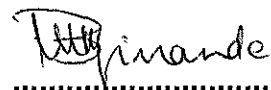


REPORT NO. 618

**INCREASE IN THE RATE OF CUSTOMS DUTY ON COMBINED
REFRIGERATOR-FREEZERS, FITTED WITH SEPARATE EXTERNAL
DOORS**

The International Trade Administration Commission herewith presents its Report No. 618:
INCREASE IN THE RATE OF CUSTOMS DUTY ON COMBINED REFRIGERATOR-FREEZERS, FITTED WITH SEPARATE EXTERNAL DOORS, with recommendations.


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MELULEKI NZIMANDE
CHIEF COMMISSIONER

PRETORIA

13 | 11 | 2019
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REPUBLIC OF SOUTH AFRICA

INTERNATIONAL TRADE ADMINISTRATION COMMISSION OF SOUTH AFRICA

REPORT NO. 618

INCREASE IN THE RATE OF CUSTOMS DUTY ON COMBINED REFRIGERATOR-FREEZERS, FITTED WITH SEPARATE EXTERNAL DOORS

Synopsis

Defy Appliances (Pty) Ltd, hereon referred to as the applicant, applied for an increase in the rate of customs duty on combined refrigerator-freezers, fitted with separate external doors, classifiable under tariff subheading 8418.10 from 25 per cent *ad valorem* to 30 per cent *ad valorem*, by way of creating an additional 8-digit tariff subheading. The application is for an increase in customs duty applicable to refrigerators with a total capacity exceeding 400 litres.

The Commission considered the application in light of information at its disposal. In particular, the Commission took the following factors into account:

- The strategic nature of the white goods industry to the country in terms of investment, value addition and job creation;
- The significant investment made by the applicant in additional capacity for the manufacture of the subject products over the past 4 years;
- The considerably low levels of capacity utilization over the period under investigation;
- Diminishing domestic employment opportunities;
- The commitment by the applicant to invest in additional capacity and efficiency improvements over the 3 years following a duty increase; and

- The applicant's commitment to increase employment in its production of the subject product over the next three years following a duty increase.

The Commission concluded that additional tariff support should enable the industry manufacturing combined refrigerator-freezers, fitted with separate external doors, to utilise its existing under-utilised production capacity, achieve economies of scale, with a reduction in the marginal cost of production.

A duty increase is expected to result in the growth of the local industry, specifically creating an appetite for investors to invest and localize the manufacturing of the subject product locally. This should result in the creation of additional jobs, strengthened local manufacturing as well as improved competitiveness of local products.

The Commission recommended that the rate of customs duty on combined refrigerator-freezers, fitted with separate external doors, classifiable under tariff subheading 8418.10, be increased from 25% *ad valorem* to 30% *ad valorem*, as outlined in paragraph 31 of this report.

THE APPLICATION AND TARIFF POSITION

1. Defy Appliances (Pty) Ltd (“**Defy**”) applied for an increase in the rate of customs duty on combined refrigerator-freezers, fitted with separate external doors, classifiable under tariff subheading 8418.10 from 25 per cent *ad valorem* to 30 per cent *ad valorem*, by way of creating an additional 8-digit tariff subheading. The application is for an increase in customs duty applicable to refrigerators with a total capacity exceeding 400 litres.
2. The applicant is Southern Africa’s largest manufacturer and distributor of major domestic appliances, with distribution centres in a number of African countries. The company manufactures and develops a range of large appliances, such as refrigerators, gas stoves, tumble dryers and convection ovens.
3. The company has three factories in South Africa. Its Jacobs factory in Durban manufactures free-standing stoves, built-in ovens, hobs and tumble dryers; its Ezakheni factory in Ladysmith manufactures electric chest freezers and electric refrigerators; and the East London factory manufactures only the subject products.

4. As motivation for the application, the applicant stated the following:

- The white goods industry in SACU is currently struggling to sustain jobs and investment;
- Defy re-launched its East London plant in 2014 following an investment of approximately R120 million to manufacture side-by-side refrigerators. This investment was on the back of a growing consumer base in Africa fuelled by a growing middle class;
- The domestic white goods industry has since been under pressure due, in part, to increasing low priced imports and this has put the viability of the SACU industry at risk;
- An increase in customs duty will ensure job retention, additional market share locally, and enable competitiveness in the export markets; and
- An increase in customs duty will also be instrumental in supporting the current and future plans for the introduction of an additional product range by Defy.

5. The application was published in the Government Gazette on 26 September 2018 for comments by interested parties, as follows:

Increase in the general rate of customs duty on:

“Combined refrigerator-freezers, fitted with separate external doors: Other, classifiable under tariff subheading 8418.10 from 25% to 30% by way of creating an additional 8-digit tariff subheading”.

6. The existing tariff structure for the subject product is as follows:

Table 1: Current tariff structure for the subject product

Tariff Heading	Tariff Subheading	Description	Statistical Unit	Rate of duty				
				General	EU	EFTA	SADC	MERCOSUR
84.18		Refrigerators, freezers and other refrigerating or freezing equipment, electric or other; heat pumps (excluding air conditioning machines of heading 84.15);						
	8418.10	Combined refrigerator-freezers, fitted with separate external doors	u	25%	Free	Free	Free	25%

Source: SARS 2019

7. The subject product currently attracts a customs duty of 25 per cent *ad valorem* when imported under general and from MERCOSUR member states. The applicable WTO bound rate is 30 per cent *ad valorem*.
8. The tariff structure as requested by the applicant is as follows:

Table 2: Requested tariff structure for the subject product

Tariff Heading	Tariff Subheading	Description	Statistical Unit	Rate of duty				
				General	EU	EFTA	SADC	MERCOSUR
84.18		Refrigerators, freezers and other refrigerating or freezing equipment, electric or other; heat pumps (excluding air conditioning machines of heading 84.15):						
	8418.10	Combined refrigerator-freezers, fitted with separate external doors						
	8418.10.05	With a total capacity not exceeding 400 litres	u	25%	Free	Free	Free	25%
	8418.10.90	Other	u	30%	Free	Free	Free	xx

Source: Applicant 2018

9. The South African Revenue Service (SARS) suggested the following description for the requested new 8 digit national tariff line for administration purpose:

“Combined refrigerator-freezers, fitted with separate external doors: Other”

INDUSTRY AND MARKET

10. The subject products are combined refrigerator-freezers with separate doors and/or drawers, with various volume capacity ranges measured in litres, all of which have a capacity exceeding 400 litres. The subject products come in various dimensions or shapes such as Side-by-side, French door combination, Bottom mount and Top mount.
11. The subject products consist of a thermally insulated compartment and a heat pump (mechanical, electronic or chemical) that transfers heat from the inside of the refrigerator to its external environment so that the inside of the refrigerator is cooled to a temperature below the ambient temperature of the room.
12. The subject products are mainly used for domestic/household purposes.
13. The main input materials used in the manufacture of the subject products include coated flat steel, cable assembly, compressors, condenser, copper pipe, drum bearings,

evaporator, grooved rack glass and aluminium pipes. These input materials are sourced from both the local and global markets.

14. The applicant is one of the two domestic manufacturers of the subject product in the SACU region; the other being Hisense, with a manufacturing plant in Atlantis, Western Cape. The latter commenced the manufacturing of the subject products in January 2019.

15. In addition to the above manufacturers, Whirlpool South Africa (Pty) Ltd manufactures refrigerators with a total capacity not exceeding 400 litres.

16. The main importers of the subject product in the SACU region include:

- Samsung Electronics (Pty) Ltd (“Samsung”);
- BSH Home Appliances (Pty) Ltd (“BSH”);
- Hisense SA (Pty) Ltd;
- Whirlpool South Africa (Pty) Ltd;
- LG Electronics (Pty) Ltd (“LG”);
- Massmart Holdings (“Massmart”);
- SMEG South Africa (Pty) Ltd (“SMEG”); and
- Imperial Air Conditioning (Pty) Ltd t/a Media Fridges (“Imperial Air”).

17. Tariff subheading 8418.10 also includes other products not subject to this investigation, such as refrigerators with a capacity not exceeding 400 litres. Due to the nature of the current tariff classification, the import volumes could not be separately analysed to show the import trends, over the period, for the subject products.

18. While the applicant’s total production and sales volumes increased over the period from 2016 to 2018, capacity utilization has declined and remains at unsustainably low levels. The decline in capacity utilization is, in part, due to the investment by the applicant in additional capacity and efficiency improvements.

COMPETITIVE POSITION

19. Competitive challenges facing the domestic industry at an operational level include, inter alia, increasing high labour costs, increasing energy costs, high transport costs, port charges and financing costs. In addition, the following challenges hindering the competitiveness of the industry have been identified:

- High volume of imports;
- High input costs;
- Small size of the local market; and
- Cost of capital to finance technology and capital upgrade.

20. The unsustainably low levels of capacity utilisation result in a higher marginal cost of production for the subject product and renders the domestic manufacturing industry uncompetitive.

COMMENTS RECEIVED

21. Support for the application was received from the Eastern Cape Development Corporation, Buffalo City Metropolitan Municipality's Economic Development, Environmental Affairs and Tourism, and the Border-Kei Chamber of Business. The support was mainly centred around the following factors:

- One of the key milestones identified in the IPAP's with regards to supporting the local manufacturing of White Goods products is to facilitate a favorable tariff regime and introduce rebate mechanisms for local manufacturers;
- Defy's intention is not only to supply the South African market but also to position itself as a production center for export markets in its shareholder's global supply network;
- A duty increase should result in the growth of the local industry, specifically creating an appetite for investors to invest and localize the manufacturing of the subject product locally. This should result in the creation of additional jobs, strengthened local manufacturing as well as improved competitiveness of local products;

- The continuation and expansion of the side-by-side refrigerator line in East London is critical to the sustainability of Defy's operations and it is expected that further jobs can be created; and
- The tariff increase will allow local manufacturers to be able to compete with low-priced imports.

22. Objections to the application were received from the following importers of the subject product, amongst others: Samsung Electronics (Pty) Ltd ("Samsung"); BSH Home Appliances (Pty) Ltd ("BSH"); LG Electronics (Pty) Ltd ("LG"); Massmart Holdings ("Massmart"); SMEG South Africa (Pty) Ltd ("SMEG"); and Imperial Air Conditioning (Pty) Ltd t/a Media Fridges ("Imperial Air").

23. The main reasons for the objections included, but were not limited to, the following factors:

- Considering that the subject products were considered under the review by ITAC and the possible increase was rejected, there is likely not much that has happened to justify a duty increase;
- The duty will only benefit the local manufacturer as it will translate to the increase in pricing and deny the South African consumers access to imported premium products of technological leadership;
- The duty increase will create a monopoly in the refrigerator market;
- There is no real import growth over the period, import volumes declined by 13% between 2015 and 2017 even though an increase in imports can be expected given that the white goods market is a growing market;
- The applicant's brand, Defy, is the leading brand in the domestic market and that makes it a price setter, and not a victim of low priced imports;
- A duty increase will have a severe impact not only on importers but also on consumers since it will likely result in increased selling prices, reduced demand and limited/reduced consumer choice; and

- A possible duty increase should be rejected since the negative effect of the duty increase will outweigh the alleged benefits by the applicant.

24. While the Commission has noted the above objections as raised by interested parties, the Commission also considered that circumstances have changed since its 2016 investigation on refrigerators and that the current application is for a split in the tariff subheading for combined refrigerator-freezers with a capacity exceeding 44 litres. Furthermore, the Commission considered that an increase in duty would encourage more localization of manufacturing for the subject product and the utilization of the existing under-utilized production capacity.

FINDINGS

25. The Commission considered the application in light of information at its disposal. In particular, the Commission took the following factors into account:

- The strategic nature of the white goods industry to the country in terms of investment, value addition and job creation;
- The significant investment by the applicant in additional capacity for the manufacture of the subject products over the past 4 years;
- The considerably low levels of capacity utilization over the period under investigation;
- Diminishing domestic employment;
- The commitment by the applicant to invest in additional capacity and efficiency improvements over the 3 years following a duty increase; and
- The applicant's commitment to increase employment its production of the subject product over the next three years following a duty increase.

26. The Commission concluded that tariff support should enable the industry manufacturing combined refrigerator-freezers, fitted with separate external doors, to utilise its existing under-utilised production capacity, achieve economies of scale, with a reduction in the marginal cost of production.

27. A duty increase should result in the growth of the local industry, specifically creating an appetite for investors to invest and localize the manufacturing of the subject product locally. This should result in the creation of additional jobs, strengthened local manufacturing as well as improved competitiveness of local products.

RECOMMENDATION

28. In light of the foregoing, the Commission recommended that the rate of customs duty on combined refrigerator-freezers, fitted with separate external doors, classifiable under tariff subheading 8418.10, be increased from 25% *ad valorem* to 30% *ad valorem*, by way of creating an additional 8-digit tariff subheading as follows:

- *“Combined refrigerator-freezers, fitted with separate external doors: Other”*