

THE FOOD & BEVERAGES SECTOR IN EKURHULENI

Briefing Paper 8

**Ekurhuleni Metropolitan Municipality – University of the Witwatersrand
joint programme of research on industrial development in Ekurhuleni**

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1. Introduction

One of the economic strengths of Ekurhuleni lies in its traditionally large manufacturing capabilities. Food and beverages are a large industrial grouping in Ekurhuleni, accounting for 14% of manufacturing output and 11% of employment. Significant food and beverage firms based in Ekurhuleni include SABMiller, Bokomo Foods, Amalgamated Beverage Industries (ABI), and Kraft Foods. Although the food and beverage sector in Ekurhuleni is mostly focused on local rather than export demand, the sector is important to the region as an employer as well as with regard to the effects it may have on other sectors.

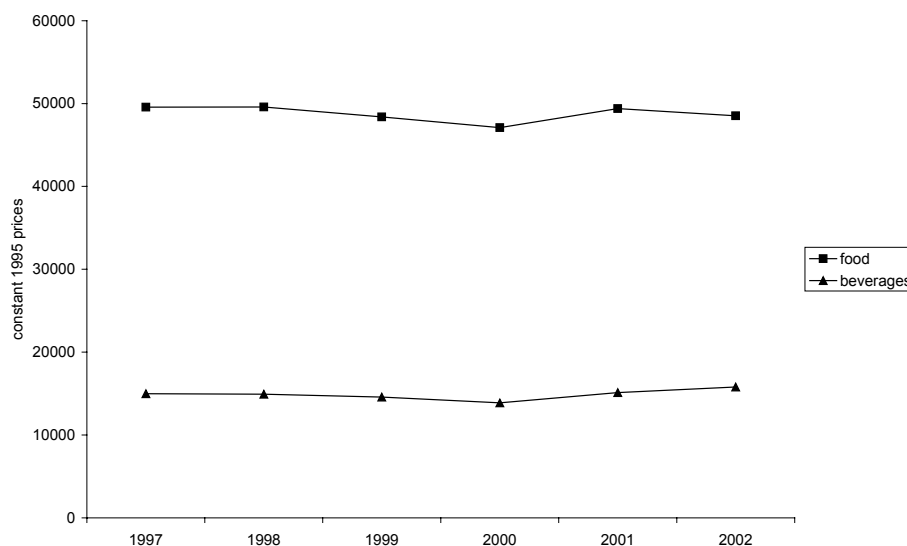
This briefing paper on the food and beverage sector in Ekurhuleni analyses data on its recent performance in the context of longer-term trends. Major factors underlying the performance of the sector will be assessed. It also reports findings from the survey of manufacturing in Ekurhuleni conducted in 2003. The impact of policy changes, as well as the implications for local government, are also briefly discussed.

The food sector is much bigger than the beverage sector. At the national level food manufacturing contributed 11.5% of total manufacturing in 2002, as compared to the 3.7% share of beverages sector. Although both food and beverages are relatively capital-intensive, this is more the case for beverages. In addition, the investment rate has been higher in the beverages sector, especially in recent years, and has accompanied employment losses as the sector has become even more capital-intensive. The food sector is more diverse and covers a wide variety of enterprises from small and medium businesses to very large businesses.

2. Performance

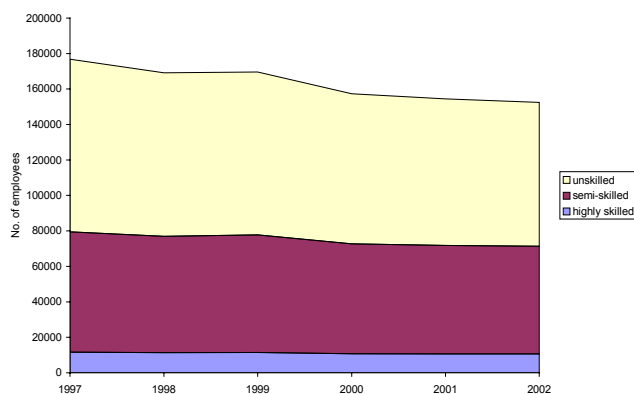
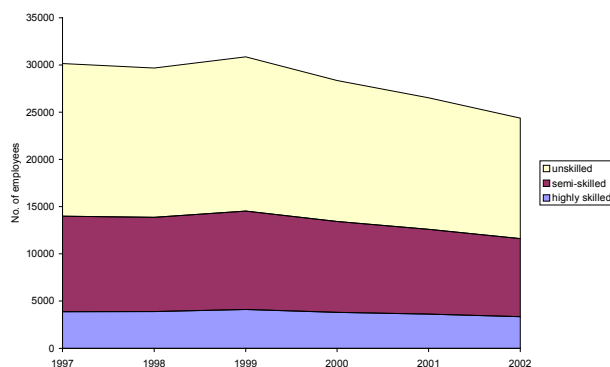
2.1. National Trends

The performance of the beverage sector overall has been better relative to the food sector. The beverage sector recorded an annual output growth rate of 1.1% from 1997 to 2002 compared to contraction at an average rate of 0.4% by the food sector (Figure 1). Low levels of capacity utilisation indicate weak local demand and the inability to penetrate other markets.

Figure 1. Output of the food and beverage sectors (Rand millions)

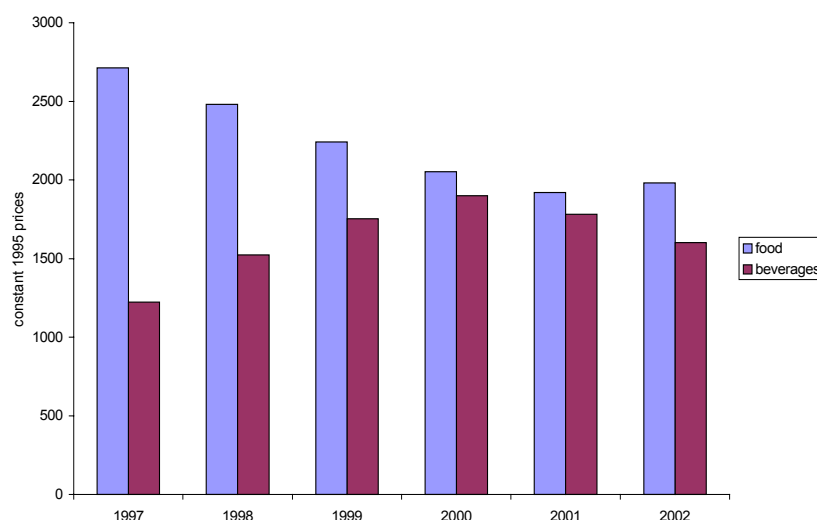
Source: TIPS Standardised Industrial Database

Neither of the two sectors recorded employment growth with the largest declines recorded by the beverage sector (Figures 2 and 3). Employment in beverages declined at an average annual rate of 4.2% from 1997 to 2002. Both sectors are relatively intensive in semi- and unskilled labour which has been the hardest hit by retrenchments, followed by skilled workers.

Figure 2. Food sector employment**Figure 3. Beverages employment**

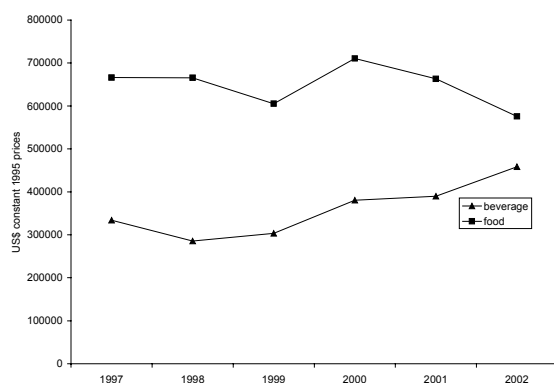
Source: TIPS Standardised Industrial Database

Fixed investment has been poor throughout the 1990s (Figure 4). Investment in the food products sector has been particularly low, given the sector's larger size, and has declined over the period. Again, this reflects low demand and capacity utilisation. By comparison investment in the beverage sector increased up to 2000, adding to total fixed capital stock. The increased investment rates in 1999 and 2000 coincided with falling output, and reflects the fact that some of this investment has been labour replacing rather than labour augmenting as illustrated by the rising capital:labour ratio (Figure X, below). Machinery and equipment are the largest components of investment in both sectors.

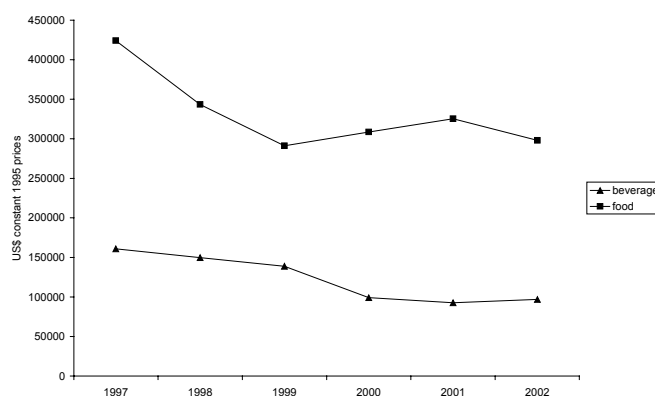
Figure 4. Gross domestic fixed investment (Rand millions)

Source: TIPS Standardised Industrial Database

Production of both food and beverages is largely oriented towards the local market with both sectors exporting less than 10% of their output in 2002. However, imports are even lower such that both sectors have large trade surpluses representing South Africa's comparative advantage in processing of agricultural products (Figures 5 and 6). The trade performance of the beverage sector has improved over the period, with increasing exports and falling imports.

Figure 5. Exports (US\$ thousand)

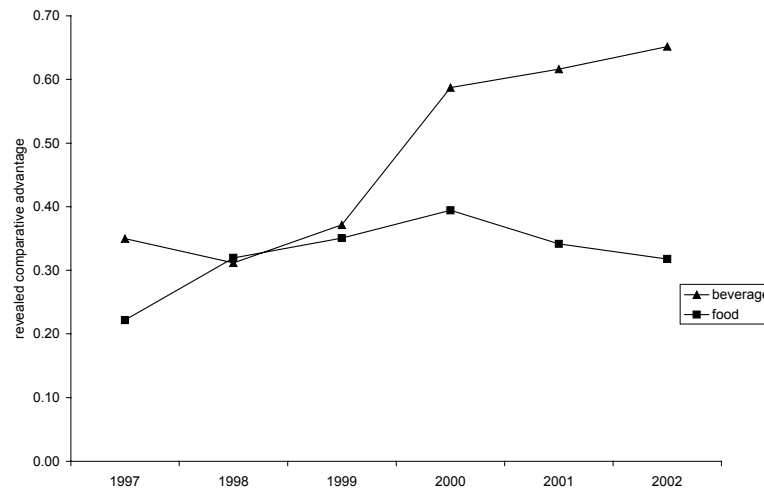
Source: TIPS Standardised Industrial Database

Figure 6. Imports (US\$ thousand)

Beverage exports are largely due to wine, which accounted for 63% of beverage exports in 2002, followed by ethyl alcohol at 13%. In food products the major exports are of sugar and sugar confectionary with a share of 43%, followed by prepared food and vegetables with a share of 34%.

The overall trade performance taking into account both import competition and exports is reflected in the net trade ratio which reveals both sectors with a trade surplus and the strengthening trade performance of beverages in particular (Figure 7).

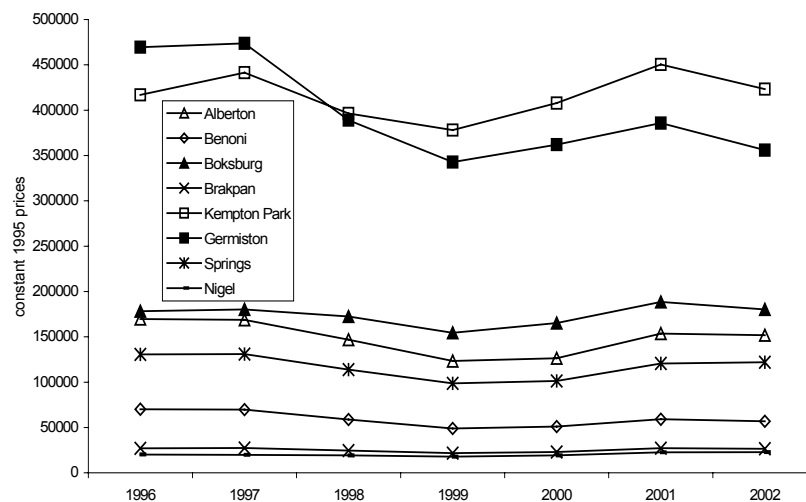
Figure 7. Net trade ratio



2.2 Performance of Industry in Ekurhuleni

The data for food and beverages is aggregated with that of tobacco at the metro level. Kempton Park and Germiston have the largest proportion of food, beverages and tobacco activity in Ekurhuleni (Figure 8). Both areas have experienced a decline in output to 1999 before recovering somewhat in the following two years. It is notable that Kempton Park has performed relatively better and is the largest concentration of food and beverages activity in Ekurhuleni.

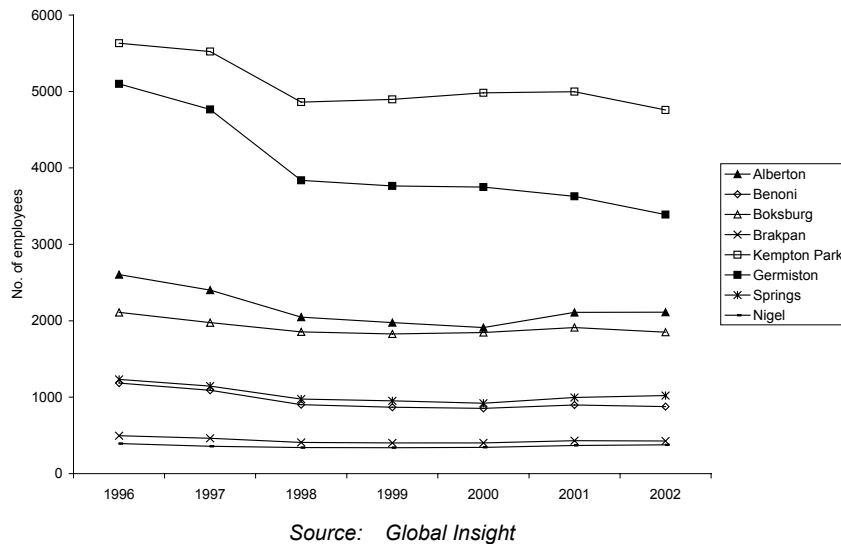
Figure 8. Gross geographic value added of food, beverage and tobacco (Rth)



Source: Global Insight

As with the national data, while output has fluctuated employment has declined (Figure 9). All regions reduced employment during the late 1990s. From 1999 there were, however, encouraging signs in Alberton, Kempton Park and Springs.

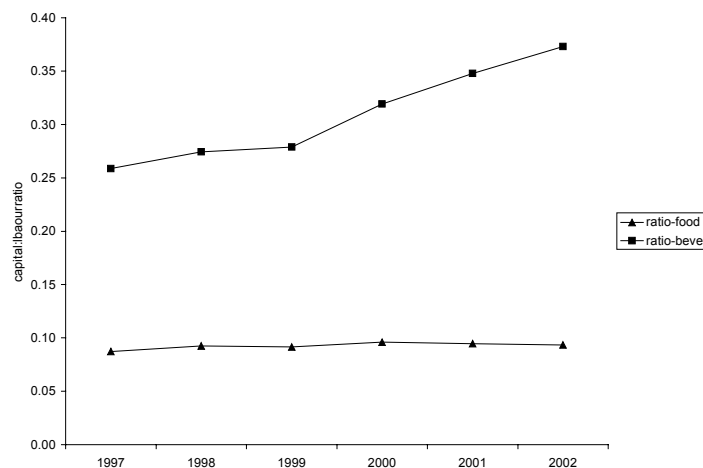
Figure 9. Employment of food, beverage and tobacco



3. Analysis of key factors underpinning performance

As already noted, the most important drive of growth in these sectors is local demand, which reflects the overall performance of the economy, employment and income levels. In the absence of increased demand, the most notable feature has been the increasing capital intensity of beverages (Figure 10) with negative consequences for employment.

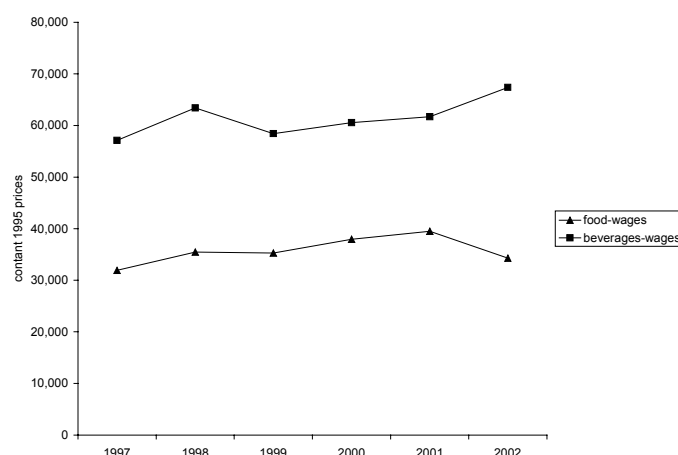
Figure 10. Capital:labour ratio



The higher capital-intensity and higher average skill levels are also consistent with higher average remuneration in beverages (Figure 11). It is notable that average wages in both food

and beverages have increased as employment fell. This largely reflects the retrenchment of lower skilled and lower paid labour, thereby raising the overall average wage rate.

Figure 11. Average remuneration per employee



3.1 Linkages: inputs and major markets for output

As would be expected the single most important input to food products is food itself (Table 1). Various services are also a major input as are transport and packaging products (in the form of paper containers, plastics, fabricated metal and glass).

Table 1. Major inputs to metals and iron & steel sub-sectors, 1998 (Rmn)

| Input sectors | Food | Beverages & tobacco |
|---|--------------|---------------------|
| Transport | 1251 | 159 |
| Electricity | 449 | 175 |
| Services | 6191 | 3455 |
| Paper containers | 1079 | 1258 |
| Plastic products | 692 | 336 |
| Trade services | 528 | 150 |
| Fabricated metal | 658 | 1551 |
| Beverages & tobacco products | 132 | 3438 |
| Glass products | 181 | 886 |
| Basic chemicals | 282 | 121 |
| Gen machinery | 124 | 37 |
| Water | 69 | 139 |
| Food machinery | 164 | 77 |
| Food | 7864 | 1115 |
| Paper products | 0 | 354 |
| Wood products | 21 | 108 |
| Other | 29508 | 2752 |
| Total uses at purchasers' prices | 49193 | 16111 |
| Value-added | 13426 | 9741 |
| Compensation of employees | 7364 | 2760 |
| Taxes-subsidies | 142 | 157 |
| Gross operating surplus | 5920 | 6823 |
| Total output at basic prices | 62616 | 25852 |

Source: Statistics South Africa, *Supply and Use Tables, 1998*

For beverages and tobacco products there are similar patterns although packaging is even more important especially in the form of fabricated metal (cans) and paper. Taking paper

containers, metal, glass and plastic together they account for 25% of all inputs to beverages and tobacco. This indicates the strong backward linkages from food and beverages to other manufacturing sectors. The importance of services reflects the key nature of logistics to food manufacturing.

4. Firm Survey

4.1 Firm performance

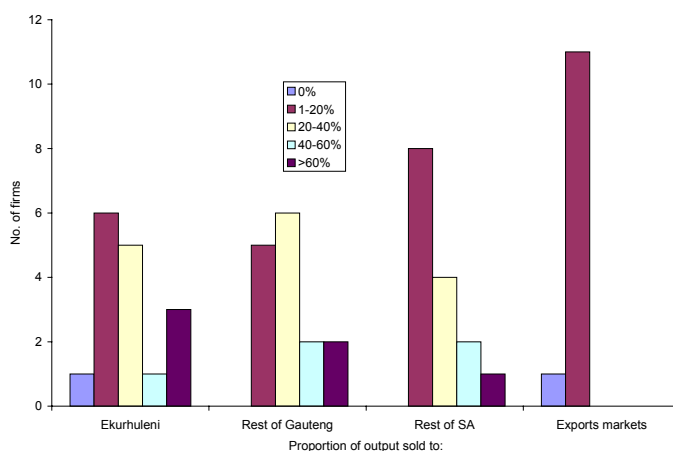
A total of 16 firms in the Ekurhuleni Manufacturing survey were in the food and beverage sector, employing a total of 1599 employees. Of the 16 firms half were small (with less than 50 employees) and a further seven had between 50 and 250 employees. Performance of the sector has been relatively good in the last two years covered by the survey. Firms increased employment at an average rate of 17%, the highest of all the manufacturing sectors with small firms recording the best employment performance while the single large firm reduced employment. And, 40% of firms recorded turnover growth greater than 10% in 2001 and 2002.

Capacity utilisation remains relatively weak, however. Only 2 firms operate at above 80 percent capacity level, 8 firms operate between 60 and 80 percent of capacity level and 6 firms operate below 60 percent capacity level. A low capacity level in this sector is of great concern and it indicates the lack of ability to penetrate other potential markets.

4.2 Market conditions and firm competitiveness

The majority of the food and beverage output is sold to Gauteng (including Ekurhuleni) (Figure 12). Export performance is very poor. While 11 firms have some exports, none export more than 20% of their output.

Figure 12. Proportion of output sold to different markets.

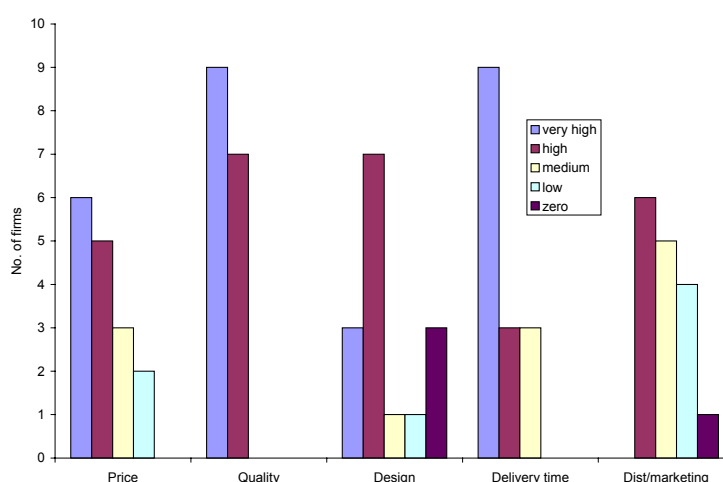


In the last twelve months firms identified that the demand for the products grew in Gauteng followed by Ekurhuleni and rest of South Africa. 6 firms indicated that more than 60 percent of their demand grew in Gauteng compared to 5 firms in the rest of South Africa and 3 firms in Ekurhuleni. Similar patterns are followed in the expected growth with the expectations of exports being better. Firms reported similar patterns in the growth of demand with most coming from Gauteng.

Unsurprisingly, firms source the majority of their inputs locally, although three firms import their main inputs.

Firms in the food and beverage sector rated quality and delivery as the most important factors for their competitiveness (Figure 13). This is not surprising since the nature of the business requires quality products which should be delivered on time. This is followed by price. Design and distribution/marketing was the least important factor for firms' competitiveness.

Figure 13. Competitive factors



For almost all firms raw materials were their largest costs of production, followed by wages and salaries, and delivery and marketing. Both raw materials and wages and salaries also experienced the highest cost increases (in excess of 10% per annum over the last couple of years) (Table 2).

Table 2. No. of firms recording different changes in production costs over 2 past years

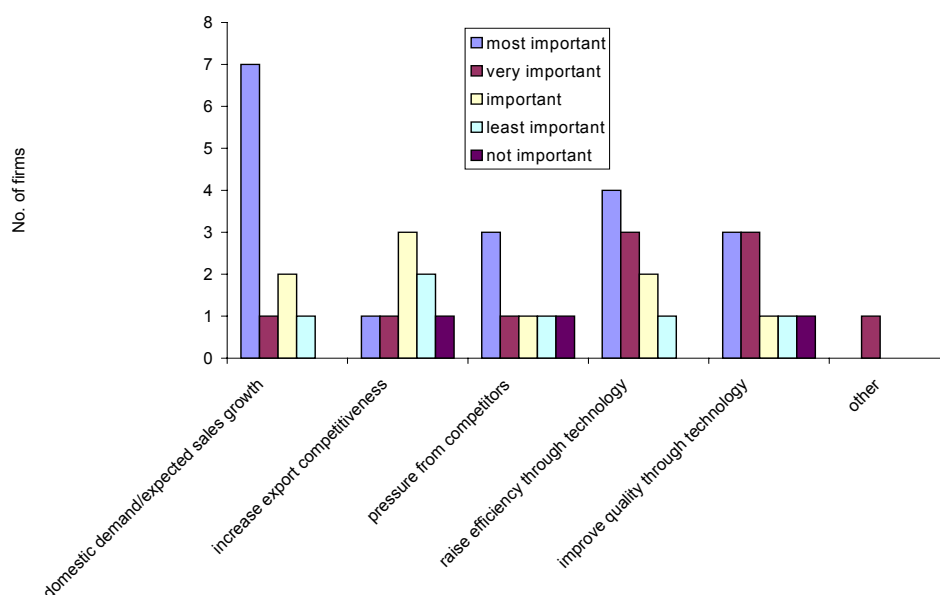
| | Negative | 0% | 0-10% | >10% |
|-----------------------------------|----------|----|-------|------|
| Raw materials | 0 | 2 | 6 | 8 |
| Interest charges and depreciation | 0 | 3 | 11 | 2 |
| Wages and salaries | 0 | 1 | 7 | 8 |
| Delivery and marketing | 0 | 0 | 10 | 6 |

4.3 Investment, skills and technology

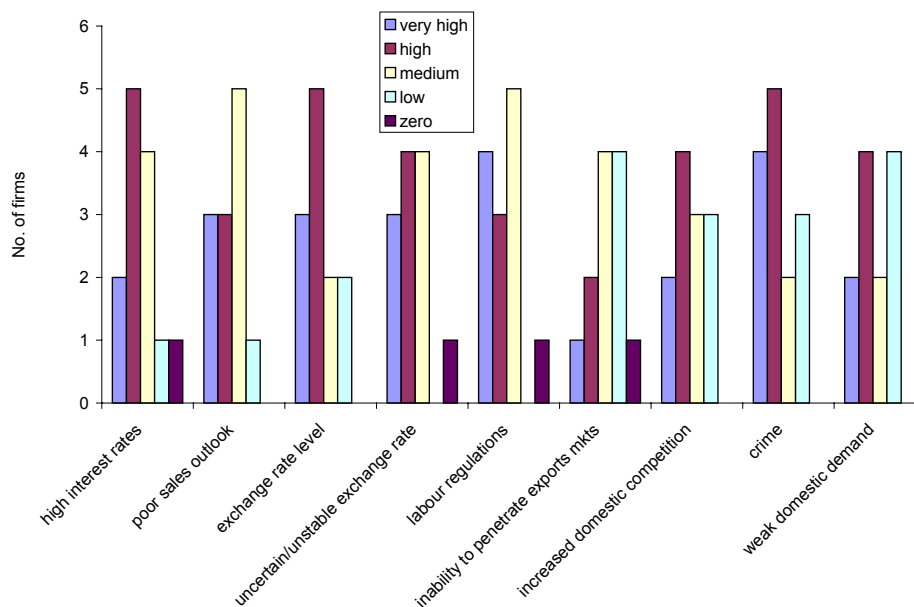
56% of firms rated the importance of up-to-date technology as very high or high for their competitiveness. This is also reflected in high and increasing investment levels in 2001 and 2002. Investment rates increased dramatically between 2001 and 2002 by 26% averaging R3.6 million per firm and investment per employee was R36 393. Investment in domestic and imported machinery and equipment grew by 42% and 54% respectively between 2001 and 2002. Imported machinery and equipment accounted for the largest share of new investment in 2002 with 48% followed closely by domestic machinery and equipment at 46%.

Expected sales growth was indicated as overwhelmingly the main motivation for investment (Figure 14). This is followed by raising efficiency and need to improve quality through the latest technology. Increased pressure from domestic competitors was also indicated as one of the motivating factors for investment.

Figure 14. Motivations for investment



There were a number of factors indicated by firms as discouraging to investment (Figure 15). Crime was reported to be the main factor in discouraging firms to invest, followed by labour regulations and exchange rate uncertainty.

Figure 15. Factors discouraging investment

Education and training

Education and training is a major challenge in this sector as in South African as a whole. Almost all firms in this sector indicated their average education level as being either matric or below. 50 percent of firms have an average education level of below matric and 44 percent firms reported an average education of matric.

Usage of the skills development levy is relatively with half of the firms in the food and beverage sector claiming back the levy. But, levels of expenditure on training are amongst the lowest in manufacturing. In 2002 the average amount of expenditure on training per employee was just R836. The preferred source of outside training is business partners and private training schools. Only 2 firms use industrial training boards as their external preference.

4.4 Government incentives and policies

Firms indicated the most important local economic development policies as being ensuring reliable services (Table 3). This was rated as being important by an overwhelming 94% of all respondents. Ensuring reasonable tariffs and reliable public transport followed at 81% of respondents.

Table 3. Local economic development policies identified as important

| | % of firms |
|---------------------------------|-------------------|
| Supporting skills training | 60 |
| Marketing the area | 44 |
| Ensuring reasonable tariffs | 81 |
| Overall quality of life | 67 |
| Reliable services (elec, water) | 94 |
| Public transport | 81 |

The awareness of different incentives schemes offered by the government is very low. Only 8 firms know about the small and medium enterprise development programme (SMEDP) with 5 firms being aware of the export marketing and investment scheme. But, what is worse is that there is only one firm in the food and beverage sectors that has made use of an incentive scheme. The only scheme used is the SMEDP.