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State localisation procurement decision is irrational

Dimakatso Leshoro
City Press

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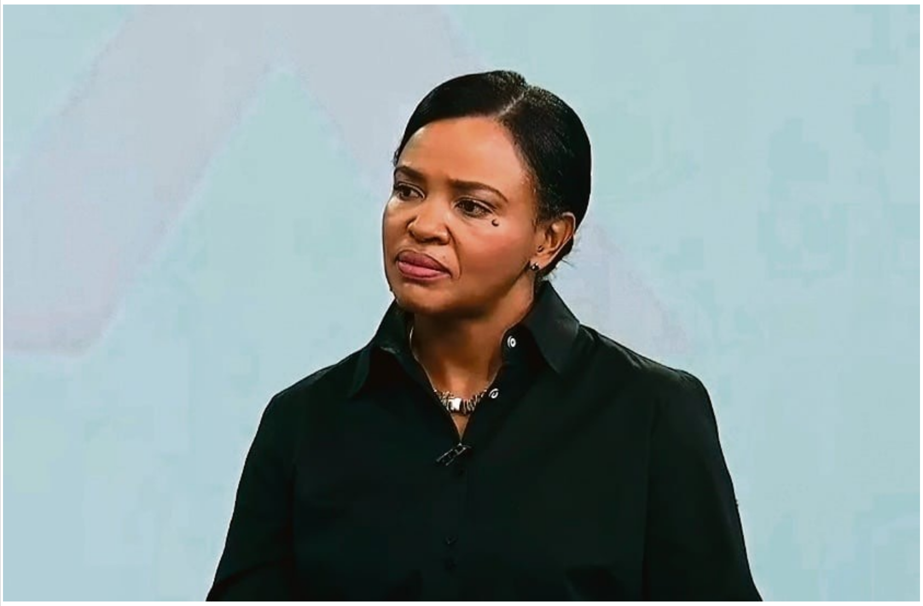

Transnet CEO Portia Derby said some local procurement requirements imposed on state-owned enterprises were onerous and to their detriment. Photo: Ngampol Thongsai, EyeEm.

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BUSINESS

Government's procurement decisions are irrational and nonsensical, according to Dr Stavros Nicolaou, a member of the SA chapter of the Brics council and senior executive at Aspen, one of South Africa's largest pharmaceutical manufacturers.

Speaking at a recent **Black Business Council summit** in Johannesburg, Nicolaou lamented what he described as the shortsightedness of government officials who did not consider the full impact of procurement decisions on creating demand in the country's lacklustre economy, but instead settled for minuscule savings.

He cited the example of the importation of some pharmaceutical products as the result of illogical pricing decisions, at a time when government sought to drive industrialisation through localisation.

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"Instead of looking at what constitutes best value for money, we say we're saving R1 per pack because we're importing it from India, but we forget that we're losing R3 per pack in multiplier impact back into the economy. It doesn't make sense.

"Unfortunately, there are departments in our country – not only in my sector, but across the board – taking such irrational procurement decisions.

> **Has the department or ministry done an impact assessment on the economic multiplier effect back into the economy before making that decision? The answer is 'no'.**

"For every R1 procured in the public system for antiretrovirals, you would add R0.32 back into the economy if you produced the product locally. If you had paid R0.32 more, you would have been in a fiscally neutral position, yet the decisions taken in these departments are based on being heroes by saving R1 while losing R20 million of economic activity. It's nonsensical," said Nicolaou.

Trade and Industrial Policy Strategies executive director Saul Levin pointed out that part of the problem was that the **industrialisation** policy was not properly funded. There was a misalignment between government's policy and budgets allocated to departments, he said.

This had been a large part of the debate about whether localisation could work in the country, with some analysts calling localisation projects nonsensical.

"We can't just say localise without changing key processes and systems within the way government does its procurement and budgeting. There must be planning around this.

> **You can't have one part of government supporting industrial development and another part of government, through its procurement decisions, not supporting industrial development.**

"What we're proposing is that government thinks about an industrial policy fund which departments can draw on if they need to get local suppliers, so that there's a compensation element," said Levin.

He added that industrial development should not be left to just one department. Currently, the department of trade, industry and competition was at the forefront of this.

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"Industrial development and localisation are all government's responsibility and need to be reflected in the way it delivers its mandates," said Levin.

Transnet CEO **Portia Derby** said some local procurement requirements imposed on state-owned enterprises were onerous and to their detriment.

"On our side, the pace constantly changes because somebody's worried that we're special crooks. There must be something about us special crooks that's different from the rest of South Africa," she said.

This comes as government is deregulating the rail and electricity sectors to provide additional capacity.

> **When you say that Transnet only has to meet a local content designation requirement, while the private sector doesn't, what are you saying? If you don't even the playing fields, you're trying to kill Transnet. So our position is that, if we're going to survive, we need to have exactly the same rules that apply to the private sector.**

"If my competitor can buy whatever they want from China without this extra 10% to 30% and then sell into the market at a lower price, how can I live?" asked Derby.

"We really need to figure out how to make this much more efficient, or the aggregate demand that we're hoping to see won't be coming up.

"The tender that we had for 1 064 locomotives was for a four-year period. There's no industry that's sustainable for four years. At the end of that period, there's a collapse in demand because the project's done.

"Local content reaches 55% to 60% during that time and, the minute the project ends, that percentage is dead because those companies have folded.

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"Thinking that one has to industrialise on the back of projects is a big mistake. It only leads to bankruptcy," she said.

"What we've got to shift to is industrialising using a maintenance programme, because maintenance is something I have to do regularly. Until now, we haven't had maintenance and materials reliability spares agreements with anyone. We can't, because there's a rule in the Public Finance Management Act that you can't enter into a long-term agreement unless you have the budget for it. That makes absolute sense in government, which depends on Treasury for funding.

"These agreements make sense if they take 15 or 20 years, because you tie them up to the life of the asset. We can't do that. For that reason, there are lead items that can take as long as 45 weeks. We can only buy a party when we can point at the money. You can't buy a company like that. It's ridiculous," said Derby.

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