

**DEPARTMENT OF ECONOMIC DEVELOPMENT, ENVIRONMENTAL
AFFAIRS AND TOURISM**

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Distinguished representatives of Government, business, civil society and development agencies,

It is a pleasure to address you this morning on such a critical topic. I have decided to structure my paper in four inter-related sections. The first looks at the broader macro-policy context within which SMMEs operate. If we are unable to develop macro instruments to support SMME growth, we will not make our target of 5 million jobs by 2020. I believe the majority of these jobs will not come from large formal enterprises, but rather from SMMEs.

The second part of my paper will look at success factors for SMME development: why has the SMME sector developed so rapidly in other countries but has been rather stagnant in our own country.

Thirdly, I will turn to examining the state of SMMEs in South Africa and the Eastern Cape. Finally, I will propose a set of Government actions that, if resourced and implemented, will unlock the potential of the SMME sector.

1. POLICY CONTEXT

South Africa's post-94 era is now approaching 18 years it is now sufficient time to reflect on what we have done right and what was less than satisfactory. By now we had hoped to be on a solidly high-growth trajectory, with associated progressive reductions in unemployment, poverty and inequality. The economic struggle is more arduous than anticipated. There are legitimate doubts that we are on the best course.

To illustrate this, during the last 18 years we have witnessed sustained economic growth, however this has also exposed serious structural deficiencies in our economy. The growth periods of the last decade have exposed the phenomenon of jobless growth.

The jobs crisis is worsening. During the recession period between 2008/2009, the South African Economy lost over a million jobs and the EC economy shed 100 000 jobs. The old accumulation dynamic of cheap labour, cheap electricity and abundant mineral resources, is not working. Why have we been unable to diversify and transform our economy? Why have we not been able to spread wealth more equitably among the black majority?

During this term of government key policy documents have been approved by cabinet, namely the New Growth Path (NGP) and the Industrial Policy Action Plan 2 (IPAP2). These articulate the crisis of jobless growth and set targets for decent job creation (5 million jobs by 2020) including focused incentives for key sectors of the South African economy. More recently the National Planning Commission has published vision 2030, which targets the reduction of unemployment by 20%. This will be a huge effort by all partners. Recently, the youth league has launched their campaign around economic freedom and nationalization. Of course, the debate is natural in a democracy, but we need

to move beyond debate to a fundamentally different approach to state support for the economy.

It is my contention that five inter-related factors account for our economic underperformance:

- The pre-dominance of monetary policy over economic and industrial policy which has resulted in an over-valued currency and high interest rates, leading to de-industrialization;
- The exceptionally poor socio-economic inheritance of democratic SA and the ongoing unstable global context,
- Our ambivalence towards the private sector, capital expansion, and issues related to the costs of doing business in SA;
- The failure to invest sufficiently in skills development and logistics;
- The failure to create a new efficient and professional government bureaucracy, that is so crucial to stimulating capital's development and social development generally.

Unless we deal with these fundamental issues, our other efforts to develop SMME's will be undermined. So we need to broaden the debate on BBBEE, and consequently ensure that our SMME sector has a voice in the bigger economic debates going on in the country.

The Eastern Cape government has approved the Provincial Industrial Development Strategy (PIDS). The department has now finalized the development of sector and implementation plans for the PIDS. Additional work will be done to set targets for SMME's to participate actively in the main levers of the provincial economy. We will continue to consult with NAFCOG, Border-Kei

and the Nelson Mandela Chamber to ensure the needs of SMMEs are integrated into our Industrial Strategy Implementation Plans.

2. SMME Success Factors

South African entrepreneurial activity is far lower than regions with similar per capita GDPs in various emerging markets. The entrepreneurial rate in SA is around 8%, compared to well over 15% in countries such as China, Brazil, India, Argentina, Indonesia, etc. Entrepreneurial activity is defined as the percentage of the population which is in the process of or have just started a business between the ages of 18-64 years. So why are a higher proportion of South Africans not starting businesses?

I would want to argue that 4 factors make for successful SMME and entrepreneurial development:

- (1)The first is specifically related to the entrepreneur and his/her orientation. There is a direct link between education and entrepreneurial activity, and education and the success or growth of an enterprise. The ability to manage and run a business beyond the initial start up is linked to necessary skills, experience and training. Cultural factors also play a role.
- (2)The second factor relates to the external support environment which may act as a hindrance or enabler. These include access to markets, access to finance, non-financial business support, the tax regime, little red-tape, etc. Clearly Government is the main player here, and can make the difference through designing and implementing the right support measures.
- (3)The third success factor is the level of organization and coherence within the sector. Does the SMME sector speak with one voice when it comes to

issues of policy advocacy? The auto sector gets the support it does because of its coherence when engaging the state. How do we ensure the same happens in the SMME sector?

(4)The fourth set of success factors include a range of factors that affect market access and business sustainability. These include sector and location; local comparative advantage; locational issues; proximity to other businesses; and clustering to share networks of suppliers and buyers.

3. SMMES in South Africa and the Eastern Cape

Having dealt with the factors that make for successful SMMEs, I would want to briefly turn to look at the state of SMMEs in SA.

The nature and profile of the regional enterprise market must be understood in order to ensure that support mechanisms are adequate and meet the needs of those in the market. It is generally accepted that SMME research is inadequate and largely unreliable. The Labour Force Survey compiled by Statistics South Africa provides a measure for the number of people owning small businesses as 2.43 million in 2007, the majority of these is in the informal economy at 1.69million. The Business Register lists the number as 536 000 companies, however this minimizes it as only VAT registered companies are listed. The data compiled by a number of agencies (Ntsika, Dti, Stats SA, Business Partners, Eskom and GEMs) puts the number between 800 000 and 2.9million. The numbers also indicate that the numbers are concentrated in the micro and small enterprises.

According to the Stats SA Business register of 2007, the Eastern Cape enterprise is largely informal with a meagre 5.3% contribution to the national

formal enterprises and more than double at 13.4% to the informal enterprises. The sectors which the formal and informal traders operate in are primarily retail and wholesale trade (52%), community services (10%), construction (9%). I am happy to see an increasing number of SMMEs in the manufacturing sector (12%). Worrying is that agriculture only has 4% of SMMEs in the Eastern Cape.

4. Government support

In unlocking the potential of South African Entrepreneurs, Government's approach to SMME development is focused around 3 pillars.

(i) Promoting entrepreneurship

- Strengthen national awareness about the critical role of entrepreneurship
- Promote alternative focus of ownership
- Expand franchise opportunities
- Strengthen business associations and networks

(ii) Creation of an enabling environment

- Maintain small-business sensitive regulations
- Improve access to finance
- Strengthen access to markets via procurement, exports and business linkages
- Facilitate availability of business infrastructure and premises
- Increase the effectiveness of enterprise support

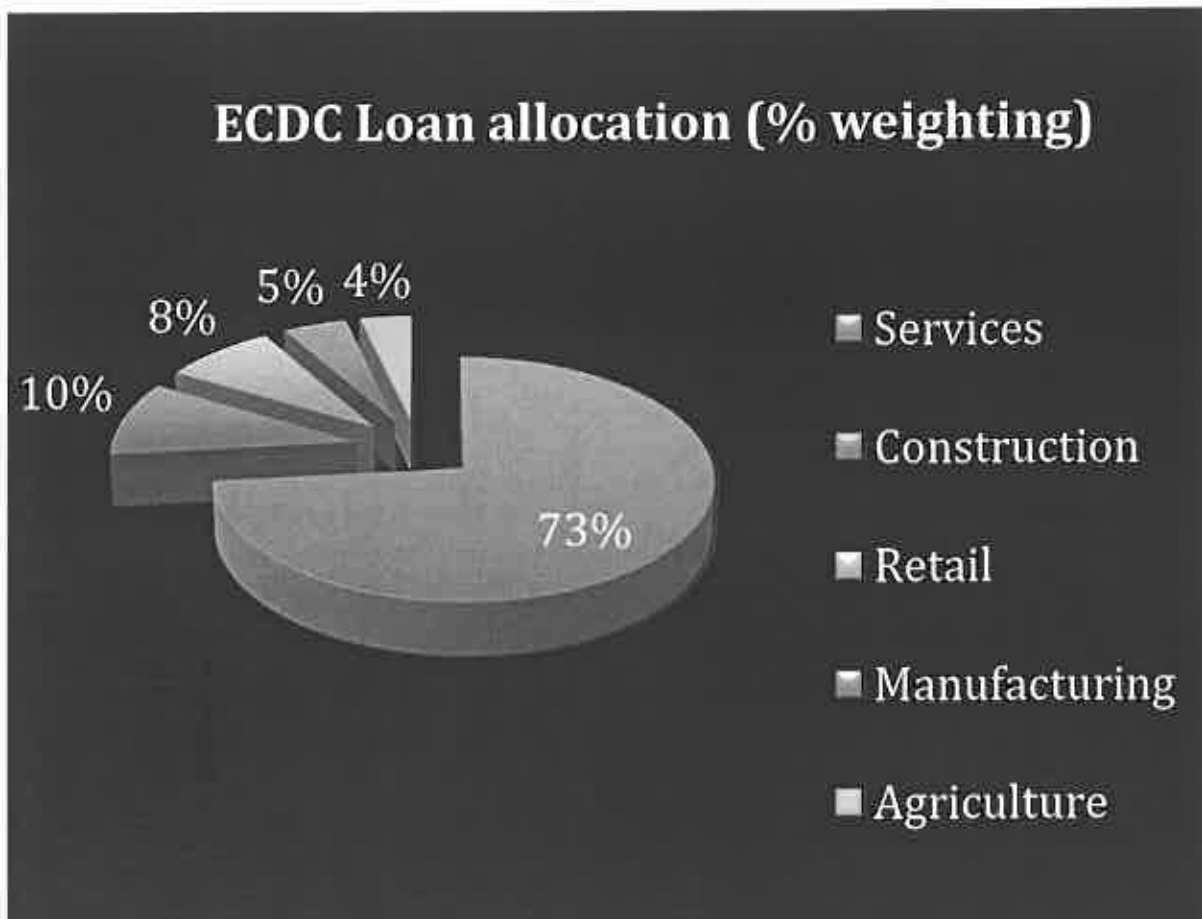
(iii) Enhancing competitiveness and capabilities at enterprise level

- Strengthen managerial, business and technical skills
- Facilitate improved quality, productivity and competitiveness
- Support technology transfer, incubation and the commercialization of business services
- Expand SMME focuses sector support strategies

These pillars must be underpinned by Information, research, monitoring & evaluation.

So how are we doing when it comes to supporting SMMEs locally?

The ECDC Annual Report reports that R109 million was disbursed in loans to 451 enterprises. 42% of lending was below the R500 000 mark. Fee-based loans form the majority of the product mix. Short-term loans go to contractors in the construction industry who provide services for the state.



Source: Annual Report, (Graph ECSECC, 2011)

The bulk of ECDC loans went to the services sector, followed by construction and retail sector with allocations of R80, R11 and R 9 million consecutively. Manufacturing and agriculture received a total of R 9 million amounting to only 9% of the total R109 million loans disbursed. Manufacturing is the foundation of the provincial economy but under severe threat. The low level of support to the productive sector is therefore a fundamental problem. One might suspect that this lending pattern is replicated by other DFIs.

Conclusion

In conclusion, we need to rethink how to strengthen our support for the SMME sector. We are currently working with EDD and the DTI on establishing a common delivery platform for supporting SMMEs and enterprise development in the province.

This will integrate and develop common programmes among a range of agencies such as the ECDC, SAMAF, Khula, SEDA, and the IDC.

We need also to better distribute SMME support spatially. Here we can use the ECDC footprint more optimally to ensure the national agencies provide equitable services throughout the province.

We also need an improved business model for support services. Support is currently mainly geared towards access to finance. It ignores other elements which are key to growth and development of SMMEs in the region. More stress is needed on issues such as market access and entry into new industries or sectors.

Access to finance must be tailored to SMME needs. Finance is predominantly targeted at the medium and formal enterprises. We need a re-design of instruments to promote the development of the informal sector. We might for example create mechanisms to support umgalelo (informal savings schemes). We also need to consider ways of valuing homesteads as a basis to raise capital. And we must focus more on women who are proven to be better business risks than men and have lower rate of failure.

Education and training for SMME development must be more effective. It can be a large contributor to the development of numeracy and literacy levels. These competencies directly impact the quality of entrepreneurship. It is hard for business support entities to compensate for the shortcomings of the education system. There needs to be more focus on courses on entrepreneurship, financial management and growing of business. We must coordinate more effectively the work of SETAs and other state institutions from the point of application for assistance. The various institutions could move towards co-financing training modules for entrepreneurs.