

3 Small business policies in South Africa, India and Brazil

With the opening up of domestic markets to world trade, many countries have resorted to promoting and supporting their respective small-business sectors to ensure local firms are able to compete against the added competition that an increase in global trade has introduced. A number of developing countries have also passed small business policies in a bid to forge more equitable economic growth in their respective countries. All three countries considered in this report have specific policies aimed at small business owners. While South Africa's small business policy is principally informed by the 1995 "White Paper on national strategy on the development and promotion of small business in South Africa", Brazil and India both passed legislation in 2006 aimed at boosting their small business sectors.

Each of the three countries has also developed institutions and agencies to support small businesses, with access to financial and business support. While an institutional make-up for each of the three countries is included in the appendix, it is worth pointing out here that in comparison to Brazil, India and South Africa have extremely complex government support matrixes (see Appendix 2 for diagrams and details). In South Africa the government's main funds and agencies are distributed across four different departments. While in Brazil one funding agency (BNDES) supports small business, South Africa has an array of funds (the NEF, Khula, NYDA, Samaf and the IDC) which creates problems when it comes to strategic co-ordination and also risks diluting the effectiveness of funding to small businesses.

South Africa

- Policy founded on 1995 White Paper.
- Merger of institutions in 2003 creates Seda.
- BEE encourages rent-seeking behaviour, rather than entrepreneurial behaviour, from black entrepreneurs.
- Schemes policies have had limited impact, little awareness of support organisations.

South Africa's 1995 White Paper outlined, among other things, the need for the government to create an enabling legal framework, facilitate access to information and advice, boost procurement from small firms and to improve access to finance and affordable physical infrastructure. The drafting of the white paper led to the 1996 National Small Business Act and the launch in the same year of Khula Enterprise Finance Limited, a government agency to finance small businesses and Ntsika Enterprise Promotion Agency to dispense non-financial support.

But in 2003 after calls to create a "one-stop" body where small businesses could get assistance from reputable sources, the government decided to do away with Ntsika, by merging it with the Community Private Partnership Programme and the successful manufacturing advice centre (MAC) programme²⁹, to form the Small Enterprise Development Agency (Seda) in 2004 – to dispense market support and business advice to business owners.

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The government's key focus with regards to small business has been on supporting black entrepreneurs, which the 1995 White Paper pointed out were the most marginalised group during apartheid. Two policies, aimed at helping more black people to become active in the economy and to aid small business owners, have been developed: the 2000 Preferential Procurement Policy Framework Act and the Black

²⁹ "Macs lauded by Minister", December 28, 2003 <http://www.businessowner.co.za/Article.aspx?Page=23&type=29&Item=2346>

Economic Empowerment (BEE) codes of good conduct.³⁰

The BEE codes, which came into effect in 2008, award points to businesses, based on seven elements, namely the percentage of black ownership, black management, black staff, black staff trained, procurement from black suppliers, business or financial assistance to black small businesses, corporate social investment. Under the BEE codes businesses with an annual turnover of above R35 million can score 15 points on the BEE scorecard if they spend 3% of their net profit on Enterprise Development. For those business with a annual turnovers of R35 million and below, the target is 2% of net profit³¹.

Yet to date there has been no study carried out on the impact BEE or preferential procurement has had on small business promotion. Presently the South African government hopes that large and medium firms will step in to assist small businesses by adopting enterprise development as a means to score BEE points. While this would go some way to expanding support and finance for small businesses, the BEE codes' strong emphasis on black ownership has inadvertently created a rent-seeking behaviour among wealthy or skilled black business people, in effect curbing entrepreneurship among this group.³²

Instead of using their skills or capital to start their own businesses, many have instead chosen to buy into existing large, often listed, companies. Black ownership may only form one of seven codes on the BEE codes of good conduct, but it is often perceived by companies to be the quickest and most visible way to transform. Companies with high BEE scores can win business with government. According to Nazeem Martin, managing director of small business financier Business Partners, this not only acts as a deterrence to entrepreneurship, but it means that the number of wealthier and perhaps more creative black businessmen are drawn away from starting productive, innovative enterprises³³. This has a direct effect on limiting manufacturing and high-growth companies, thus in effect further threatening to de-industrialise the country. BEE also threatens the tax base from growing, putting more strain on the country and its already 14 million welfare recipients³⁴.

BUSINESS SUPPORT

According to small business researchers SBP, despite numerous initiatives over the last 15 years aimed at both high end enterprise development, and the encouragement of micro enterprises, government support agencies and initiatives "have been less successful than intended", adding that this could also be "inferred from the institutional re-jigging". SBP concludes that the impact and achievements of the government's initiatives have "fallen disappointingly short of aspirations". The small business research organisation points out that since 2009 there has been a large-scale acknowledgement from those inside as well as outside of the government that the significant funding and support initiatives for small businesses have not had the desired effect in growing the sector.³⁵

On top of this awareness of government support has remained limited in the country: a 2007 report by Centre of Entrepreneurship at the University of Cape Town's (UCT) Graduate School of Business revealed that in Gauteng just 13.5% of entrepreneurs had heard of Seda and 1.3% had accessed the agency. In the Western Cape awareness of Seda stood at just 10%, with 0.5% having visited a Seda branch there. Added to this in the recent FinScope 2010 South Africa Small Business Survey only 3% of entrepreneurs reported that they had heard of Khula, while 10% said they had heard of National Youth Development

³⁰ When it comes to selling to the government, the Preferential Procurement Policy Framework Act of 2000 provides that, depending on the value of a government tender, 10% or 20% of the points awarded to a bidder be for the percentage of ownership in the bidding company of women, blacks or disabled people. The act is presently being aligned with the Black Economic Empowerment (BEE) codes of good conduct, which currently only apply to businesses bidding for work from the private sector.

³¹ Bignews, August 2007.

³² This is the view of Moeletsi Mbeki in *Architects of Poverty: Why African Capitalism Needs Changing*, Picador Africa, 2009.

³³ Interview with Nazeem Martin, Business Partners, September 2010.

³⁴ Business Times, September 12, 2010.

³⁵ SBP, 2009. "Small Business Development in SA: Time to Reassess".

Agency (NYDA) and 4% said they had heard of Seda. Only one percent of small businesses reported that they had visited Seda or NYDA branches.

CONCLUSION

South Africa's small business policies have done little to create effective support agencies to help support business owners to start up and grow their business. Added to this awareness of many of the government's support schemes also remains very low.

Much of this is as a result of the government's lack of co-ordinated strategies aimed at small business and a government support architecture (see Appendix 2) which is both clumsy and confusing – both to business owners and to government officials themselves. The government simply has too many agencies trying to assist business owners, which are in turn spread across two different departments – in turn confusing government officials.

Added to this the country's BEE legislation has acted as a deterrent to skilled black people starting their own businesses. The government should take active steps to get entrepreneurs to steer away from such rent-seeking behaviour by recrafting BEE legislation so that it incentivises and supports black entrepreneurs that want to start up or expand their own businesses, rather than incentivise those that want to buy a slice of an existing business.

India

- India has long promoted small businesses through a reservation policy for manufacturing of certain goods.
- In 2006 it passed the MSME Development Act, but some say it has had little effect.
- Because of institutional issues the government has made little impact in supporting small businesses.

Much of the Indian government's support schemes and policies for small businesses were introduced after 1991 in a bid by the state to cushion small firms as the state gradually does away with its policy of reserving certain goods for manufacture by small enterprises.

Small business promotion in India however is not new and dates back to 1967 when the government enacted India's Small-Scale Industries (SSI) Reservation Policy which sets aside certain manufacturing activities exclusively for small firms. At its height in 1978 the government's list of reserved goods for small firms contained 504 products. With the gradual removal of reservation since 1991, the small-business sector is facing much greater competition than before.

More recently in 2000 the Government of India announced a comprehensive policies package to strengthen small businesses. The package provided for easier access to credit, availability of collateral free loans up to Rs2.5 million capital subsidy for technology upgradation and improved infrastructure³⁶.

Though primary responsibility for the development of small business remains in the hands of the state and Union Territory Governments, the central government has always shown an interest in supplementing the efforts of the various states. At the national level, the Ministry of Micro, Small and Medium Enterprises (formed after the merger of Ministry of Agro and Rural Industries and Ministry of Small Scale Industries in 2007) serves as the central authority which assists the states in their efforts to support small businesses. The Ministry is empowered by the 2006 MSME Development Act which aims to boost support and promotion of small businesses. Among other things the act makes it easier for business owners to register their business, allows for the setting up of facilitation councils to deal with late payments owed to small firms and provides for the crafting of preferential procurement policies by government for small enterprises.

³⁶ <http://www.lubindia.org/ssi/what-is-ssi.php>

The Government of India has a number of support schemes for small businesses, including schemes aimed at increasing the competitiveness of small firms, making it easier to access finance, export and helping firms to acquire new technology. However business owners and small business associations offer a mixed account of how the Indian government has fared when it comes to supporting small businesses. Of note is the fact that the awareness of government schemes is very low. A study by consultancy Milagrow Business & Knowledge Solutions shows that only between 20% to 30% of micro, medium and small enterprises are aware of various government initiatives. This is somewhat similar to the situation in South Africa (see above section).

Milagrow's Rajeev Karwal believes part of the problem is that the MSME ministry plays only a minor role in the Indian central government and is often subjugated by the various industries ministries in central government. Most of these ministries are dominated by big businesses. The MSME ministry, he says, is "lacking in teeth"³⁷. Anil Bhardwaj, secretary general of the Federation of Indian Micro and Small & Medium Enterprises (Fisme) echoes this view. Bhardwaj commented that the largest drivers for the growth of small businesses have been the changes to the economic framework in the 1990s and the country's young sizable population, not the government's support schemes for small enterprises.³⁸

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The 2006 MSME Development Act introduced a new definition for small businesses (MSMEs) which the government applies to determine which enterprises can benefit from its support schemes, but critically, it also introduced a system by which small businesses waiting on payments from corporates or public-sector organisations can approach facilitation councils to settle outstanding debts. However, according to some, the act has made little if no difference to small enterprises in India; and in the words of the general secretary of Fisme Anil Bhardwaj, it is "basically a promotional act" which "doesn't have any teeth".³⁹

Added to this, not all the facilitation councils have been set up so far. Only 13 of the country's 35 states and territories had set up one as of March 2010. However, the uptake of cases to the councils is affected by business owners staying away from the councils, fearing that though they may be able to recover their outstanding money by taking an entity to a council, that entity will simply never want to do work with them ever again. This problem also applies to payment delays: a trained engineer, Chander Goel, who owns Goel Engineers, said public sector companies and large companies took a minimum of three months to pay him. He has already stopped supplying one public-sector company because they were taking too long in paying him. He said that whereas under the MSME Act one can complain when payments are not made within 60 days, this was not "a practical solution". "When you make a complaint, next time you are not going to get the business," he said.⁴⁰

BUSINESS SUPPORT

The National Small Industries Corporation (NSIC) which has been tasked by government to support small businesses was also criticised, including most notably by a leading small-business financier running a government-backed fund and by Milagrow's Karwal. Karwal points out that the NSIC has made next to no impact in supporting small businesses, other than in its warehousing of raw materials programme (See Chapter 4 on schemes).

Dr HP Kumar, the NSIC's chairman and managing director, however disagrees. He says the corporation has made an impact and has been "highly successful" in assisting small enterprises. He points out that the amount of total manufacturing sector output contributed by MSMEs and the fact that these entities

³⁷ Interview with Rajeev Karwal, New Delhi, March 2010.

³⁸ Interview with Anil Bhardwaj, New Delhi, March 2010.

³⁹ Interview with Anil Bhardwaj, New Delhi, March 2010.

⁴⁰ Interview with Chander Goel of Goel Engineering, New Delhi, March 2010.

contribute 40% of exports, is evidence of this. Added to this, the sector has raked up growth of 12% to 13% in recent years. Kumar's view is that the sector needs further support, not protection or reservation or direct grants and subsidies, but rather support through programmes like the government's scheme which subsidised ISO 9001s, to build the capacity of small businesses.⁴¹

However new developments in India could introduce changes to small business support and the business landscape. In August 2009 after a meeting with 19 small business associations with Prime Minister Manmohan Singh, the prime minister constituted a task team in September that year to look into ways of boosting support to small businesses. The associations highlighted a number of things, such as the problem of obtaining finance from banks, the need for a focused procurement policy, the need for prompt payment of small businesses and simplification of labour laws. The task force subsequently submitted its report to the Singh (in January 2010). An expert group was formed by the government to look at recommendations for the promotion and development of micro, small and medium units. The group is headed by Planning Commission Member (Industry), Arun Maira.⁴²

CONCLUSION

The various problems India faces in the area of business support and as a result of its less than satisfactory institutional landscape are being dealt with following the task force meeting to ensure a further boosting of small businesses. One of the recommendations that has emerged from the resulting report to target at least 20% of the central government's purchases, from micro and small enterprises (MSEs), has however since been done away with (see section on market support in the Chapter 4).

Currently, the Development Commissioner (MSME) is the focal point for all policy matters, the formulation of various promotional and developmental schemes as well as channelling certain incentives and subsidies to the MSME sector; the Small Industries Development Bank of India (Sidbi) is the principal financial institution for financing and related promotional and development work for small businesses, while the National Small Industries Corporation Limited (NSIC) has been set up to facilitate MSMEs in procurement of raw material and helping in marketing of their products. The idea is that the proposed independent body could use the existing structures of these organisations after making appropriate changes in their charter and mandate.⁴³

India's support for small businesses has been less than impressive, in a country also marred by high corruption (see Appendix 5). This may well play a part, along with the country's confusing and clumsy government support architecture for small businesses (see Appendix 2 for details).

Brazil

- Strong policies, driven by measurable targets set by the country's planning ministry and backed by recent laws have seen Brazil make marked progress in supporting small businesses.
- However, business owners still battle with red tape and to access finance.
- Idea to set up small business ministry receives support.

In contrast to South Africa and India, Brazil's small business policies appear to have made some impact. Backed by strong reference to the support of small business in its national plans, the South American country is working overtime to boost support to small businesses, from informal street traders to more established small businesses.

The Brazilian government's policy on small businesses is contained principally in Lei Geral, a law passed in 2006 which has simplified taxes for small and micro firms and boosted government procurement among other things.

⁴¹ Interview with HP Kumar, New Delhi, March 2010.

⁴² Yahoo News India: <http://in.news.yahoo.com/20/20100303/372/tbs-govt-constitutes-expert-group-for-ms.html>

⁴³ Indian government press releases: <http://pib.nic.in/release/release.asp?relid=57553>

A recent addition is the Empreendedor Individual (Individual entrepreneur) law, approved in 2008, which aims to help informal one-man-show entrepreneurs (who do not have a share in any other business and who have an annual income of up to R\$36 000) to formalise and to therefore have access to social benefits such as pension and medical aid and workman's compensation. To simplify the registration of these types of entrepreneurs wanting to benefit from the law, the Ministry of Development Industry and Commerce (MDIC), which oversees the development of small businesses, launched an internet portal in 2009 where entrepreneurs looking to formalise can sign up. The law also reduces the number of steps and pieces of information (41 to seven) an entrepreneur is required to follow to register and offers them lower taxation.⁴⁴

The promotion of small businesses forms an important part of the federal government's four-year Pluriannual plan, at a time when Brazil is increasingly debating the role small enterprises can play in creating equitable growth. Under the Brazilian constitution, each newly-elected government must submit a multi-year plan, or Plano Plurianual, to guide public policy. The plan outlines major objectives, challenges, and guidelines for the government as well as programmes and actions for the achievement of these objectives. An important emphasis in the 2008-2011 plan is the need to strengthen innovation in Brazil if the country is to grow and meet its goal of regional and social inclusion. Another is to target 3.8 million small and micro businesses by 2011 with loans.

The goals in the Plano Plurianual 2008-2011 for MDIC concerning small businesses⁴⁵ name 65 actions distributed in four challenges: continuing to implant Lei Geral in more municipalities, the participation of micro and small enterprises in the local and international market, improvement of management and the increase in capacity of innovation in these enterprises and incentivising them to join associations and co-operate.

One of the measurable goals is to ensure that by 2011, 65.42% of all jobs in the formal sector are created by small, medium and micro enterprises. In 2008 the Brazilian government exceeded this target, with a figure of 65.21%. The projection for 2011 is to reach a target of 68.24%. Another goal is to increase the percentage of micro and small enterprises involved in exporting, with a goal to have 8.58% of all small and micro firms exporting by 2011. In 2008 the figure reached 6.58%.

The plan also sets various goals for assisting small businesses to commercialise, gain access to the international market, for research on clusters and for financing SMEs through specific programmes of Caixa, Banco do Amazônia and Banco do Brasil.

A recent development in 2010 was the suggestion to create a small business ministry by the country's outgoing President Lula. Policymakers will have to wait and see what will come of this.

SUCCESS & PROBLEMS

The Brazilian government, it appears, is not doing too badly on disbursing finance to small businesses. Of the five government funds mentioned in the evaluation report for MDIC under the Plano Plurianual 2004-2007, two exceeded their target in loans lent out and amount of finance lent out, with a further two falling just short of meeting their respective lending target.⁴⁶

However an assessment by the Ministry of Planning, Budgeting and Management of MDIC's goals in the last Plurianual (2004-2007)⁴⁷ revealed that very few of the government's goals to promote small enterprises, were achieved. It found that the MDIC was hindered in achieving some of the goals because of the difficulty in obtaining from the fiscus certain statistics needed to measure the government's performance in assisting small businesses. Measures have since been amended for the 2008-2011 plan.

⁴⁴ Tres Anos da Lei Geral da Micro e Pequena Empresa, Sebrae publication, 2010

⁴⁵ Relatório de Avaliação do Plano Plurianual 2004-2007: MDIC Caderno 18, 2009.

⁴⁶ For example, the state's Banco do Brasil handed out 1.6 million loans to medium, small and micro firms, slightly below the target set of 1.8 million. But it exceeded the R\$25.9-billion target for finance handed out, disbursing R\$31.8 billion in 2008.

⁴⁷ Relatório de Avaliação do Plano Plurianual 2004-2007: MDIC Caderno 18, 2008

There were nevertheless some successes in the last plan, including the setting up of the Permanent Forum for Micro enterprises and small business (Fórum Permanente das Microempresas e Empresas de Pequeno Porte e da Portaria) in 2007, which has enabled members from the private sector and the government to discuss problems related to the SME sector and to together develop solutions.

What is notable is that Brazil's planning ministry is already preparing for the effect an increasingly entrepreneurial workforce will have on the economy. Roberto Mangabeira Unger, a Harvard University lecturer and former chief minister of the Secretariat of Long-term Planning between 2007 and 2009, believes the Brazilian economy is moving from a wage-based economy to a entrepreneur-based economy.⁴⁸ Unger's ascertain is that with its hefty labour laws and institutions mainly geared to serving big businesses, Brazil is not sufficiently prepared to face this new challenge.

The move towards an entrepreneur-based economy has all sorts of consequences for the country. With many one-man businesses and contractors having formalised their operations through the Individual Entrepreneur law, questions have already been raised about whether many of these businesses are actually businesses at all, or whether the business owners were really just employees masquerading as contractors. The problem is that if these business owners register under the law they access special conditions which bypass labour laws. Employers could therefore be encouraging employees to register to get past the country's strict labour laws.

The Presidency's Secretariat of Strategic Issues (Secretaria de Assuntos Estratégicos) is currently evaluating the performance of the various government policies aimed at SMEs which have been put in place in the last 10 years (including Lei Geral, clusters and the Individual Entrepreneur law). So far many in the private sector are generally positive about the government's SME policies. José Dornelas of Empreende, which provides business training and consulting services to business owners, believes the state had come to see supporting small and medium enterprises (SMEs) as a way to develop the country. And Dr Joseph Couri the president of employer's association Simpi, which represents businesses with 50 or fewer employees and has 100 000 members, pointed that Brazil is working "rapidly and intensely" to solve problems faced by SMEs.⁴⁹

Milton Bogus, the director of the micro, small and medium department (Dempí) at Federação das Indústrias do Estado de São Paulo (Fiesp) said with the passing of Simples Federal (the country's new tax for small business through Lei Geral in 2007) it was possible that small businesses with a turnover up to R\$2.4m to be taxed less and be prioritised government procurement of up to R\$80 000, among other advantages. He said one unfavourable aspect of the current Simples Federal is that the turnover for SMEs is set very low though this has been amended to increase the turnover threshold to R\$3.6 million.

Despite these changes, small businesses in Brazil still battle to obtain finance and lower interest rates from banks and funders. There are still too many procedures to open and close a business in Brazil. The 2009 Gem Report on Brazil also suggested that, among other things, state agents should provide incentives to create angel funding networks.⁵⁰ The report also suggested that the government should set up and rigidly apply indicators to evaluate its vast number of entrepreneur support programmes. Many interviewees that Gem spoke to in compiling its 2009 report on Brazil, indicated that heavy bureaucracy and red tape were key reasons why many Brazilian entrepreneurs opted to remain in the informal economy. Incorporating a start up requires 15 procedures, three times more than in the US.

Noting the above, according to Gem's 2008 report on Brazil, a collection of experts from each specific participating Gem member country, rated Brazil's government policies as more favourable (-0.48) than those of South Africa (-1), Russia (-0.7), but behind policies of Chile (-0.2) and South Korea (about 0.2). Brazil's support for incubators and science parks was the main reason for the South American country's more favourable rating when compared to other rated emerging economies.

⁴⁸ Interview with Nabil Moura Kadri, a chief of cabinet in the Secretaria de Assuntos Estratégicos, Brasília, August 2010.

⁴⁹ Interview with Joseph Couri, São Paulo, August 2010.

⁵⁰ Angel investors provide equity, grants or capital to businesses, usually those that are starting up. Many of these investments are done on an informal or ad hoc basis.

Many such as Dornelas, support the idea mooted by Lula to set up a Small Business Ministry. However Nabil Moura Kadri, at the Secretariat of Strategic Affairs (SAE), though backing the need for more government support to small businesses, in contrast feels that setting up a ministry may not be the best way to assist the sector. He believes what may transpire instead will be a special secretary linked to the presidency, rather than a full ministry. He believes that co-ordination and evaluation is lacking when it comes to effective SME policies. Therefore, a separate unit is required that is dedicated to SME policies.

CONCLUSION

Despite some challenges specifically regarding the red tape small businesses face, the Brazilian government has achieved many successes in promoting small businesses. The country's Presidency has set clear and measurable goals contained in the country's overarching development plan (Plano Plurianual) and regular reviews of these targets by Brazil's Presidency are undertaken. The targets in the overarching plan allow for a co-ordinated support system among the various government departments and small business support agencies. This is something both India and South Africa could do well to learn from.

Conclusion on Policies

India and South Africa, whose policies have made little impact on small businesses, can learn much from Brazil in the way that it devises its small business policies which are backed by measurable targets set by its planning ministry. Also, South Africa's planning must centre more around not only targets but a long-term vision about what the country wants in terms of how its economic ownership should look like, as in the case of Brazil which is already planning for a shift from wage-based employment to a more entrepreneurial-based system.

There is also a need to simplify the government's architecture of support for small businesses. All too often when complaints are made of insufficient support to small businesses, the South African government simply sets up yet another agency or department, which only makes it more difficult to co-ordinate policy and programmes. Instead of growing bigger, the government must look to become smarter in the way it assists small businesses.

South Africa can also learn from Brazil in the way the South American country prioritises the building of partnerships. Brazil has a number of groups that focus on small business policies: the Permanent Forum on Micro Enterprises and Small Businesses, the Working group on clusters and the presidential group on small businesses. All of these contain members drawn from both the private sector and government. South Africa could learn from this to form a national consensus. Partnerships offer a plausible way to do this.