

# TIPS

TRADE & INDUSTRIAL POLICY STRATEGIES



HOW SOUTH AFRICA CAN BOOST SUPPORT TO SMALL BUSINESSES:

LESSONS FROM BRAZIL AND INDIA

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## Abbreviations

ALIs	Agentes Locais de Inovação (Local Innovation Agents)
APLs	Arranjos Produtivos Locais (Local productive arrangements)
Assocham	Associated Chambers of Commerce and Industry (India)
BBSDP	Black Business Supplier Development Programme (South Africa)
BEE	Black Economic Empowerment
BIC	Business Innovation Centres (EU)
BNDES	Banco Nacional de Desenvolvimento Econômico e Social (Development Bank of Brazil)
BRIC	Brazil, Russia, India and China
Busa	Business Unity South Africa
Cerne	Centro de Referência para Apoio a Novos Empreendimentos (Reference centre to support new enterprises)
CGTMSE	Credit Guarantee Trust for Micro and Small Enterprises (India)
CII	Confederation of Indian Industries
Cipro	Company and Intellectual Property Registration Office (South Africa)
CNI	Confederation of National Industries (Brazil)
CNPq	O Conselho Nacional de Desenvolvimento Científico e Tecnológico (Brazil's National Research Council)
CPPP	(The) Community Public Private Partnership Programme (South Africa)
CRD	Credit Risk Database
Dempi	Fiesp's small and medium department (Brazil)
DTI	Department of Trade and Industry (South Africa)
ECDC	Eastern Cape Development Corporation (South Africa)
EIP	Enterprise Investment Programme (South Africa)
Emia	Export Market and Investment Assistance
Fampe	Fundo de Aval às Micro e Pequenas Empresas (Guarantee fund for micro and small enterprises)
Fiesp	Federação das Indústrias do Estado de São Paulo (Industry Federation of the State of São Paulo)
Fisme	Federation of Indian Micro and Small & Medium Enterprises
GDP	Gross domestic product
Gem	Global Entrepreneurship Monitor
Geor	Gestão Orientada para Resultados
GTP	Grupo Trabalho Permanente (Permanent Work Group)
HACCP	Hazard Analysis and Critical Control Points
IBA	Institute of Business Advisors (South Africa)
Ibsa	(The) India, Brazil and South Africa (Initiative)
IDC	Industrial Development Corporation (South Africa)
IID	Integrated Infrastructure Development
IPAP	Industrial Policy Action Plan (South Africa)
Ipea	Institute of Applied Economic Research (Brazil)
KVIC	Khadi and Village Industries Commission
LBSCs	Local Business Support Centres (South Africa)
MAC	Manufacturing Advice Centre (South Africa)
MDA	Marketing Development Assistance (India)
MDIC	Ministério do Desenvolvimento, Indústria e Comércio (Ministry of Development Industry and Commerce)
MPEs	Micro e pequenas empresas (micro and small enterprises)

MSEs	Micro and small enterprises
MSMEs	Micro, Small and Medium Enterprises
Namac	National Manufacturing Advisory Centre (South Africa)
Nectar	Núcleo de Empreendimentos em Ciência, Tecnologia e Artes (Centre for Enterprises in Science, Technology and the Arts)
NEF	National Empowerment Fund (South Africa)
NIEs	Newly Industrialising Economies
NMCC	National Manufacturing Competitiveness Council
NPA	Non-performing asset
NRF	National Research Foundation (South Africa)
NSIC	(The) National Small Industries Corporation (India)
NYDA	National Youth Development Agency (South Africa)
OEM	Original Equipment Manufacturer
PBE	Programa Brasil Empreendedor (Programme Enterprising, Brazil)
Prime	Programme First Innovative Business (Brazil)
PUC	Pontifical Catholic University - Rio University
R&D	Research and Development
SAB	South African Breweries
SAE	Secretaria de Assuntos Estrategicos (Secretariat of Strategic Affairs)
SAMAF	South Africa Micro Finance Apex Fund
SARS	South African Revenue Service
SBDC	Small Business Development Centers (US)
Seda	Small Enterprise Development Agency (South Africa)
SEZs	Special Economic Zones
SICDP	Small Industry Cluster Development Programme (India)
Sidbi	Small Industries Development Bank of India
Sinvest	Sindicato das Industrias do Vestuario de Pernambuco (Industry syndicate for clothing businesses of Pernambuco)
Spil	Support for Industrial Innovation (South Africa)
SPVs	Special Purpose Vehicles
SPX	Sub-contracting and Partnership Exchanges
SSI	Small-Scale Industries
TEA	Total Early Activity
TePP	Technopreneur Promotion Programme (India)
Thrip	Technology and Human Resources for Industry Programme (South Africa)
UCT	University of Cape Town
Unido	UN Industrial Development Organisation

# 1 Introduction

In its efforts to craft a new economic growth path and assist small businesses, South Africa could do well to look to emerging economies such as Brazil and India, which have attracted much attention in their recent efforts to create greater and more equitable economic growth. There is much South Africa can learn from these two countries, with gross domestic product (GDP) growth in India edging towards 10% a year and with Brazil ranked as one of most entrepreneurial countries in the world according to the 2009 Global Entrepreneurship Monitor (Gem) Report.

Policymakers, consultants, bureaucrats and all those that serve small businesses in South Africa have become increasingly aware that more needs to be done to support small businesses if the country is to address widening inequality and persistent poverty as well as unemployment and job losses.<sup>1</sup> It is also crucial to build a society that can create wealth more effectively, particularly with South Africa heading towards a dangerous dependency on state benefits with the number of social grant beneficiaries having risen sevenfold in just 10 years, from two million in 1999 to 14 million in 2009.<sup>2</sup>

The promotion of small businesses is one way the government could tackle South Africa's current and future economic challenges. In particular, the growth of small businesses could help reduce the population's dependence on state-funded grants, while boosting job creation and creating equitable growth. However, numerous factors such as a lack of business and financial management skills impede the growth or setting up small enterprises. In the meantime serious developmental opportunities are being foregone: according to researchers Finmark Trust's Finscope 2010 survey, small businesses could create 2.5 million jobs by 2020. Added to this Finmark believes that the government could take about 500 000 people off social grant schemes if it supported small businesses more actively.<sup>3</sup>

## Why Brazil and India?

While Brazil and India both have larger populations and land areas than South Africa, the three emerging do share some similarities in that all three are grappling with similar development issues, including a lack of quality education, a shortage of quality infrastructure and a low share in international trade. The three countries are also part of the India Brazil South Africa (Ibsa) initiative, set up in 2003, which aims to act as a forum to share various developmental and economic learnings and experiences. Nevertheless, Brazil is particularly similar to South Africa in that the two countries are among the most unequal in the world.

There is therefore a case for contrasting South Africa with Brazil and India. One reason to look to India and Brazil rather than to the Newly Industrialising Economies (NIE) of Southeast Asia as many developmental economists prone to do, is that the NIE model is not directly comparable to the policy context of South Africa. For instance, Alan Hirsch<sup>4</sup>, deputy director-general in South Africa's Presidency, points out that although the ANC began looking East, shortly before the end of apartheid, with the intention of modelling South Africa's growth on the export-led strategies of Southeast Asian countries, these countries were more authoritarian and had more skilled managers than South Africa, making it difficult to apply lessons there in South Africa.<sup>5</sup> More recently, international growth performances

<sup>1</sup> See Business Report, 9 October 2009. Also, a report by the OECD in July 2010 also noted that among emerging economies such as Turkey, Chile, Russia, Mexico and Brazil, South Africa had made the least progress in reducing poverty (see Business Report, July 9, 2010).

<sup>2</sup> See Ann Bernstein and Anthony Altbeker, "Rapid growth the only way to rid SA of stubborn poverty", in Business Day, 31 August 2010.

<sup>3</sup> Trevor Kaseke, Finmark Trust research specialist, quoted in "Millions of small businesses operate in dark", Business Day, 21 September 2010.

<sup>4</sup> Hirsch, Alan, *Season of Hope: Economic Reform under Mandela and Mbeki*, University of KZN Press, Scottsville, 2005: p118-119.

<sup>5</sup> This is although lessons were applied around policy focusing on innovation, education, private-public partnerships, industrial-sector targeting combined with geographic targeting, export promotion and training.

suggest that there are new lessons to be had from Brazil and India as part of the group of emerging economies labelled the Bric (Brazil, Russia, India and China) countries.

Several key differences across the three emerging economies stand out, however. For instance, Brazil is ranked as the sixth most entrepreneurial country in the world, according to the 2009 Global Entrepreneurship Monitor (Gem) Report, with a total early stage activity (TEA)<sup>6</sup> rate of 15.3%<sup>7</sup>, while South Africa is ranked a lowly 35<sup>th</sup> out of 54 countries with just one in 17 people involved nationally in starting or running a business (compared to one in seven in Brazil). In India about one in nine people are involved in starting or running a new business (with a TEA rate of 11.5%), according to figures from the Gem Report in 2008 when the country last took part in the Gem survey. During that particular year India was ranked at 15 out of 43 countries.<sup>8</sup>

Turning to Brazil again, policymakers in the world's eighth largest economy it seems are preparing for an entrepreneurial explosion. Though the country's entrepreneurs may still struggle to access capital and battle with red tape when starting a business, macro economic conditions have made it easier to start and run a business, particularly with GDP growth expected to touch five percent this year. Brazil also already escaped the worst of the 2008 global recession (with GDP growth of 0.2% in 2009, compared to South Africa's -1.8% and India's 6.8%) and following GDP growth averaging 3.7% between 2000 and 2008. This follows a decade or more where Brazil battled with a notorious inflation problem, growing at just 1.7% between 1990 and 1999.<sup>9</sup>

Meanwhile in India a task team by the Prime Minister Manmohan Singh is looking at various proposals to boost financial and business support to small businesses. Also on the agenda is the possible re-engineering of those public institutions that support small businesses. This follows a period where India's economic growth averaged at a little over 6% a year since 1991, when the country began implementing market reforms and gradually doing away with its infamous licensing regime which once choked entrepreneurialism. Like Brazil, this country too is betting on an explosion in the number of entrepreneurs.

## How is small business defined in these countries?

The governments of India, South Africa and Brazil each make use of their own unique definition when classifying an enterprise as a small or micro business. For example in India the Micro Small Medium Enterprise (MSME) Act of 2006 defines a small or micro business by the value of its fixed assets depending on whether the firm is based in the manufacturing or services sector. Like this a manufacturing firm is classed as a small business if the investment in plant and machinery is between Rs2.5 million and Rs50 million, while a firm in the services sector is defined as a small business if its investment in equipment falls between Rs1 million and Rs20 million.

In Brazil, a small and micro enterprise is defined by its annual turnover (up to R\$2.4 million), while the country's small business support agency, Sebrae, goes further by also defining a retail and construction business according to the number of employees they have.

In South Africa the governments makes use of a combination of annual turnover and number of employees to define an enterprise as small, micro, medium or large. Generally speaking a small business is defined as an enterprise which has 50 or fewer employees. Businesses are further defined as small, medium, micro or large according to their turnover by sector.

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<sup>6</sup> Gem's TEA rate measures the percentage of all those in the population involved in either setting up a business or running an enterprise which is up to three-and-half-year old.

<sup>7</sup> Equivalent to 18.8 million people, according to the 2009 Gem Report.

<sup>8</sup> 2008, 2009 Gem Report for Brazil. The last Gem country report on India was carried out in 2001.

<sup>9</sup> Figures from Brazil's Institute of Applied Economic Research (Ipea) quoted in Wikipedia ([http://en.wikipedia.org/wiki/Economy\\_of\\_Brazil#cite\\_note-28](http://en.wikipedia.org/wiki/Economy_of_Brazil#cite_note-28)).

More information on how small business is defined in each of these respective countries is provided in tables produced in Appendix 1 of this report.

## What is the aim of this report?

The aim of this study is to inform policymakers and the government, particularly South Africa's Department of Trade and Industry and its Department of Economic Development, on key learnings from fellow emerging nations India and Brazil when it comes to improving business support, market access and access to finance for small businesses.

To date there has been no reported studies on small business schemes in India and Brazil. This study aims to bring to light what may possibly be the best emerging countries against which South Africa can compare itself to.

The focus of the report is on those business owners in the formal sector starting out as well as those that employ between 10 and 50 employees. The focus is defined by the fact that these have been shown to make the most significant contribution to employment as we illustrate in this report.<sup>10</sup>

## Structure of the report

Following this introduction the report takes a brief look at the basic characteristics of small businesses in India, Brazil and South Africa – including a look at the respective business environment in each country and the size and performance of the sector and the ability of small firms to create jobs in each of these countries. A chapter follows on the policies that each of the three countries has in place to support small businesses. Some comments are also made on the architecture of support each government has set up with which to assist small businesses.

The bulk of the report is then taken up in Chapter 4 in looking at various support schemes South Africa could learn from as these are applicable in India and Brazil in the areas of: financial support, market support and business support. This report then concludes.

Much of the information in this report is gleaned from many interviews with various heads of small business associations, various government officials and policymakers who oversee small businesses and business owners themselves in South Africa, Brazil and India (see a full list under References). The interviews were conducted during visits to India (between March and April 2010) and Brazil (during August 2010) as well as via many telephonic discussions and email exchanges with various experts in each of the respective countries.

## Key findings

The report focuses on the various policies, government support schemes as well as the environment in which small businesses operate in each of the three countries under focus. In general policies and schemes to support small businesses appear to be working best in Brazil and less successfully in India and South Africa.

The report posits a number of reasons for this in the section on policies. These include better monitoring mechanisms, specific targets driven from the top and a more simplified support architecture in the case of Brazil compared to that of India and of South Africa.

The report also makes several other key findings, these are that:

- The state needs to co-ordinate its support better by simplifying its architecture of government agencies and departments that support small businesses.

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<sup>10</sup> According to Neil Rankin from Wits University 73% of employed people in South Africa work for firms with fewer than 50 employees for instance.

- The South African government's finance agency Khula can put its ailing credit guarantee scheme back on track by learning from India's Credit Guarantee Trust for Micro and Small Enterprises (CGTMSE).
- South Africa must get buy-in of businesses and banks if it intends to set up a credit rating subsidy scheme similar to that run by India's National Small Industries Corporation (NSIC).
- South Africa can learn from an innovative card implemented by Brazil's Development Bank and which helps improve access to finance for small businesses, while promoting local production.
- The National Treasury in South Africa should reconsider set-asides for small businesses based on the experience of Brazil, it must also look at adopting IT systems to streamline the procurement system.
- The Small Enterprise Development Agency (Seda) can learn a number of key things from Brazil's small business support agency Sebrae's innovative and professional practices.
- The experience of Brazil is evidence that incubators can play an important part in building innovative businesses and develop regions, but that their ability to drive job creation is limited.
- Clusters face many challenges in India, but the South African government should not overlook the importance of focusing support on existing clusters rather than creating new ones from scratch. It should support these existing clusters by helping them to build strong business associations to drive these clusters and construct effective monitoring mechanisms to ensure cluster support delivers optimal business support to small businesses.

## Way forward

It is important that South Africa benchmarks its support organisations, programmes and general architecture of support, against peer countries such as India and Brazil. Though specific lessons are provided under each support scheme looked at in this report, in general there are five key learnings for South Africa from India and Brazil. Chapter 5 includes a more in-depth discussion of these key learnings, which are:

- Craft a national entrepreneurial vision based on measurable targets and which has backing from the President.
- Build more forums based on partnership with the private sector.
- Simplify the government's support architecture.
- Put effective real-time monitoring mechanisms in place.
- Better capacitate government agencies.