SPECIAL REPORT

Privatization in the minerals sector in South Africa

By M. H. Solomon and J. van Schalkwyk

Privatization of South African diamond producer Alexcor will take place in the near future. This paper provides criteria and mechanisms for the company's conversion to the private sector.

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The issue of privatisation of State-owned mineral assets in South Africa is simple on one level because there is only one operating mine owned by the State, and complex on another in that the privatisation of this one remaining operating asset cannot be seen in isolation from the objectives of the major programme of political and economic reform adopted by the interim Government of National Unity (GNU), the Reconstruction and Development Programme (RDP), and the programme for privatisation of many other state assets in line with these objectives.

The programme of privatisation of state assets in South Africa is not one of merely "selling the family silver" to pay for budgetary deficits or to prop up (in the short term) the depleted state coffers as is happening in many developing countries. It is far more complex. State assets must in the first instance be defined as those assets that are income generating on a commercial basis but wholly owned by the government, in other words, those assets that could conceivably be more appropriately located in the private sector.

Secondly, the reason for the State having established the facilities as public enterprises is a critical consideration. For example, Armscor was established by the state to develop weaponry for the enforcement of apartheid during the period of sanctions and international isolation. The civil war and sanctions are over and the need for military arsenals is severely diminished, as is the need to maintain Armscor in terms of its original rationale. However, during its peak period of development, a national competence in military technology was developed, and its products had the advantage of being field and battle tested. In certain areas, South Africa's military technology is world class, and without considering the moral arguments around the marketing of military technology, there is a commercial case for retaining and not disbanding this competence. However, it is inappropriate to retain Armscor as a private enterprise.

Many enterprises that were established for historical political reasons no longer exist.. Alexcor is the last remaining such mineral asset. Whether or not this particular asset would better serve the objectives of the RDP within or without the State structure will be the focus of this study.

THE CURRENT PROGRAMME OF PRIVATISATION OF STATE ASSETS

In January of 1995, an extraordinary cabinet strategy session held on privatisation decided to "reorganise" state assets (*GNU Discussion Document*). This decision was made not only in respect of the minerals assets (Alexcor), but all other commercialised assets.

The role of the commercialised state assets has to be reconsidered in the light of the objectives of the Reconstruction and Development Programme. Essentially this means that the State has to reprioritise state expenditure (many of these assets run at considerable losses and place a drain on the fiscus) and optimise the utilisation of all state resources. These decisions will be taken in the light of the historical motivation by the previous governments in establishing the assets (Armscor, Denel, Alexcor), the required institutional composition of the public sector in the light of current political and economic agendas, and the need to achieve the government's commitment to fiscal discipline. The elements of this process will incorporate:

- the maximisation of existing budgetary resources;
- the mobilisation of new resources
- provision of efficient financing mechanisms for a range of activities related to the RDP;

- re-deployment of the existing resources within the public enterprises;
- development of human resources.

A major consideration in respect of the reorganisation of State assets must be the function, location and areas of jurisdiction of the wide range and diversity of state enterprises. This means that the decision as to whether a particular asset is to be privatised or not needs to be taken in the light of whether it can serve the objectives of the RDP more effectively as part of the State structure, or within the private sector.

An important factor in this respect is the new provincial structure of government, and the relations between, and the respective powers of, the various levels of government as defined in the interim constitution. Juxtaposed with this must be the overall strategies for private sector development and the restructuring and reform of the public sector, which are founded on the principles and objectives of the RDP. The two sectors play essentially different roles in these objectives, and these roles in turn are contingent on their respective functions and core competencies. Where there is overlap or inappropriate location of these functions and core competencies, they must be optimised as part of the process of restructuring. That is, if an asset does not fit the redefined role of the state in the current political and economic direction, it is appropriate that the asset be privatised.

The role of the public sector can be broadly defined in terms of its responsibility for the provision of a range and diversity of social and security services that would be inappropriate for the private sector in terms of political philosophy, effective performance under private sector control(unprofitable in respect of private sector requirements but strategically necessary), or the exacerbation of inequalities created during the apartheid era. Fundamental to the current drive for privatisation is the facilitation of an efficient partnership between the two sectors in which the competencies of the private sector (capital, management and technology) can complement and enhance the roles that are necessarily the domain of the public sector.

Objectives

The objectives stated here are drawn directly from the documentation issued by the Department of Public Enterprises, but are interpreted in the context of this study. These are:

- the facilitation of economic growth;
- the funding of the RDP;
- creation of wider ownership in the South African economy;
- the mobilisation of private sector capital;
- the reduction of state debt;
- the enhancement of the competitiveness of state enterprises;
- the promotion of fair competition;
- the financing of growth and competitiveness.

The guiding principles and values governing the process

Political reform in South Africa has just begun, and it is unreasonable to expect that various regulatory, fiscal, economic and social regimes established over centuries of colonial rule and decades of apartheid rule be undone overnight. However undesirable these orders may be, a rapid, unstructured and inadequately planned transition would prove disastrous. One has merely to consider the current plight of many of the de-colonised African countries to ratify this argument. The country is however in the throes of an aggressive, well co-ordinated and consultative process of regulatory and legislative reform in all sectors of society and civil reform.

The process of restructuring state assets is integral to the process of societal and civil reform: the restructuring and the concomitant disposal of State assets cannot be an arbitrary fund raising exercise undertaken in isolation from these other processes. In other words, they must be undertaken in such a manner that they serve these processes.

The principle issues affecting the values and guidelines are:

- coherence with legal and regulatory developments;
- participation and protection of the interests of organised labour and employees of affected state enterprises;
- the participation and enhancement of interests of the poor and disadvantaged groups;
- the participation of all other directly affected stakeholders;
- transparency of process;
- restructuring should be geared towards the provision of new, or improvement of existing, services to poor and disadvantaged communities;
- restructuring should be evaluated in terms of macro-economic effects, particularly with respect to savings, investment, balance of payments, ownership, economic growth and employment creation;
- a sectoral approach incorporating enterprise specific case studies is imperative;
- integration of socio-economic imperatives is of tantamount importance;
- restructuring should as far as possible facilitate the development of new projects that will encourage further local and foreign investment;
- direct foreign ownership should be limited, and the focus of any foreign investment should as far

as is possible be associated with technology transfers; and
- conflict of interest between the public interests and private interests must be minimised.

The privatisation criteria of the previous government

The move towards privatisation is not new. It began in the late 1980s with the publication of a White Paper on Privatisation and Deregulation, but the pressures and motivations at that stage were fundamentally different to those of the present government, as were the principles and guidelines. The previous initiative was based primarily on a move to reduce public sector involvement and intervention in the economy through a transfer of state-owned productive capacity and capital to the private sector.

The objectives were stated as being:

- to limit or reduce public sector involvement in the economy in order to make more capital, production resources and opportunities available to the private sector; and
- to afford the private sector the opportunity to develop and grow optimally with minimum Government interference and regulation.

The stated principles and guidelines also differed markedly from those of the current government as outlined above, and starkly highlight the difference in political motivation. The principles in terms of which State-owned assets were deemed suitable for privatisation were described as being those that:

- were incorporated in terms of the Companies Act;
- conducted private sector activities;
- operated and competed in terms of free market principles;
- were profitable and taxable;
- were professionally managed, and had experienced boards of directors; and
- were not monopolies.

In addition to this, the guidelines for privatisation prescribed a process facilitating:

- deregulation of the activities of the privatised organisation to allow for free competition;
- the establishment of a corporate profile for the organisation;
- a programme of commercialisation to establish a profitable business;
- a process of transfer of ownership to the private sector; and ultimately
- stock exchange listing.

KEY DIFFERENCES BETWEEN THE TWO APPROACHES

The two approaches clearly distinguish the points of departure in political philosophy of the governments and these differences are discussed here.

Fundamental philosophy

The major motivation of the apartheid government was clearly to use privatisation as a vehicle for reducing State intervention in the economy through limiting or reducing the State ownership of the means of production.

In contrast, the Government of National Unity's (GNU's) approach is to use privatisation as a tool in a structured programme of economic development that is by design interventionist, in the sense that it is being driven by the government with the co-operation of the private sector and the community at large. It is aimed at optimising the country's resources rather than reducing intervention in the economy. The approach is thus one of inclusive mobilisation of resources through re-deployment rather than exclusive withdrawal from the economic process through disinvestment in the means of production.

There is another remarkable difference in the philosophy behind the two privatisation initiatives: the approach of the last government was extremely technical in that even the objectives were prescriptive and restrictive. For example, the objectives addressed implementation issues such as management, profitability and taxation, rather than the economic rationales behind the privatisation initiative. This is markedly different in the current initiative, where the objectives are based on principles rather than methodologies.

Ownership

The specification of ownership is the starkest indication of political motivation. The Nationalist specification was that privatisation was ultimately to lead to transfer of ownership to the private sector, which was at the time (and still is) dominated by white capital and interests, and to a listing on the stock exchange, primarily a white preserve. The lack of mobilised or individual black capital would ensure that any privatisation would result in white ownership, even though this is not specifically stated. The process of privatisation was thus intrinsically exclusive and partisan to the benefit of the white sector of the community.

There may also have been a more sinister aspect in that, even at the time of Iscor's privatisation, there was a growing realisation amongst the country's leaders that a move towards majority rule was inevitable, and that privatisation of the major means of production under State control would ensure ongoing white control of the economy subsequent to political transfer to the black majority. The Afrikaans suffered from this plight at the hands of the English after the Nationalist Government came to power in 1948: for almost twenty years after the onset of Afrikaans-dominated political rule, the English community retained critical economic control of the country. It would be surprising if this strategy had not been recognised and adopted by the nationalist leadership as an essential means of ensuring the balance of power and the strength of the white sector in a democratic regime.

There is no documentary proof to support this theory, but it is supported by the fact that the organisations privatised were either means of production, or those that governed logistical control of the means of production (Transnet) rather than service organisations such as Telkom. (Eskom appears to be an exception.)

The democratic government's approach is very different, but no less partisan. In this instance, privatisation to all intents and purposes prescribes black ownership through the specification that privatisation should be directed towards "wider ownership", should incorporate the "enhancement and participation of poor and disadvantaged groups" and should "integrate socio-economic imperatives".

A further difference in approach between the two initiatives is the specification that foreign ownership in newly privatised initiatives be minimised. This was not specified in the last round, which adds weight to the theory that the purpose of the process was to enhance local white ownership.

Economic development

The political motivation in promoting the specific interests of the primary constituencies of the two respective governments is clear and underpins the argument of the political flavour of privatisation. In this respect, however, the current privatisation programme is far more orientated toward structured economic development than the previous process.

Socio-economic imperatives

The objectives of the current programme are dominated by the need to use privatisation for the benefit of the community at large. It explicitly emphasises the importance of integrating socio-economic imperatives into the process as well as stating that privatisation should benefit all stakeholders, not only the fiscus and the shareholders. There was no allusion to any of these aspects in the objectives laid down by the previous government.

Transparency of process

The manner in which the current process is taking place is constructive in that there is an active attempt to solicit public participation in the process. The last government issued a white paper for comment, but made no invitation to the public to materially participate in the process.

CASE STUDY: ALEXCOR

History and background

Alexcor is the State-owned diamond mining operation in Namaqualand. It was started in 1925, and since its inception, has been an extremely controversial organisation. Alexcor started life as the State Alluvial Diggings after a proclamation was passed forbidding the prospecting for and recovery of diamonds. The reason for this was to control the production of diamonds, and hence to stabilise the market, a move probably inspired by De Beers.

During the era of Nationalist Party rule, the State Alluvial Diggings became a haven for poor whites, and consequently mining efficiencies were highly suspect. In 1992, two years prior to the election, the company was commercialised, a move that has greatly enhanced the profitability and efficiency of the company.

The organisation makes profits of some R50 million a year, and one-third of the after-tax profits are given to the Alexcor Development Trust Fund, the company's corporate social investment programme.

The organisation is controversial for a number of reasons. It is under the control of a board which, although it incorporates members from the community of Namaqualand, is still dominated by elements of the old order. It is notable that the organisation still employs a predominantly white work force from outside the territory, particularly in the senior strata, and that little effort has been made to integrate the Alexcor Alexander Bay community into the Port Nolloth community. This has drawn sharp criticism from the Port Nolloth community, who resent the fact that, for example, new sports facilities have been built inside the mine's residential complex for the use of a privileged few, whilst they have few facilities to speak of. Other issues, such as the continued hiring of outsiders, and the contracting of laundry to white concerns in Springbok while there is a 70 per cent rate of unemployment in Port Nolloth, have drawn equally sharp criticism. It is anathema to the community that the *State* is extracting the area's natural wealth, while the local communities are suffering.

The Northern Cape Minerals Development Advisory Committee

On 20 September 1995 a meeting was convened by the Department of Economic Affairs, Trade, Industry and Tourism to set up a task team to address the problems facing the minerals industry in the Northern Cape and Namaqualand. The meeting was attended by representatives from the government, community-based organisations, non-governmental organisations, and industry. A number of priority issues were identified for the attention of the task team. The general objective of the team is to promote minerals-driven sustainable economic and social development in the Northern Cape Province, with particular reference to Namaqualand. This is to be achieved through building linkages between national and provincial actors, and incorporating short-term deliverable projects into medium-term economic planning processes. These objectives are to be achieved by incorporating all relevant role players.

A list of specific potential projects was discussed. These are to be prioritised by a Minerals Development Advisory Committee, which will be convened as a permanent committee before the end of October 1995.

In the interim, as an indication of the importance that the Northern Cape legislature attaches to the privatisation of Alexcor, the task group has identified this as a major priority for its attention. This case study will reflect the criteria, principles and values discussed above as a basis for discussion and debate on the matter.

Options for community participation in the privatisation of Alexcor

The study needs to demonstrate the considerable benefit that the mining of diamonds in Namaqualand provides at various levels of the economy. Unfortunately, it is the local level that benefits least from the mining of diamonds at Alexcor, and this is where the most volatile conflicts between the communities of Port Nolloth and the Richtersveld and the company arise.

For the local communities, the broader issues of balance of payments, fiscal contributions and multiplier effects are essentially meaningless. Apart from the employment created on the mine itself and in a few service sectors, and the corporate social investment programmes subscribed to by the various mines, there is little benefit for the communities. In their living memory they have seen the rights of access to diamond deposits being handed out to whites from outside the area and the state-owned interests commercialised with very little tangible benefit to them. Alexcor is making a profit for the state of around R50 million per year while the communities live in poverty.

With the downscaling of the minerals industry in Namaqualand over the next two decades, job losses are going to be substantial. To offset the disastrous effects of downscaling on both the economy and the environment, there has to be provision made in any privatisation of Alexcor for the significant returns from mining to be directed not only into private hands, be they black or white, but to the community at large. In this respect a mechanism needs to be found whereby the profits derived from mining can provide the engine for sustainable development. The dramatic effects of the imminent downscaling, which are quantifiable at various levels of the economy, serve to underline the need to replace the wasting mineral assets and the associated declining wealth with the sustainable economy that mining cannot provide.

If one accepts then that a pre-requisite for privatisation must be that it provides for sustainable development, it is necessary to examine the implications of this theory. The primary implication would be that large amounts of money accruing from the mining would have to be set aside and utilised for investment in sustainable development projects such as tourism, agriculture, livestock and game farming, social forestry, and other alternative economic activities.

There are a number of critical riders to this statement. These are dealt with below.

Funding requirements for proposed models

What amount would be realistic to provide for an effective programme for sustainable development that would outweigh the negative effects (at a local level) of the environmental damage due to mining? As potential investment is infinite, one has to define a minimum amount of money that would be significant in terms of meaningful investment in sustainable development projects. One could attempt to quantify the amount scientifically by calculating the amount of investment required to develop eco-tourism infrastructure or selective alternative projects, but such an exercise would be futile. This would need at least a number of qualified pre-feasibility studies on land-use options which would then be optimised. This is beyond the scope of this study.

Intuitively, the corporate social investment funds already provided by the mining companies, even if they were redirected from community halls, schools and other community facilities towards the establishment of economic projects, is insufficient, and little significant development could be catalysed with these moneys.

This leads to the conclusion that, subject to the premise that there should be no additional taxation, royalties of levies that will add to the input costs. These will serve merely to sterilise ore reserves through raising the cut-off grades, and effectively shorten the life of the mine. This would be counter-productive to any economic development programme. If this is to be achieved, there has to be some other means of harnessing the returns from mining to serve the interests of sustainable development. Options whereby this is possible are examined here.

Community considerations and land claims

There are a number of land restitution issues in progress in the feeder constituencies to Alexcor, and one of the problems being experienced is the determination of which communities have legitimate rights to benefit from participation in the privatised Alexcor, assuming that a successful vehicle for community development could be found. The community or communities that would benefit from this participation are thus not defined for the purposes of this study.

Models for community participation in Alexcor

A number of possible options are presented here. These may not be the only options available, but are intended to demonstrate two concepts:

- effective community participation in, and benefit from, the mining operation beyond direct employment and corporate social investment benefits; and
- the investment of the financial returns from mining in the sustainable economic development of the area.

Much work needs to be done before determining the exact a model that would be effective in achieving the objectives of investment in sustainable development, whatever these prove to be.

The Canadian NTI Model. There are various models that make it possible to provide for minerals-driven sustainable development without resorting to higher taxation or making the investment unattractive. One of these is that recently employed by the Innuit people in the North West territories of Canada, whereby a commercial company called Nunavut Tungavic Incorporated (NTI) was set up to manage the natural resources in the Innuit territory. These include land, water and fishing rights, mineral rights and rights to game and eco-tourism, which were acquired through a land restitution claim by the Innuit, and are owned jointly by the six communities in the region.

The NTI model provides for joint ventures with private sector specialist companies to exploit these assets. The profits earned by NTI are then ploughed back into development projects that are to the general benefit of the community rather than they being distributed as dividends for individual gain.

Partnership with a mining company. In the time-frame allowed for privatisation, it is unlikely that the community will be able to provide or muster the core competencies required to mine the deposits owned by Alexcor efficiently. It is thus imperative that should a practical and workable model be established to purchase the company for the equity participation of the community, this vehicle will have to manage Alexcor jointly with an experienced and financially sound mining company partner.

It is one thing to theorise on the need for sustainable development, and put forward convincing ideological arguments for its promotion through the contribution from mining. It is entirely another question whether the concepts are palatable to potential mining company partners. The question is whether a mining company would consider the options to be sufficiently attractive to participate in any of them.

Any potential partner's viewpoint would be typically commercial. Companies see themselves as making a considerable contribution to the fiscus, operating effective corporate social investment programmes, and having a primary responsibility to their shareholders. Thus any erosion of profits for altruistic purposes is undesirable and in principle, unacceptable.

In examining options for partnership, therefore, it is only the options that prove to be sufficiently attractive to a potential mining company partner that are meaningful. The willing participation of the company in examining the financial alternatives is crucial.

Equity participation by the community. A vehicle whereby an equity position could be purchased in Alexcor needs to be established. This could be achieved by setting up a professionally run resources company (i.e. a commercial enterprise as opposed to a community trust or non-government organisation) which would be charged with the management of all the natural resources of the area on a commercial basis. These natural resources would include the endogenous minerals, agro-forestry and ecological potential of the area.

The proceeds from mining (dividends accruing to the company from its investment in the minerals leases) would be reinvested in other forms of commercially sustainable development such as tourism, forestry and agriculture. The returns from these would in turn be reinvested in a similar manner. In this fashion, mining would provide the catalyst for sustainable development.

The company, if set up along the Canadian lines, would be professionally managed on a commercial basis, with half of the board of directors appointed by the community, and the other half by other *direct* stakeholders such as the parks board, agricultural representatives, mining interests and provincial and central government. It would manage commercially all natural resources in the area defined for use or ownership by the community.

Definition at this stage of the "community", or the manner in which land-use is restored (usufruct or title) is immaterial. This is an important point, as it means that implementation of such an option could commence prior to the outcome of the land restitution proceedings.

There are two ownership options here:

a. Equity Partnership in the Company. The resources company could take an equity position in Alexcor (the extent of which would be contingent on the affordable level of investment) alongside the partnering mining company. The partnering mining company would undertake the mining and management of Alexcor.

The resources company would pay for its participation in the project through loan funding, and would thus be required to service the loan before reinvesting the dividends. It would thus be equivalent to any other equity partner. The community ownership element is irrelevant to the business arrangement, but important in respect of its benefit from the dividend returns.

b. Resources Company Ownership of Alexcor. In this option the entire share-holding of Alexcor is purchased from the State by the resources company at a market-related price. A partnering mining company could then undertake responsibility of mining and managing the mineral rights on the basis of a management contract.

The major issue is the cost to the resources company of purchasing all or a part of the Alexcor share-holding, whether loan funding could be secured for this purchase, the rate of interest applicable to such funding if it was available, and finally, after servicing the loans for this purchase as well as the resources company's share of the capital investment in mining plant, whether there would in fact be returns for investment into sustainable development projects.

Community Royalty. Another ownership option is that Alexcor is sold to a private sector operator in its entirety, but that the community retain full mineral rights (which are currently State owned), through the resources company. The private sector operating company could then pay a negotiated royalty to the resources company. This royalty would then be used for investment in sustainable projects.

This could be effected in two ways: pre-tax revenues or after tax profits. Adding the cost of the royalty to pre-tax revenues is unwise, as it would add to input costs, thus lowering operating profits, and hence raise cut-off grades. This could result in sterilisation of some of the ore reserves, which is highly undesirable.

A royalty on profits, which is auditable, would be preferable from the company's perspectives, but would serve to lower the returns on investment. Although auditable, it would nevertheless be possible for the mining company to manipulate the calculation of profits. There is little doubt that there would be profound suspicion on the part of the community unless the appropriate checks and balances were built into any arrangement of this nature.

General Comments. There are no doubt other options that could be examined. However, whichever options are proposed, the deciding factors would be acceptability to all parties including the mining company, a workable format for the resources company, and the economic viability of the options considered.

Lack of representation of the community on the management structures of the company is very much part of the issue, and needs to be addressed. This matter should be raised on a political level with Minister Sicgau.

Alexcor also has potential for the development of small enterprise in the area. It is already involved in commendable programmes such as the cultivation of oysters in worked out diamond trenches; co-operative ostrich farming schemes; agriculture along the Orange River, and various other non-mining, developmental schemes. It is also suitable for experimental small mining projects on dump re-treatment, bedrock sweeping and other possible forms of sub-contracting. As the organisation is State-owned, the logistics of setting up these projects should be simpler than with privately owned companies.

Adherence to the objectives of privatisation

The Facilitation of economic growth. As the sale of Alexcor to a mining company or capital interests will not lead to an increase in production, it cannot serve to facilitate economic growth in any direct sense other than through the emersion of the proceeds of the sale in the pool of RDP funding. There will thus be no means of directly measuring the effectiveness or efficacy of the privatisation. Furthermore, as the proceeds of mining are already reporting to the fiscus, there is little to be gained from the sale other than the immediate availability of a limited amount of money: if sustainable development is the criterion, whether locally or nationally, a longer-term return to the fiscus will arguably be preferable to a shorter-term fillip.

The funding of the RDP. This has be considered at a number of levels, sub-regionally, regionally, provincially and nationally. It could be argued that present and future corporate social investment through the Alexcor trust is serving this purpose. However, this is not strictly true in that the practice, while making a very valuable contribution to the quality of life of its beneficiaries, is nevertheless charitable and paternalistic, and does not contribute to economic development as such. It therefore does not serve the RDP in its fundamental sense. This is also true of the regional context, as the fund is not confined to the Alexander Bay/Port Nolloth sub-region.

At a provincial level there would be little or no direct benefit from the sale of Alexcor, and this is a cause for concern as it is ultimately the provincial government that will have to take responsibility for, and bear the brunt of, the closure of mines in Namaqualand. Proceeds from the sale of the company will be returned to the central fiscus, where there will be an indirect, but not tangible, transfer to provincial RDP allocations. At a national level, there will be benefit, as the sale will result in a considerable amount of money.

The greatest concern is that there will be a once-off RDP funding benefit, with no sustainable returns.

Creation of wider ownership in the South African economy. Sale of Alexcor to existing black-owned capital interests would not optimally serve the creation of wider ownership. Equity participation in the privatised Alexcor at individual and community levels from within the Namaqualand community would serve this purpose. The model for privatisation is thus critical.

The mobilisation of private sector capital. Any model that will achieve participation of the funding community at the levels discussed must involve the mobilisation of private sector capital. This should however be mainly through the provision of underwritten loan capital to community interests, rather than through the stock market as was the case in the privatisation of Iscor.

The reduction of state debt. Because of its critical role in the development of sustainable economy in a region dependent on a declining minerals economy, the privatisation of Alexcor should be more orientated towards the facilitation of economic development at a sub-regional and regional level, than towards the reduction of State debt. Privatisation for this purpose would be tantamount to discounting the sale of extremely valuable "family silver" to remedy the follies of the previous government.

This said the reduction of State debt, whoever created it, is a major economic and budgetary issue. The interest on public debt in South Africa in 1994/95 is a massive 17.3 per cent of the national budget against a world average of 7.3 per cent . This must be seen relative to the expenditure on general administration of 7.6 per cent (against the world average of 15 per cent), security services at 18.1 per cent (15 per cent); economic services at 11.8 per cent (26.9 per cent) and social services at 45 per cent (36.8 per cent).[1]

The problem of State debt is demonstrated in the distortions of South African budget relative to the rest of the world. Notable is the unhealthy emphasis on social services as opposed to economic services (the focus on spending as opposed to earning - a fundamental problem of political transition which afflicts many developing countries). The concomitant increase of 15 per cent over the past two years in the servicing of government debt is alarming. Juxtaposing on this situation the actuarial under-funding of public pension funds, and the increase in the ratio of national debt to gross domestic product from 18 per cent to 55 per cent [2] in the last four years, the indication is that South Africa is falling into the developing-country economic trap of disproportionate socio-economic spending against an inadequate economic support of national production (as reflected by the GDP). If this trend continues, the country is headed for serious economic straits.

The effect of addressing the budgetary and fiscal crisis through the sale of State assets could be significant. Disposing of R50 billion of assets could reduce the debt:GDP ratio by between 10 per cent and 45 per cent , while diminishing interest on debt payments by about R5 billion per year. However, arresting the trends temporarily through disposing of means of production without appropriate allowances for contribution to socio-economic development is not a solution, as this would effectively be tantamount to flogging off the family silver.

The enhancement of the competitiveness of state enterprises. The commercialisation of Alexcor has already demonstrated major increases in efficiency. Privatisation would no doubt enhance that trend. It has to be taken into account that the existing diamond resources of the erstwhile eastern block countries; the burgeoning Canadian diamond mining industry; the demise of the civil war in Angola; and increasing South African and international involvement in Zaire and the rest of Africa present major threats to the domestic South African diamond industry. (The Central Selling Organisation as a "South African" company is also under pressure.)

Increases in efficiencies through privatisation could contribute greatly towards the overall competitiveness of the South African diamond sector.

Promotion of fair competition. There are two aspects to this. The first is the fact that Alexcor currently markets its product through the Central Selling Organisation (CSO), and it has been mooted that these contractual arrangements may be reviewed in the interests of fair competition. Sale to a De Beers dominated consortium will almost certainly jeopardise this end. However, it has to be taken into consideration that the diamond market is essentially an artificial one that is driven by the extremely successful marketing efforts of De Beers and the CSO, and that too successful an undermining of the power base of the CSO in the interests of "fair competition" could serve to destabilise the market to the detriment of the South African industry, and its contribution to the fiscus and the country's balance of payments. The over-zealous promotion of fair practice though the privatisation should thus be approached with extreme caution.

The financing of growth and competitiveness. The financing of growth can only come about at a sub-regional level through the re-investment of returns in sustainable development projects: with the arid nature of the Namaqualand environment and the relative lack of infrastructure, there is little potential for commerce and industry that is not directly related to local natural resources. As far as competitiveness is concerned, this would relate primarily to tourism and possibly limited game farming (especially ostriches) as agriculture and livestock farming on a commercial scale has little potential. The diamond-related competitiveness issues are discussed above.

At a national level, the financing of growth and competitiveness from the proceeds of the sale would depend entirely on the re-deployment of these proceeds. The sale in itself will not necessarily guarantee this.

Adherence to the values and guidelines of the government's privatisation criteria

Coherence with legal and regulatory developments. There are no obvious legal or regulatory impediments to the sale of Alexcor in whatever manner. The fact that the company has been progressively privatised through an acts of parliament and the establishment of a private corporate structure has effectively paved the way for full-scale privatisation.

Participation and protection of the interests of organised labour and employees of affected state enterprises. There is growing and expressed concern at the privatisation of Alexcor by the National Union of Mineworkers at the mine, and through the union's Namaqualand structures. These concerns need to be addressed.

The participation and enhancement of interests of the poor and disadvantaged groups. As has been frequently expressed in this document, sale of Alexcor to corporate interests will not achieve this. However, the models mooted for community participation will do so.

The participation of all other directly affected stakeholders. Between 50 per cent and 60 per cent of the inhabitants of Namaqualand arguably depend on the diamond mines. The dependency on Alexcor as such can be calculated with some accuracy in a more detailed study. In the absence of any other major economic base, the broader community of the region can thus be realistically construed to be directly affected stakeholders over and above the employees. The participation at an individual and communal level of the broader community has been allowed for in the models discussed, but again would not be achieved through corporate purchase.

Transparency of process. As the company is so important to local economic development, the choice of new owner, as well as the mechanisms for privatisation and change of ownership, along with the *modus operandi* of the privatised country needs to be established with a reasonable degree of consensus of the local community. It must be stressed that the Namaqualand community is a highly politicised and aggressive one, and that decisions of the company without due consultation would be politically disastrous.

Restructuring should be geared towards the provision of new, or improvement of existing, services to poor and disadvantaged communities. The entire community of Namaqualand outside the traditionally white residential areas in centres such as Springbok and Port Nolloth, and the residential areas of the mines, can be construed to be poor and disadvantaged. Communities such as Eksteenfontein and Leliefontein do not have even basic services such as sewerage and electricity. The profits currently returning to the fiscus, insignificant in relation to overall fiscal return, can make a huge difference to the quality of life of these communities.

Restructuring should be evaluated in terms of macro-economic effects, particularly with respect to savings, investment, balance of payments, ownership, economic growth and employment creation. The sale of Alexcor is not going to have any major impact on the macro-economic factors at any of these levels if sold as a going concern to an operator other than the State. The company is in decline, and is not going to expand to create more employment. At a national level, the balance of payments will not be affected whatever the form of ownership, as the production of diamonds will remain constant.

In this respect Alexcor is fundamentally different from Iscor. Steel is a basic commodity and an essential intermediate input into economic development. Diamonds are an artificial commodity, the sales of which are marketing driven as opposed to demand driven as in the case of iron ore and steel. Diamonds will thus not be able to contribute to macro-economic growth to the same extent that steel can.

Restructuring with respect to other forms of investment of both the capital and the future revenues from mining will dictate the extent to which savings, investment and issues such as employment creation are addressed. This has been dealt with in other sections of this document.

Sectoral approach incorporating enterprise-specific case studies. The sectoral aspects have been covered in the context of the competitiveness of the South

African diamond industry. However, in the case of Alexcor, it is the benefits that can be derived other sectors (agriculture, livestock and game farming, tourism) that are as important, if not more important than the sectoral benefit.

Integration of socio-economic imperatives is of tantamount importance. Sustainable development is the most critical of socio-economic imperatives facing the people of Namaqualand. The RDP is secondary, although important. The importance of the manner of privatisation with respect to both of these has been discussed at length here.

Restructuring should as far as possible facilitate the development of new projects that will encourage further local and foreign investment. Again, the development of new projects can optimally be achieved by retaining future returns in the region for re-investment in sustainable projects.

Direct foreign ownership should be limited, and the focus of any foreign investment should as far as is possible be associated with technology transfers. Foreign companies may have to be considered as equity or operating partners if local companies find the cultural transition to a business partnership with the community intolerable. This is distinctly likely if one considers the existing neo-colonial and old South African cultures that pervade in the major formal sector diamond mining companies operating in Namaqualand.

Conflict of interest between the public interests and private interests must be minimised. It is important here that a distinction is made in the respective contributions that the State, private sector, non-government organisations and community-based organisations have to play in the development of Namaqualand. In this context, ownership of Alexcor by a community trust would not be appropriate in that efficiency and profitability can best be achieved through private sector management. In turn, the greater the profitability of the operation, the greater the direct benefit to the community should community equity participation become a reality. Too great an interference in the running of the mine by political interests either at a national political or community political level should be guarded against in the restructuring, as this could conceivably negatively affect or even destroy the company.

By the same token, too great an influence by local individuals in the management and operation of the company could lead to corruption and hence a conflict between private and public interests, and should be guarded against in the restructuring.

Other considerations

Maximisation of existing budgetary resources. Optimisation of the use of the intrinsic financial potential of the mine inherent in both the capital sale of the mine and future returns is possible, and should be a fundamental principle of the sale and restructuring of the company. This would serve to optimise existing budgetary resources.

Mobilisation of new resources. The attraction of development aid funding, foreign or local loan funding and equity participation from the communities would give effect to the mobilisation new resources. Investment of existing capital from established South African finance houses who can well afford to purchase the company outright would not.

Provision of efficient financing mechanisms for a range of activities. The models proposed are highly conceptual, and lack an in-depth study into financial and equity structuring that would determine the ultimate feasibility of the proposals. This study is in progress.

Re-deployment of the existing resources within the public enterprises. This is contingent on the final model adopted for the restructuring.

Development of human resources. The involvement of the Namaqualand community in the direction, management and investment in the company that would be facilitated through the community participative models proposed here would serve this purpose far more effectively than an industry standard affirmative action policy that would in all likelihood be adopted should the company be purchased in its entirety by an existing mining company.

Conclusions

The above analysis may be crystallised into the following conclusions:

- It is imperative in the light of the downscaling of the diamond industry, and the economic and environmental disaster that could be precipitated by this process, that the privatisation of Alexcor be managed in such a fashion that future returns may be harnessed to provide for sufficient sustainable economic development to offset the effects of mine closure in the next two decades;
- The sale of Alexcor to interests outside of Namaqualand, be they mining houses based in Gauteng or the Western Province, black owned or white owned, will have little or no benefit to the people of Namaqualand;
- Sale of the company to outside black capital interests will merely serve to support affirmative action in other areas, and the accumulation of black capital, but will not directly serve the interests of sustainable development whether inside or outside the region;
- The sale should thus be managed in such a way that the ownership by the aboriginal people of Namaqualand is facilitated and provided for in such a manner that there is predominantly a communal benefit, but that there is scope for individual equity participation;
- Because of the nature of the people of Namaqualand, models that do not allow for participation by the aboriginal peoples of the territory are likely to lead to long-term conflict and political instability in the region;
- The question of "wider ownership" needs to be redefined in terms of percentage shareholding rather than number of investors;
- Employee equity participation was inadequate in the case of Iscor, and needs to be a serious consideration in the privatisation of Alexcor; and
- Privatisation should cater for new investment and not recycling of the existing institutional financial resources as happened in the case of Iscor.

Recommendations

It is recommended on the basis of the conclusions drawn that:

- The proceeds from the sale of Alexcor report to the central fiscus in order that the nation as a whole can benefit, but that the sale be based on a model that will ensure that the ongoing revenues remain within Namaqualand and be utilised to contribute to the sustainable economic development of the region;
- The sale ensures the active participation of the Namaqualand community, individually through the appointment and development of management and direction from within the community, as well as scope for individual equity in the privatised company;
- The sale benefits the inhabitants of Namaqualand communally through the bulk of the equity being investment of the proceeds in other commercial ventures;
- The sale of Alexcor to Namaqualand interests should not benefit only individuals within the community as has happened with past allocations of mineral rights;
- Due diligence should be exercised to ensure that individual aboriginal investors are not fronts for

white interests as has happened in the exploitation of mineral rights in rural reserves in the past;

- In order to achieve the benefits as discussed here, that a resource development company be established as a vehicle for community participation and reinvestment in sustainable development;
- This vehicle provide for both communal return and individual equity participation;
- The vehicle be funded through a blend of development aid, loan capital, corporate and individual investment;
- The direction and management of the vehicle be such that community interests are protected without jeopardising the professional management or profitability of the company;
- The restructuring of the company be undertaken in such a way that private interest, corruption and undue political influence does not undermine the efficient operation of the company;
- A greater degree of employee equity participation needs to be considered in the case of Alexcor;
- "Wider ownership" should be effected in terms of greater shareholding by previously disadvantaged people, not in numbers of people;
- Caution should be taken not to entrench institutional ownership, and hence the ownership of the means of production, in existing capital interests, be they black or white - it should be used to create new stratas of institutional and individual ownership; and
- As national interests will be catered for in the returns from the sale whoever purchases the company, the longer term contribution of the company to the socio-economic, political and ecological stability of region take precedence over national interests in the sale and restructuring of Alexcor.

Notes

[1] Schlemmer, 1995. World Averages calculated by E Calitz of the South African Department of Finance.

[2] Financial Mail 8 September 1995. ■

...continued from page 12

Annex 3. Current management agreement tenders[1] (oblast, name and location)

Atyrau oblast– 1 object
1. Petrovsky Plant, Atyrau

Almaty – 3 objects
2. JSC "Hidromash", Almaty
3. Almaty Margarine Plant, Almaty
4. Almaty Tea Factory, Almaty

East-Kazakstan Oblast– 1 object
5. JSC "Ust-Kamenogorsk Condensat Plant", Ust-Kamenogorsk

Karaganda Oblast – 2 objects
7. JSC " Corbit", Temirtau
8. JSC "Karagailinsky GOK, Karagaily
9. Karaganda Margarine Plant, Karaganda

Kokshetau Oblast – 1 object
10. Plant for production of oxygen apparatus for breathing, Kokshetau

South-Kazakstan Oblast – 2 objects
11. JSC "Plant of Ispolnitelnykh Mechanisms", Petropavlovsk
12. Kirov Plant, Petropavlovsk

Taldy-Korgan Oblast – 2 objects
13. Lead-Zinc Combinat, Tekeli
14. JSC "Kazaccumulator", Taldy-Korgan

West-Kazakstan Oblast – 2 objects
15. Plant "Metallist", Uralsk
16. Plant "Hidropribor", Uralsk

South-Kazakstan Oblast – 2 objects
17. JSC "Achpolymetal", Kentau
18. JSC "Techosnastka", Turkestan

Note: In all cases Initial Price and payment period enterprise debts payables till January 1, 1996.