Can SMEs address the agenda of Radical Economic Transformation in South Africa?

Vrinda Chopra analyses whether the increasing focus on small, medium and microenterprises is a viable way of reducing inequality in South Africa.

The problems of South Africa's persistent inequalities are glaring in the face of an unemployment high of 27.7 per cent and youth unemployment at a staggering 50 per cent. The tenacious face of inequality showed itself with the intense #FeesMustFall protests across South African universities in 2015 and 2016. And now in the aftermath of those events, we see deepening conversations around radical economic transformation (RET) of the South African society and State and Private sector response in the form of increasing emphasis on growing Small, Medium and Microenterprises (SMMEs).

While RET itself is a highly contested term at the moment, with no real synthesis, this article will concentrate on a specific element of RET: reducing inequalities and whether SMMEs can be the adequate policy response. The South African state certainly seems to think so – state response to problems of escalating unemployment and inequalities has predominantly been around encouraging entrepreneurship in lieu of adequate opportunities for formal employment.

The state supports SMMEs in two significant ways. The first is a direct approach, where entrepreneurs can access financial and business support through state-owned agencies like the Industrial Development Corporation (IDC), Small Enterprise Finance Agency (SEFA), Small Enterprise Development Agency (SEDA) and the like. These agencies form a group that support SMMEs at various stages of growth. They are ideally supposed to work as a consortium of agencies, providing support at varied levels of enterprise development as well as on different aspects of running a business – ranging from finance, operations, marketing, soft skills and so on.

The second is a more indirect approach by incentivising corporates through the points system of the Broad-based Black Economic Empowerment (BBBEE) policy to work on Enterprise Development as part of their social investments. These incentives have led to a tiered development strategy to encourage SMME development. Corporate Social Investments (CSIs) are increasingly supporting entrepreneurs in marginalised communities, by working with a network of organisations – such as incubators, intermediaries, and non-profits. In turn, this feeds back into the policy structures, strengthening incentives and encouraging others to get on board with SMME development.

Kapula Candles is a large scale industry today, but it started as a microenterprise with founder Ilse Appeklgryn making these handcrafted candles in her home.
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The tiered development strategy looks effective on paper – if it worked at its optimum level. CSI funds need to work with incubators as they do not have the skills, human resources or adequate knowledge to work directly with communities; incubators need the CSI funds to further their programs; communities need incubators to support them for resources and given that their education did not prepare them for such a career; intermediaries need examples of best practices to research and encourage others to support entrepreneurship and so on.

While this need-based value chain is essential in ensuring some impact, the extent of impact on the communities is unknown. Each organisation talks about the number of jobs created and sustained, but the looming concern is that there are not enough incubation programs or enough funds available to support all the aspiring entrepreneurs and create significant jobs. Moreover, as many note, the sector is highly competitive with close to 50 or more applicants for one space in an incubation programme.

With demand outstripping supply, there is a need to highlight some systemic issues that problematise SMME development in South Africa and their ability to address the unemployment abyss and ideas of RET.

The first systemic issue is that South Africa's liberal market structure does not create enough economic opportunities. Most entrepreneurs face stiff competition and are bogged down by red tape and rigid regulations when turning to the state for support. There are serious inconsistencies in its macro-economic policies that supports large conglomerates in most sectors, while indulging in SMMEs in the micro-economic framework.

There is argument that SMMEs will create the necessary employment, but when there is such divergence between different policy imperatives, SMMEs that are already susceptible to failure have little to hope for. Even when they succeed, most are only able to create a handful of jobs, and given the current tight economic conditions, these jobs are liable to come down. Statistics corroborate this fact, as the annual unemployment growth rate (4.8 per cent) is double of employment growth (2.4 per cent) in the country. The goal of bringing down unemployment (forget redistribution of wealth) to 14 per cent by 2020, as stated in the Medium Term Strategic Framework (MTSF) seems like a faraway dream.

The second systemic issue is that the socio-economic conditions of the marginalised looking towards entrepreneurship does not showcase them as individuals capable of the available support, due to their level of education, their lack of resources and need for survival versus want for entrepreneurship. For instance, there is evidence to show that many organisations' due-diligence processes including those of the likes of SEFA and IDC, prevents them from supporting much of the youth for fear of damages. The marginalised youth do not have resources to show as collateral, or in most cases the education to write good applications, even if they have good ideas, putting them in a disadvantaged position for private sector support as well.

Already disadvantaged by their education and literacy levels, it could also be that the desperation of the marginalised is further affecting their cognitive abilities seen in the quality of their ideas. Research by Harvard Professor Sendhil Mullianathan and Princeton's Eldar Shafir, shows scarcity makes it difficult to concentrate on much else other than the scarcity in question – which in this case is access to basic needs. A preliminary connection can be made to claims by most incubation and acceleration programmes that the quality of the bulk of their applications is poor. In other words, those who turn to entrepreneurship for survival are unable to access available resources in the form of state grants, loans or private incubation and skills development programmes, all of which follow a competitive market model.

In a nutshell, the marginalised population, the bulk of the unemployed given the evidence and circumstances can barely rely on SMMEs, either for employment or as entrepreneurs themselves. In the interim, therefore, it is questionable that SMME development in SA can realistically pander to the calls for RET. What is needed is a systemic and holistic approach that recognises that it does not always make market sense for even support structures encouraging entrepreneurship to reach the chronically marginalised in order to stay competitive. Market imperatives implicit in policy structures, restraining deep-set impact consequently need to be understood, differentiated and circumvented for a serious outlook towards RET in South Africa.

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