

## ENTERPRISE DEVELOPMENT AS A DRIVER OF ECONOMIC GROWTH IN SA

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South Africa has one of the worst levels of entrepreneurship and sustainable new enterprises creation by global comparison with 35 other countries. The Global Entrepreneurship Monitor hosted in South Africa by the UCT Centre for Innovation and Entrepreneurship ranks South Africa as **last** amongst their sample of developing countries for entrepreneurial activity in 2005, with only 5.1% of adults between the ages of 18 and 64 owning a start-up business less than 3.5 years old. This compares to an average achieved by the 35 sampled countries of approximately 10.5% and 7.5% for developing countries and developed countries respectively. Of the 5.1% of 18-64 year old adults involved in start-up businesses, only about half of these are seen as 'opportunity' entrepreneurs who leave formal employment to pursue a perceived business opportunity – the remainder are considered 'survivalist' entrepreneurs who have started up as a result of a lack of formal jobs. Worse yet, only 25% of the early stage entrepreneurs result in businesses which survive a full 3.5 year period (which again, is the worst performance of all 35 countries sampled\*).

The causes of South Africa's poor levels of entrepreneurship have been debated at length and there has been no shortage of attempts to rectify the situation – be it Non-Governmental Organisations advising Government on Small Medium Enterprise (SME) support policy or Government Organisations with a mandate to disperse public funds to new SMEs. So why the continuing poor levels of entrepreneurship and inability to create sustainable businesses?

In our experience, we believe that there are 3 ingredients critical to the creation of a sustainable business. The first is having access to the market and a potential set clients who have a need for a product or service and are willing to pay for it – i.e. a viable business opportunity. The second requirement is sufficient skills and experience to not only provide the product/service, but also to set up and manage a growing business. Finally, initial venture funding is required to set up the business and allow it to test the business opportunity until the business stands on its own. You will notice that there is nothing particularly earth shattering about the above and the ingredients mentioned are the fundamentals for any successful business.

Too often though, Government support for SMEs has been confused between a focus on poverty alleviation and reduction of unemployment rather than sustainable new enterprise development.

However, the DTI's recently released BEE Codes of Good Practice provides a great incentive for private sector companies and the banks in South Africa to become significant drivers for

sustainable new enterprise development through various elements of the BEE balanced scorecard.

The **Enterprise Development element** directly encourages established companies to spend 3% of their NPAT on starting up new black businesses. This is not a small amount of money, it totals billions of Rands for the top 200 companies listed on the JSE. Many companies unfortunately follow Government's lead by spending their Enterprise Development money on small-scale poverty alleviation projects which look like Socio-Economic Development. On the other extreme, some large corporates set up BEE funds to become the BEE partners to traditional companies (e.g. RMB's Makalani management company and Bidvest's Dinatla). While this is not bad, only a few large SA corporates are setting up specific funds such as the Anglo-Zimele fund to develop sustainable **new** enterprises to support the growth of their core business.

Companies can make their own BEE Enterprise Development ventures successful by providing a guaranteed market against which a bank can lend initial funding, as well as leveraging their own internal skills to support the new entrepreneurs. The Codes allow companies to achieve their BEE score here with minimal additional budget required by providing the guarantee and some support skills and leveraging the banks in what they do best – lending money against a guarantee or asset.

The **Preferential Procurement element** also encourages established companies to procure 20% of their goods and services (by value) from black owned companies and 15% from enterprises with annual turnovers less than R35m. The DTI incentivises procuring from one's own enterprise development investments, which would clearly be the best way to optimise one's BEE score.

But companies need to be careful not to go against best practice procurement. A large company with an annual spend of say R1 billion requires R150m to be spent with 4 (BEE compliant) suppliers of average turnover R35m. This multiplies rapidly to 30 suppliers if the supplier is a small company with a turnover of R5m. To add large numbers of small suppliers to the procurement database goes against international best practice in procurement. Best practice requires that companies consolidate the number of suppliers in order to optimise fewer relationships thus reducing the cost of procurement. The implication is that companies intending to maximise their BEE points should be setting up larger ED companies which can become key suppliers.

One could argue that companies really should be focussing on their core business and not dabbling in the start-up of new businesses, so a key question companies in SA should be asking is: How do we most efficiently meet our BEE enterprise development targets and create sustainable businesses **which aid us in our own strategic objectives?**

**We recommend a three step process.**

The **first step** is to create an overarching framework for (BEE) Enterprise Development which has Board approval and an assigned budget to develop selected opportunities. This could take the form of an internal department or an external fund. A clear relationship should be

established between the parent company and this unit to address issues such as staffing and skills transfer, financial targets and budgets. Again, the DTI incentivises this as all costs to set this up can be considered as BEE enterprise development spend.

The **second step** is to search for opportunities which align with one's strategy and interrogate the supply chain to look for real and needed business opportunities. This means understanding the company's longer term growth strategy and looking for opportunities which support this growth. An example of this would be the alcoholic beverages company which realised that the core growth in its market was going to come from the growing Black Middle Class. Historically, they had little understanding of how to access this market. So they helped start up a Black owned and managed 'Events Management' company which began hosting marketing events on their behalf in the townships and now manages some of their most successful marketing campaigns.

The **third step** is to look for ways to combine efforts with other players in the industry or related industries to create further scale if necessary. Involving players in the financial services sector will significantly reduce the financing requirement for your company and involving specialists who can provide new business support services and reduce the risk of starting up a new business and management attention required to create a sustainable business.


As a last note, more and more highly talented South Africans (of all races) are looking for opportunities to exercise their entrepreneurial flair. What better way attract and retain top talent than to offer the best performers the opportunity to participate in such Corporate New Venture creation units?

Ultimately, Corporate support for BEE Enterprise Development can be a major driver of growth and entrepreneurship in South Africa – as well as a route to **real** Black empowerment.

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