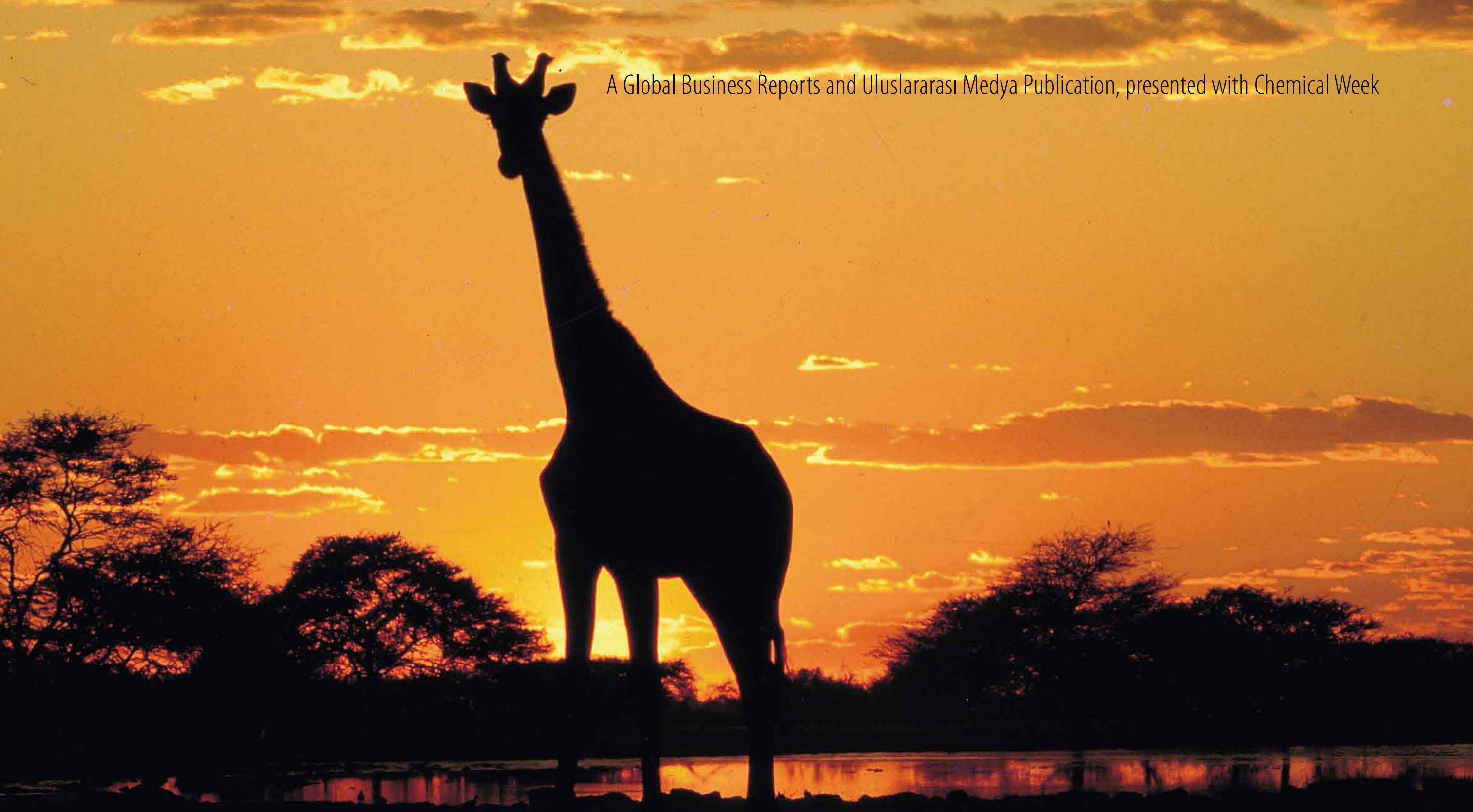


South Africa:

A crossover from inward thinking to a global outlook

This report was compiled by Global Business Reports after meeting with many of the key players in South Africa's chemical industry. It looks at efforts to add value to South Africa's considerable resources, find new markets for an export-driven economy and maintain a responsible approach to manufacturing. Authors are Marco Peralta and Anna Stark.

Twelve years after the country's first democratic elections, South Africa has made great progress in dismantling its old economic system, which was based on high tariffs, subsidies, anti-competitive conduct and broad government intervention in the economy, and has witnessed a remarkable turn around in its social fabric. Reduction of crime through the creation of jobs is a key force in driving the higher levels of economic growth required to achieve South Africa's aim of halving poverty and unemployment by 2014.

Consumer demand has been the main driver of consistent growth in Africa's biggest economy over the past couple of years, spurred by the lowest interest rates in more than two decades, low inflation and an emerging black middle class. South Africa is considered an increasingly attractive destination for investment and tourism.

While South Africa boasts infrastructure comparable to developed countries, its cost structure is distinctly third world. At around 1.70 US cents per kilowatt-hour, it has one of the cheapest electricity costs in the world. Labour rates are also competitive, although rising due to the lack of new young talent and the "brain drain" characterized by the emigration of highly skilled people to Europe, the United States and Australia. South Africa has an official unemployment rate of 26%, but it is believed that the number of people without formal jobs could be as high as 40%. Thorsten Iske, Managing Director BASF SA & Sub-Sahara appreciates the direct and indirect importance of investing in South Africa: "I wish industrialized countries would take more interest in Africa in terms of opportunities for economic growth and social political necessity. There is a direct adverse effect on those that do otherwise"., With BASF posting roughly 228 million dollars in sales last year and double-digit growth for the past three years running, Iske has a positive outlook for the future.

BASF is not alone in its optimism and belief in a bright future for the South African market. There are several sectors pushing growth, a good example being the automotive sector, which is of particular interest as one of South Africa's leading industries. Roughly 500K units per annum are produced with potential to rapidly increase this figure. Chemicals companies are tapping into this growth supplying coatings, plastics and chemicals for paints, interior parts, break fluids and antifreeze to name but a few components. Local research and development companies capable of global developments are also experiencing strong performance. Karbochem is a clear example of such, having developed in-house technology for high performance tyres. Dr. Abraham Brink, Executive Director of Karbochem (Pty) Ltd, shares the details of their technology: "We have developed 3,4 polyisoprene rubber. The market is small (about 3000 tons worldwide) but it is the best rubber in the world for enhancing the wet-grip properties of tyres. We see all major tyre manufacturers in the world slowly attracted to our technology." This example highlights the potential South African companies have to compete on a global level. Other prominent technological developments include Sasol's unique liquid-to-gas methods that are currently being sold to China with other major gas producing countries showing increasing interest.

"Consumer demand has been the main driver of consistent growth in Africa's biggest economy over the last couple of years as it witnesses the emergence of a black middle class"

Although South Africa is increasingly confident of its position on the world stage, there are still major challenges ahead to be overcome in order to remain competitive. Companies such as Chemical Services Limited (Chemserve) have restructured their operations to better compete with extremely flat and efficient organizational structures. A subsidiary of AECI, one of the largest groups in the country, Chemserve is a group of twenty-two chemicals related companies operating in diverse sub-sectors across South Africa. Each company offers a full service package of products, services and knowledge to their customers and manages their own core activities. "One area where we believe we have global expertise is mining chemicals. We took all the learning we have gained in our local South African market and bundled it into one applicable mining service package that is then tailored to specific needs. Under that model we are now well established in South Africa and are quickly moving into Zambia. If we get the opportunity to enter other markets with similar mining profiles in particular South East Asia and South America, we will take it" says Frank Baker, Managing Director. Chemserve is one example of how South African companies are adapting to the competitive international environment and demonstrating to the global investment community the country's potential to compete.

Sasolberg, South Africa

" South Africa boasts an infrastructure comparable to developed countries, but its cost structure is distinctly third world."

A major hindrance to attracting new investment are the negative perceptions that Africa evokes of corruption, high crime levels and political instability, perceptions that South Africa is desperate to change. In reality, the country is an emerging market with an abundant supply of natural resources and well-developed financial, legal, communications, energy and transport sectors. Legislation dictating local ownership, employment equity, preferential procurement and corporate social investment is key in integrating previously disadvantaged people into the economy, but at the same time could discourage FDI if not implemented correctly. Whilst still remembered for it's former racial discrimination, the general consensus however, is that South Africa is currently regarded more favourably as an investment destination than ever before. The following report, researched over a period of two months spent interviewing leading chemical executives in South Africa, attempts to communicate the realities of doing business in the South African chemical sector today.

Contract Manufacturing and Distribution

A springboard to the African continent

Opportunity and risk in a delicate balance.

South Africa is already a natural regional hub given the size and importance of Durban, the largest and busiest port in the Southern Hemisphere. Although many companies retracted manufacturing installations during the apartheid era never to return, others have since made long-term production investments. Easy access to the international port of Durban and a substantially developed road infrastructure makes for easy transportation of raw materials and the export of finished products. The South African market is not a particularly large one with a population of 45 million, but economic indicators point at steady growth for at least the next few years. Other parts of the continent are also beginning to show signs of economic and political stability unheard of in the past. Africa is becoming an increasingly interesting market for foreign companies. A viable option for international players wanting to enter the African market without heavy investment into the development of infrastructure and distribution chains is third party manufacturing and distribution.

Crest Chemicals, a Brenntag – Chemical Services joint venture, are positioning themselves as a reliable source of next day delivery for both commodities and specialities. “We are an extension of the manufacturing arm for companies in diverse sectors. We are always looking for new suppliers mainly in the food, oil & gas, paint coating and pharmaceutical industries to bring their products to South Africa. We have warehouse facilities in the five main areas of the country; Johannesburg, Cape Town, PE, Durban and East London . We have packaging facilities in Johannesburg and Durban and a solvent, blending and packaging facility on the shell refinery site” indicates Michael Vijverberg.

The pharmaceutical sector in particular has become highly regulated through Government intervention in recent years, with new, inhibitory legislation lowering the incentive to manufacture locally. Richard de Chastelain, Country Division Head of Healthcare of Bayer South and

East Africa explains: "In general, companies don't see investment in local production as viable. Our company imports 100% of our products from Germany at present , having closed local production a number of years ago. Based on the current regulatory environment, with more changes to come , there is limited incentive for multi-nationals to commit to local manufacturing. Legislation favours generic houses through mandatory substitution of the original scripted item at Pharmacy level. Thus while at present South Africa remains a reasonably favorable market for originator medicines , the future landscape appears uncertain. Nevertheless most companies remain committed to contributing to the huge healthcare challenges that the country faces and I believe will remain so in the future." In 2002 Bayer retracted its manufacturing operations from South Africa but has clearly enjoyed more than satisfactory returns from remaining present in the market.

In order to capture international investment and products, various companies offer their manufacturing, distribution and administration capabilities to maximise capacity and efficiency. Sandoz, a leader in the multinational generic pharmaceutical sector is one such company. Their NCA and World Heath Organization certified manufacturing site holds capabilities to produce at the highest international standards. CEO, Lynton Lomas, extends his invitation to potential alliances: "Besides manufacturing, developing, distributing and marketing for ourselves we offer third parties certain avenues and opportunities for manufacturing and entering the South African market. We have just appointed a national export manager to take care of further developing other African markets such as DRC, Nigeria and Angola. Nothing prevents us from entering into a manufacturing trade situation with a feasible partner. There is a world of opportunity for developing such relationships". Sandoz currently dedicate 20% of manufacturing to licence agreements.

One of the largest South African based privately held chemical, manufacturers and distributors in the country, the CHC Group, made up of six independent subsidiaries, has enjoyed successful growth through manufacturing partnerships. "We have just acquired a manufacturing site from Dow Agrochemicals which we are going to convert in order to produce for the construction and mining sectors. We also have powder plants, a solvent plant, emulsion plants, tank farms and packaging lines from 25 litres down to 1 litre at a rate of 7,500 litres per hour. For the moment we have idle capacity and so welcome partners who want to take advantage of our facilities and local knowledge", says Group CEO Neil Hellmann. The CHC Group and BASF/Elastogran recently merged their polyurethane businesses (CHC Urethane Products and Elastogran) into a joint venture company, called CHC Elastogran. In a steadily growing market, the CHC Elastogran joint venture will allow the CHC Group to be in a better position to respond to the changes and opportunities in the market. CHC Elastogran will have the advantage of having direct access to essential raw materials. This, along with the combined R&D technological capabilities of its partners, will place the company in a strong position for new partnerships and growth into the future, claims Hellmann.

Today, the country is capitalizing on present opportunities promoting an open market that is attracting international investors and is solidifying trade with other African nations insuring their place as the regions hub and a springboard to the continent.

Agrochemicals

At the root of prosperity

South Africa exported agricultural produce worth nearly USD 3 billion in 2002-04, which constituted almost 9% of the total value of national exports.

Whilst fully aware of the economic and social havoc land redistribution can cause, South Africa also recognizes the necessity that land ownership better reflect the demographics of the population. This requires a smooth transition of land from white commercial farmers to black emerging farmers to ensure the sector's future stability and prosperity. A lack of know how is recognized as the major obstacle to achieving this, a concern not exclusive to the agricultural sector. Omnia Group Managing Director, Rod Humphris believes the land transfer will fail without direct support; "As a farmer you have to be a business person. If you are sitting on the tractor you have got it wrong for sure. We are a company serving three distinct markets: agriculture, mining and chemicals. One area we feel we can contribute to quite strongly is the agricultural sector, where we can play a more than important role in assisting future commercial farmers. Farming today has become far more technical and business orientated. You have to understand markets, financial derivatives and sophisticated tools such as GPS technology for precision farming. Then consider emerging farmers who do not necessarily have these skills and have to compete with others that are performing on a much larger scale using all the latest techniques. There are many stories of land which has been transferred to untrained farmers, with the result that a year or two later the farm has substantially failed. On the other hand, we have certainly seen some successes, which normally involve technical assistance from somebody. I think it's a perfect opportunity to have stacked private partnerships to reduce risk and assist the various players to overcome difficulties". Clearly assistance in shifting land ownership with minimal negative impact to output and quality is welcome, and offers an interesting area where agrochemical companies can position themselves for growth.

Plaaskem an R&D based company, and a leader with roughly a 25% share of the innovative agro-chemical market, offers complete farming solutions. Alongside their product offering of herbicides, pesticides, fungicides and nutrition, the company positions itself as a one-stop-shop farming service center. Plaaskem's objective is not to sell one-off products, but rather to become involved in helping the farmer increase yields through the design and development of complete crop programs, technical backup and project financing. In the words of Managing Director, Hugo Minnaar, "The key is to provide farmers with a solution to the problems they might have on a product and knowledge level". Their supporting formulation and trial facilities ensure that farmers can resolve problems quickly and efficiently.

Internationally, the recent development of agricultural produce in the production of alternative fuels holds exciting potential for the South African agricultural sector. Ethanol, or ethyl alcohol, is on its way to trading as a mainstream world commodity, as soaring prices for crude oil and gasoline and rapidly depleting fossil-fuel reserves incite a push towards "green" fuels, produced from renewable resources such as sugar, corn and soybeans.

Villa Crop Protection, the leading domestic generic agrochemical company, with approximately 19% share of the local market, is keen to see South Africa join this global development and reap the benefits of alternative fuels. Jos Dujardin, General Manager, enforces his conviction in bio-fuels: "We are absolutely confident that maize will be converted into ethanol at a substantial level in this country in the near future. It will stabilize the agricultural market and increase the acreage needs. Ethanol can be produced economically given the percentage limitations of fuel blends. This is going to happen. The government has already stated a commitment to it. Sasol, a South African company, currently produces approximately 40% of local energy demand from coal and gas. Sasol believes we can increase energy self-sustainability from 40% to at least 50% through bio-fuels. The development of these fuels will no doubt help grow the agrochemical sector.

Pharmaceuticals

Balancing healthcare and profits

New legislations could be a double edged sword.

South Africa (SA) has been implementing a substantial amount of new legislation that affects all industries. The pharmaceutical sector in particular has been forced to cope with a considerable amount of regulation covering price interventions, dispensing fees, a new health charter and a prohibition on distributor bonuses and kickback's. A further challenge is the increasing competition from Asian generic products, as is the case internationally. In response, multinational, national, generic and innovative companies have been reshaping both strategy and structure to comply with the wave of new regulations in order to remain competitive.

Regardless of time, effort and resources allocated to following and adjusting to regulatory changes, the sector is performing well, posting strong growth across the board according to Deon Vos, local CEO of German pharmaceutical and chemical group, Merck SA. "In order to compete successfully in our market you need to be quite nimble and preferably present in the innovative, generic and consumer healthcare markets as Merck has done. On the one hand, legislation can hamper business on the pharmaceutical and the Black Economic Empowerment (BEE) sides, but if you are clever, enthusiastic and believe in the country you will have a successful business. Despite the challenges, our pharmaceutical division has posted double digit growth of between 15-20% for the past few years, as low-income medical aid schemes, the rise in generic drugs and economic growth in general have created millions of new customers". As the South African economy continues to perform with an average growth rate of 4-5%, a large emerging black middle class is expanding the size of the market. It is estimated that 7 million people pay for private care. For the rest, the state provides care, though sometimes involving tedious waits. The state is keen that the private sector remains affordable so that the patients in that sector do not fall back on the state for care. The intention is to bring more patients into the private sector at a lower cost level. For the past five years or so, the government has taken initiatives to force down prices and promote generic substitution; in the opinion of some, a limited short-term approach.

The most notable price regulation that the government has implemented is the 'single exit price'. For the past three years, pharmaceutical companies have been barred from raising prices, which remain fixed at their 2003 values. Estimates from the Pharmaceutical Manufacturers Association (PMA), one of the two industry bodies representing innovative companies, suggests growth has been restricted due to regulations. Vicki Ehrich, COO, explains: "Previously prices were set and companies discounted off that price. Now you have to take out all discounts and give a set net price. Consequently, pricing came down and we had a 21% drop in market value. Since then there has been minimal value and volume growth. The 'single exit price' (SEP) is phase one, if we include the elimination of bonuses, discounts and incentives to whoever can influence the use of products to patients. Phase two, which is what the government is now working on, is the benchmarking of prices with international mediums, because of the perception that we (SA) are highly priced when compared with the rest of the world. We have submitted our views on how the benchmarking should be done and will know the results by the end of the year. We don't expect that new products will be affected as they are launched at a fairly similar price around the world. In the case of older products, prices have most likely crept-up as they have not been subject to the regulatory environment in the past". Ehrich believes: "that our prices are competitive by world standards and therefore if our methodology is accepted it would give further modest reductions on the SEP and give confidence that South Africa is not out of line with international standards." The area of concern for the official study is which countries will be included in the benchmarking basket. The selection of counties chosen as the medium will obviously affect the results. The dilemma lies in the fact that South Africa's pharmaceutical sector meets first world standards in terms of the quality of medicines, but sells to a third world economy, hence the discrepancy. The general feeling amongst pharmaceutical executives is one of confidence in the government's ability to integrate private sector concerns in the process. When first considering the 'single exit price', the government suggested a staggering 50% reduction in prices. The figure was revised after submissions by both representative associations, the PMA and Innovative Medicines South Africa (IMSA).

The theory behind price reduction has two estimated parallel effects. Firstly, enforcing a more affordable price will increase accessibility to drug care, and secondly, it is estimated that volume will offset loss in value for pharmaceutical companies. GlaxoSmithKline (GSK) one of the global industry leaders, with an estimated seven per cent of the world's pharmaceutical market has already taken the initiative to reduce its prices in South Africa. According to Mustapha Karim El Alaoui, General Manager for GSK Pharmaceuticals SA: " In February this year, GSK identified the need to make some of its key medicines (two of which still enjoy patent protection) more accessible to patients in South Africa. This decision was taken in order to see more people benefit from our high quality medicines. I am confident that GSK has made the right decision to cut prices substantially. Yes, we see the effects on profits per unit, but at the same time we see our volumes growing with a larger market. We will have to see the final balance in the future". As is the case with most pharmaceutical industries, industry associations play a pivotal role in aligning companies with local pharmaceutical issues. Both the PMA and IMSA have a huge concern about potential further measures.

Val Beaumont, Executive Director of IMSA, explains; "The medicine pricing regulations provide for the development of further price reduction mechanisms – so-called reference pricing. It is not yet clear which of the possible approaches to reference pricing will be adopted by the government. Internationally, governments follow reference-pricing policies but these are backed up by guaranteed reimbursement. Once a final price has been agreed with the government, patients have the assurance that medicines will be funded for either by the government or by medical schemes. Such is not case in South Africa where medical schemes still have the right to refuse full or partial payment for our medicines. A reference pricing system without the eventual assurance that patients would have access to our medicines is of serious concern to us'. At the same time Beaumont is confident in the government's ability to take account of the issues and needs of the private sector; "We have been heard by the government to a certain extent and there has been an openness across the board, particularly with the Heath Charter. An initial Department of Heath proposition of 51% mandatory local BEE ownership for all pharmaceutical companies was negotiated and brought into line with the Department of Trade and Industry (DTI) target of 25% black ownership. Regardless of the compromise reached, many multinational companies cannot give away equity due to their global corporate structure, hence the need for alternative solutions. One such alternative currently under consideration is the possibility for companies to fund public health projects, their contribution equating to the BEE benefit flowing from the sale of a 25% share holding in the company. This fund would then be invested into training doctors, nurses and improving access to healthcare in general. This serves as an example of how the government is listening to the private sector. All of our members are supportive of the funding proposals so far. We will see what the final document looks like at the end of the year".

Companies are waiting in anticipation for the final results that will clearly influence their current and future investments in South Africa. As Maturin Tchoumi, CEO of Roche South Africa, reiterates: "I do fully understand the need for transformation in the country by bringing previously disadvantaged people into the mainstream economy. It really is a noble intention. On the other hand, the cost associated with compliance weighs heavily on our operation. Equity ownership is a challenge for us because it is not in our business principles to enable ownership of our subsidiaries in the countries where we operate. We have clearly stated that we will not give up equity in South Africa. Twenty years ago we had to offer equity in certain markets such as India and China because it was a business requirement. We are currently looking at buying back that equity. If ownership becomes mandatory we will have to evaluate our position and take an appropriate decision". Tchoumi's sentiments and Roche's stance on ownership are shared across most of the multinational community. Presently, efforts are being focused on the other pillars of BEE (Broad Based BEE) such as employment equity, preferential procurement and corporate social investment in order to contribute to the countries objectives and accumulate points for their BEE scorecards. Pharmaceutical companies in particular have incentive to rank high on the BEE scorecard, as the government pays strong consideration to BEE ranking when awarding public tenders, with a knock-on effect that will influence the purchasing patterns in the private sector, hence its importance to companies bottom-lines.

The emergence of BEE certified companies such as Biotech Laboratories, Sisonke Pharmaceuticals and Batswadi Pharmaceuticals, provides much needed options for BEE partners / suppliers. While participation in BBBEE is voluntary, a business' BEE status/score becomes an important factor when doing business with government (e.g. tenders, licensing, etc.) or with other businesses (e.g. medical schemes / health insurers, wholesalers, hospitals, etc). Businesses with a good BEE status/score will have an advantage over businesses that do not participate in BB BEE.

Reuben Mawela, Director and Sales Manager of Sisonke sees embracing South Africa's economic equality initiative as fundamental to doing business in the continent. "Sisonke's operation as a broad based BEE company have shown interesting profit margins, certainly driven in part by our status. Sooner or later you will not be able to compete in our market, or Africa for that matter, without proving social responsibility and investment by empowering locals". Some companies have been slow to implement BEE as it has only been a draft to date, but as the proposal is before Cabinet, BEE will become a way of doing business sooner rather than later. Voluntary participation by all will be encouraged by the ultimate ability of a company to win tenders. When that situation arises, companies that have embraced and implemented change will have a substantial competitive advantage and will be seen to be part of the solution, at least in the eyes of the government.

Christopher Whitfield, an American citizen by birth, has understood both the opportunity and necessity of BEE in South Africa. After a 17-year career with El Lilly, including a five and a half year posting in South Africa, Whitfield has launched Batswadi Pharmaceuticals, a biotechnology company dedicated to diagnostic tools, human devises that enhance the body's ability to work, and innovative products that enable systems within the body to deal with existing conditions or emulate future ones. "Black Economic Empowerment in this country is on the go. Companies are going to have to become more diversified in terms of ownership, leadership, etc. I saw opportunity in the lack of innovation and lack of able black empowered companies to take on biotechnology work. I think the general perception around the world is that Africa is a fairly unsafe, risky place to do business. As a fully BEE accredited company, I want to communicate to those individuals who have this type of technology, that we can be their representatives in South Africa and Sub-Sahara until they are ready to enter the market on their own. My tip to those contemplating entering the market is: come in understanding the rules of BEE, as they are fundamental, be ready to fully commit to corporate social investment programs – in my opinion they must be focused on training and development - and lastly, take a long-term strategy for your investment – 5 to 10 years".

In addition to local legislative complications, companies also face stout competition from generic imports from Asia, (mainly India and China). Sandoz, a Novartis company, is a world leader in generic pharmaceuticals. They have positioned themselves in the chronic 'hard to make' market and are ready to defend it against lower quality imported products. As Lynton Lomas, CEO, outlines: "We have warned some companies that we will do impurity tests here. We have the laboratories in place and are quite happy to take a competitor's drug and test it. If we find that there are impurities we will make it known. At the end of the day we differentiate ourselves on quality and so we will challenge people on it. The policing system in place here could allow for inferior batches to come through. We have spent a substantial amount of money on developing drugs and educating people on the benefits of our drugs, so we are not prepared to lose our market and investment to inferior drugs". Lomas believes the current market conditions are not ideal and evaluates competition as intense, but has a very optimistic outlook for companies providing quality products with maverick ideas.


Sandoz Lab

If compared with the innovators, Sandoz and other generic companies may not face the same difficulties. In line with the objective of affordable prices for a larger portion of the population, dispensers are obliged by law to offer patients a generic option for treatment whenever one is available. Furthermore, in the opinion of many, the government is also showing a trend towards awarding tenders on price rather than on the cost / benefit ratio of international standards and pharmaceutical research for basic medical schemes and reimbursements.

According to IMS statistics the South African private pharmaceutical market has grown 8% between July 2005 – 2006, driven in large part by generic companies. A combined public / private effort will be needed to ensure that adequate legislation is in place to benefit patients without restricting current and future investment. As is the case for all other sectors in the South African economy, a long-term investment into social and economic equality will in the long run grow the available market size and hence benefit everyone involved, or so it is assumed.

Black Economic Empowerment (BEE)

Tackling social and economic disparities

According to 2005 World Bank figures, South Africa is ranked 19th in terms of PPP – GDP in the world. The country has a population of 45 million: black African 79%, white 9.6%, coloured 8.9%, Indian/Asian 2.5%. Of the total population only 7-8 million (16%) people are considered to be in the mainstream economy. The wealth and power base is still held in a large part by whites, a situation that has slowly began to shift in recent years. Black Economic Empowerment (BEE) is a unique program. It is a joint public / private initiative that is being integrated into economic legislation and its understanding is fundamental to doing business in South Africa today.

BEE was conceptualized to counter the marginalizing effects of the apartheid era where blacks were disempowered economically, educationally and socially. BEE has two major aims: the deracialising of ownership and control of South Africa's economy, and to financially affirm the historically disadvantaged majority. The underlying BEE initiative is broadly accepted in the business community; the critical issue on hand is effective implementation, in other words adding value to the economy and both maintaining and increasing incentives for both foreign and domestic investors.

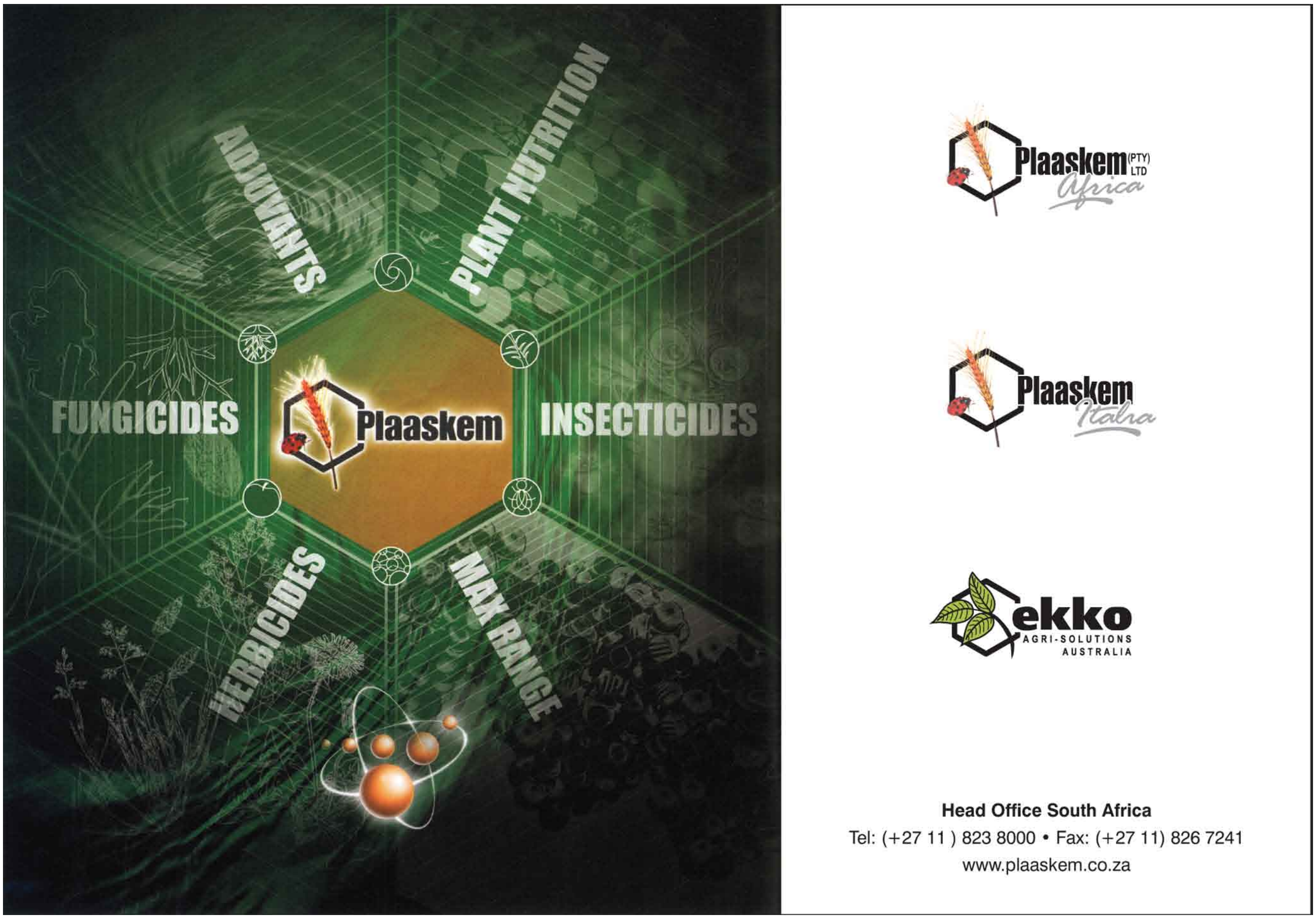
Since the inception of BEE in 1993, the 'across the board' results have been mediocre. It is evident that a small group of ambitious people from the previously disadvantaged group have accumulated a vast amount of wealth. In response to the results the Black Economic Empowerment Commission released a landmark report which affirmed a broad-based approach to BEE (BBBEE), that is, a change from the exclusive focus on ownership to other elements such as employment equity, skills development, preferential procurement, enterprise development and corporate social investment, amongst others. The report was the foundation for the government's current BEE Strategy document (2003) and the Department of Trade and Industry's code of good practice second phase (2005). The devised BBBEE scorecard gives each company points according to the level of integration in each of the areas. BBBEE is seen by the private sector, and multinationals in particular, as a more realistic and beneficial approach to supporting the country and its objectives. Thorsten Iske, heading the South African and Sub-Saharan branch of the largest chemical company in the world, BASF, reiterates the point; "I think the BBBEE approach is an intelligent one. Ownership is only one area; there is also skills development, enterprise development, preferred BEE suppliers and corporate social investment. These are areas where companies can make a difference and contribute to the development of this country. I am personally convinced that investment into enterprise development, suppliers and especially skills development is the right way to bring South Africa forward. That does not mean that ownership is a no. When we see added value in having a partner in any industry, no matter where they come from, we discuss it and consider it seriously. So, BEE ownership is not a no-no issue but neither is it a yes-yes issue".

For many multinationals, namely in the pharmaceutical sector, the sale of equity is not an option that falls inline with their global structure. Regardless, the value of BEE deals in South Africa reached their highest level ever - R56-billion (7.3 billion USD) - in 2005 even though the number of BEE transactions dipped slightly, from 243 in 2004 to 238 in 2005.

Some sectors are in more advanced stages of their respective charters and hence in the degree of BEE implementation than others, as Morvin Subban, General Manager of Shell Chemicals South Africa, explains: "The liquid fuel charter was a pioneer in BEE. Currently it will not recognize any other element of the BEE scorecard unless 25% of equity is in the hands of the previously disadvantaged. It is something we must live with and so that specific area of our company is now in negotiations with a black equity partner".

Henkel South Africa has recently completed their transaction of a 26% sale of their equity to local company Vuya Investments. Managing Director Michael Zipp was quick to adapt to the local trends: "When I came to South Africa in 2003 we realized that we had to address the BEE issue because there was mounting pressure from our multinational customers who would not sell shares and hence were trying to score in other areas of the scorecard, for example preferential procurement. They want us to be empowered. We ended up teaming up with a woman based BEE investment company because we did not want to go with 'the usual suspects'. BEE is working for us. It is not just about attracting more business; we want to integrate as much as possible. So, all in all BEE works for Henkel and we will be investing time and energy in further improving our scorecard". Taking Henkel as an example, the preferential procurement side of BBBEE is seen to be working with the desired trickle-down effect.

Some companies such as Huntsman – Toxide have strong global social corporate cultures that help to naturally integrate BBBEE. Huntsman prides itself in its social and environmental initiatives ranging from local community development to AIDS care. "On the health front we have done a lot of work around the management of HIV-AIDS in the workplace as it is a key challenge for South Africa. We embarked on an anonymous testing for which we had a turnout of 91% of our workforce. This was unheard of and in fact caught the attention of the Global Heath Initiative (UN). Although HIV-AIDS has a minimal direct impact in our organization, we are currently engaged in a strategy focusing on preventing new infections and supporting those infected. We have also shared this initiative with our customers and suppliers. We are quite proud of our effort on this front. We have a major issue with the lack of education in this country so we have put our efforts to contribute in this area. To date Huntsman – Toxide has built roughly 240 classrooms in semi-urbanised and rural communities benefiting 11,000 learners. We have also installed supporting infrastructure such as electricity and water. Social responsibility is very ingrained in our company. John Huntsman, the chairman and founder of Huntsman, is one of the most renowned philanthropists around. He has personally given away half a billion dollars of his personal savings to social causes". Education is one the largest



challenges for future growth in South Africa and one of the key areas most multinationals are contributing to.

As there is a lack of talent in the country, especially amongst the previously disadvantaged group, poaching individuals is not uncommon. Companies find that investment is often made in training individuals to later loose them to larger companies offering higher wages. Michael Zipp from Henkel finds himself in such a position not for the first time, "For companies that are not scoring in other areas, employment equity is a must for their scorecard. They are prepared to pay a salary premium. With 280 employees we are not a large player in South Africa. The Sasol's or large automotive companies can afford to employ more of these candidates and even warehouse them We can't afford to do so. We had the same situation in China years ago. When I went to Mainland China from Hong Kong we were fighting for the few talented English speaking people available. In the beginning the Hong Kong Chinese were the ones who were highly valued but wanted double the standard salary. Today, after more than 15 years there are enough Mainland Chinese available to replace the Hong Kong Chinese. I see the same happening in South Africa."

It is fundamental having corporate support for the initiative if change is to take place. Stavros Nicolaou, Senior Executive for Strategic Trade at Aspen Pharmaceuticals, summarises his conviction: "It's about getting the balance right. If you give up to much to BEE you could get into the situation whereby you don't get the growth needed and hence are globally uncompetitive. If you lean too much on the other side, not helping to invest in previously disadvantaged persons, then we will not have a stable democracy. That is the decision that any astute businessperson has to make, and they have probably made it already. Obviously, if the business community invests in making the market grow from 8 million to say 14 million, it is going to benefit any business in the long run. We'll take some short-term pain for some long-term gain. For me it's not a choice, it is very clear. BBBEE is not the perfect concept but it is the best model I have seen." Ernst & Young director Dave Thayser thinks BEE is one of the biggest drivers of corporate activity in South Africa's economy, adding that the BEE process is maturing, with BEE deals becoming more broad-based and increasingly involving women's groups.

A joint effort at a national level is needed to shape the way forward taking into consideration profitability and shareholder return as well. The general consensus is that the future stability of the economy, as well as the general wellbeing of its people, will be critically hampered – to the impairment of all South Africans – if the majority of its people are not included in the mainstream economy. It is essential for the government to fully accept the roll of a facilitator of the process while the private sector must embrace black people to participate in business. Resolution on the BEE codes of good practice and other regulatory issues would remove a degree of current uncertainty in the business community. For new entrants into the South African market a long-term successful business equals a long-term commitment to BBBEE. BEE should benefit the disadvantaged, but investors can also benefit from an initiative designed to heal the nation.