED KEY QUESTIONS OF THE SURVEY

This procedure mainly aims at detecting additional information on the question, whether specific types of EU-based companies gauged by alternative variables (see section 8.1) contributed relatively more than other firms to the assessment of the business climate in South Africa as depicted in the general and summarising survey results. The approach is explained per question below, in the question numbering sequence.

Question 22: 'When setting up or developing the business in South Africa, did you get support from a South African based organisation on anyone of these topics?'

There are 18 possible answers to this specific question in the questionnaire. The empirical analysis only employs four binomial variables with regard to *decision* (comprising the original answers 01–06), *entry* (answers 07–09), *implementation* (answers 10–13) and *operation* (answers 14–18). The resulting new binomial variables have either a value of one or a zero value indicating whether or not an EU-based company received a specific form of support by a South African based organisation.

Question 26: 'What percentage of your South African workforce has been provided with skills training over the past 12 months?'

The original four ranges have been merged into a new ordinal variable comprising three possible outcomes. In particular, there is only one new range, which is composed of the original answers 3–4, meaning that more than 50 per cent of the company-specific South African workforce has been provided with skills training over the past 12 months.

Question 27: 'What type of support has your company provided to other South African businesses, if any?'

For technical reasons, the statistical analysis reduces the set of ten possible answers to this question to one new binomial variable that only indicates whether or not an EU-based company has provided support to other South African businesses.

Question 28: 'How satisfied or dissatisfied are you with the overall business climate in South Africa?'

Drawing on the originally existing ordinal variable with outcomes ranging from 1–5, the new binomial variable only states whether an EU-based company is satisfied with the overall business climate in South Africa or not.

Question 30: 'How is the current business climate in South Africa compared with how it was 12 months ago?'

After rearranging the answers to the already existing ordinal variable with outcomes ranging from 1–5, the new ordinal variable indicates whether EU-based companies rate the business climate in South Africa worse, the same, or better compared with how it was a year ago.

Question 32: 'Do you expect the business climate in South Africa to get better or worse over the next 12 months?'

After rearranging the answers to the already existing ordinal variable with outcomes ranging from 1–5, the new ordinal variable indicates whether EU-based companies expect the business climate in South Africa to get worse, remaining unchanged, or get better over the next 12 months.

Question 34: 'How concerned is your EU company about each of the following threats to doing business in South Africa?'

Here, the set of possible answers to the existing four variables has been reduced from three to two alternative outcomes. The resulting binomial variables indicate whether an EU-based company is concerned with specific threats or not.

Question 35: 'Here is a list of barriers to doing business in South Africa that EU-based companies have experienced in the past. For each of these items, please tell us to what extent your company has experienced it as a barrier.'

Here, the set of possible answers to the existing 10 variables has been reduced from three to two alternative outcomes. The resulting binomial variables indicate whether or not an EU-based company has experienced a specific barrier to doing business in the South African economy.

Question 56: 'To what extent would you recommend South Africa to another EU company as a place to do business?'

Again, the set of possible answers has been reduced from three to two alternative outcomes meaning that the resulting binomial variable only indicates whether or not an EU-based company would recommend South Africa as a place to do business.

8.3 ADDITIONAL RESPONDENT INFORMATION

FIGURE 34 COMPANIES REGISTERED AS LEGAL ENTITIES IN SOUTH AFRICA

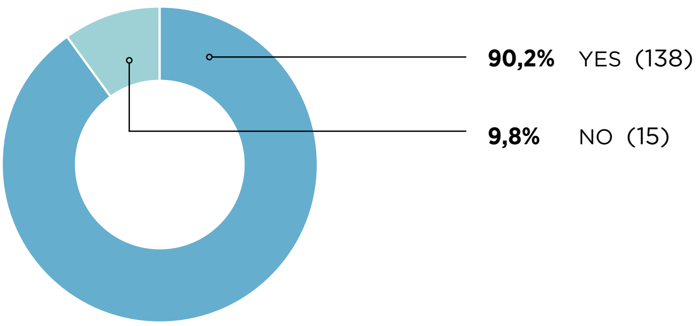


FIGURE 35 CATEGORY OF LEGAL REGISTRATION IN SOUTH AFRICA

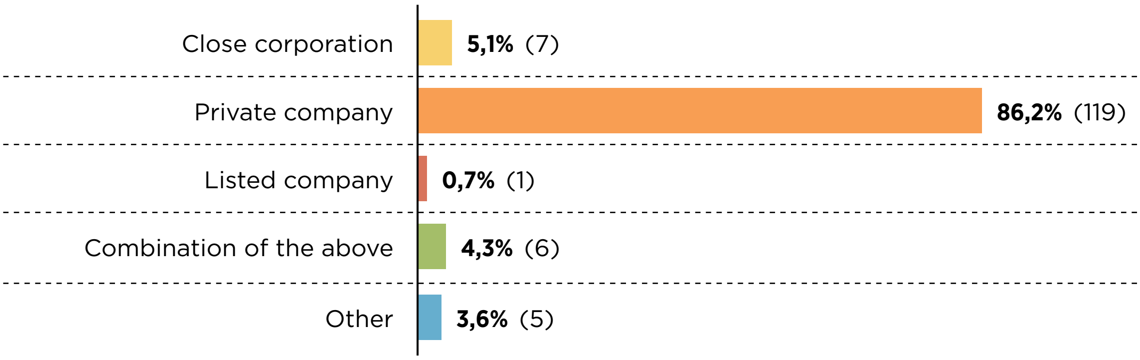


FIGURE 36 HOW THE EU-BASED COMPANY ESTABLISHED THE LEGAL ENTITY IN SOUTH AFRICA

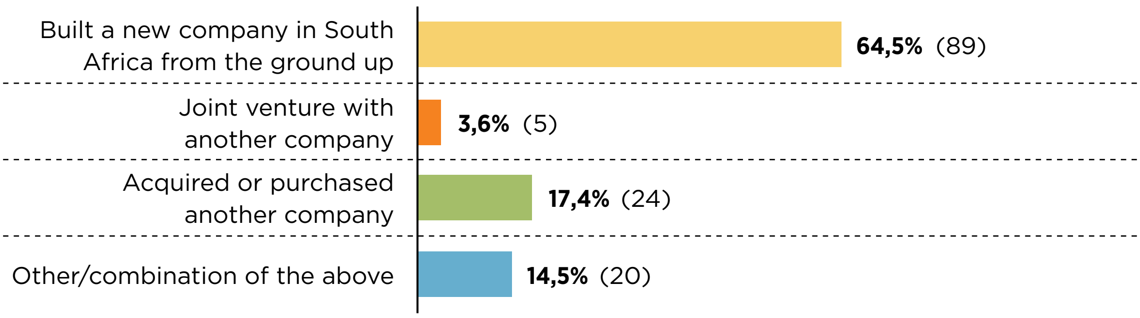
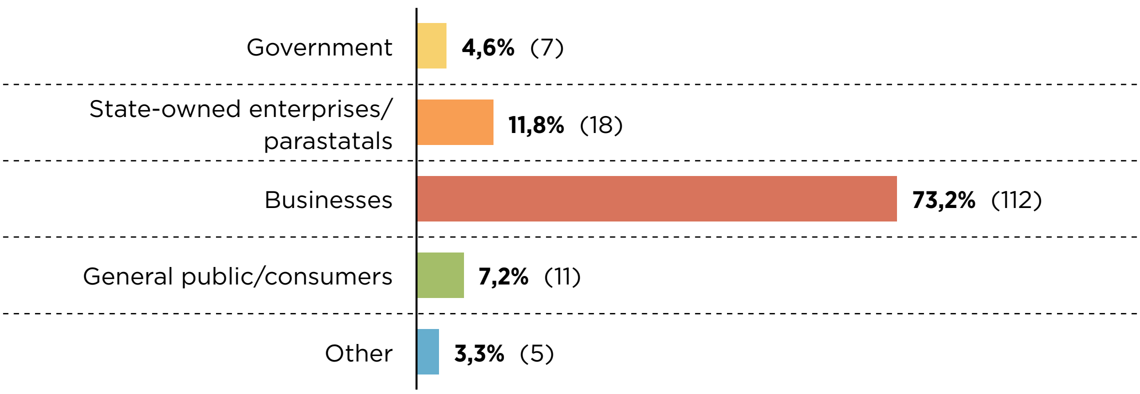


FIGURE 37 SOURCES OF THE MAJORITY OF THE COMPANY'S INCOME IN SOUTH AFRICA



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