



# SME FINANCE NEEDS ASSESSMENT

QUALITATIVE AND QUANTITATIVE STUDY IN GAUTENG  
PROVINCE-FINAL REPORT

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# FINANCIAL SECTOR PROGRAM

**SME Finance Needs Assessment-Qualitative and Quantitative  
Study in Gauteng Province-Final Report**

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The authors' views expressed in this publication do not necessarily reflect the views of the United States Agency for International Development or the United States Government.



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## LIST OF ACRONYMS

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BDS	Business Development Services
BEE	Black Economic Empowerment
BSM	Business Sophistication Measure
CC	Closed Corporation
DBSA	Development Bank of Southern Africa
DTI	Department of Trade and Industry
FDI	Foreign Direct Investment
FI	Financial Intermediaries
FSP	Financial Sector Program
GEP	Gauteng Enterprise Propeller
HDI	Historically Disadvantaged Individuals
ICT	Information and Communication Technology
LRA	Labour Relations Act
NEF	National Empowerment Fund
ODA	Official Donor Assistance
PAYE	Pay-As-You-Earn
SADC	Southern African Development Community
SARS	South African Revenue Service
SEDA	Small Enterprise Development Agency
SETA	Sector Education and Training Authority
SME	Small and Medium Enterprises
UIF	Unemployment Insurance Fund
USAASA	Universal Service Access Agency for South Africa
USAF	Universal Service Access Fund
USAID	United States Agency for International Development
VAT	Value Added Tax

## EXECUTIVE SUMMARY

The Financial Sector Program (FSP) is an initiative funded by the USAID. The program's objectives are to expand access to financial services and lower financing cost for small and medium enterprises (SMEs) through reforming the legal and regulatory framework affecting the financial sector and business environment and improving the commercial viability of lending to historically disadvantaged SMEs in South Africa, thereby expanding SME access to a range of high quality and affordable financial services. The FSP has the following four project workstreams:

- Financial business development services (BDS);
- SME finance;
- Legislative and regulatory reform; and
- Knowledge management.

The important role played by SMEs in the South African economy is recognised by both the Small Business Act (1996) as well as the Financial Sector Charter. Government is increasingly looking to this sector as the source of job creation. Recent research show that members of the second economy are faced with distinct challenges such as access to markets, finance and business opportunities.

This study was commissioned by the FSP team with a view to gather and analyze key information about HDI SMEs in Gauteng on the four workstreams of the FSP project. The objective was to collect and analyze a broad range of detailed information on the financial needs of BEE SMEs, in order to accurately design and implement the next year work plan and determine the targets of the Performance Management Plan. This study will build on the 2006 FinScope small business survey, which delivered a comprehensive understanding of the small business market in the Gauteng province.

Since previous research showed that the Business Sophistication Measure (BSM) provides the most realistic assessment of small businesses, it was decided to use this model in the present study. It was decided to exclude micro enterprises from this study and rather focus attention on HDI SMEs in the BSM 6 and BSM 7 categories.

The approach followed by the research team was to engage on two research strategies, i.e. qualitative and quantitative methodologies. The quantitative strategy involved an analysis of the 2006 FinScope small business survey results, and the qualitative strategy was used by conducting focus groups across the province with HDI owners of businesses with an annual turnover of more than R200 000. A total of 11 focus groups were conducted in which 106 individuals participated.

### **The 2006 Small Business Survey**

The results show that there are about 109 000 HDI owned small businesses in the BSM 6 and 7 categories in Gauteng. This amounts to about 10% of all small businesses in the province. An analysis of the survey results showed that there are significant differences among small businesses when one analyzes them by the various BSM categories. The

degree of formality of the business increases as they progress from BSM 1 to BSM 7 with a significant increase in sophistication from BSM 6 to BSM 7. HDI ownership is more concentrated in the lower BSMs. The use of formal record keeping and business planning is limited among the lower BSMs with the highest in BSM 7. A similar trend was also observed in the case of ICT use. Compliance with legislative provisions such as being formally registered and complying with tax related requirements is significantly higher in BSMs 6 and 7 compared to the lower BSM levels. The most pressing problem that SMEs face related to access to finance to start and grow their businesses.

### **Results from the focus groups**

While there appears to be good awareness amongst small businesses of the existence and what fBDS providers provide, it is clear that few SMEs are using them. It is recommended that more in-depth research be done on the support services provided by private and public fBDS in terms of what they offer, the effectiveness of their services and how they communicate these services to potential customers. Simple information products, possibly in the form of a booklet or pamphlet, should be provided on the services offered by the various institutions. A key area to focus on is communication with SMEs.

Training workshops to address the needs of small businesses is also a recommended approach and is already used quite widely. Cognisance must be taken of the concerns of small businesses in terms of the time that they have available and the limited financial resources they have to pay for them. One area that should be investigated further is the development and implementation of effective sector specific mentoring programmes for small business owners. A key area of focus should be financial literacy.

A strategy needs to be developed to improve awareness of the support provided by fBDS and to ensure that SMEs use them more effectively. Another concern raised was that fBDS providers be located closer to where the historically disadvantaged SME business premises are situated. There is also a clear need for fBDS staff to be better trained in being more responsive to the needs of small business owners.

While respondents reported that in general they were able to open and operate bank accounts, they find that obtaining access to finance from outside sources for their business is extremely difficult. The challenges were not confined to formal financial institutions alone but included the support institutions as well. This has resulted in much of the external funding for business being secured from informal sources (i.e. family and friends) or to an even larger degree from personal savings, pensions etc. Black males and to a larger extent female respondents, were more challenged than their Coloured and Indian counterparts when it comes to financial access and in the majority of cases, the sentiments were more forcefully expressed in the Black groups. Lack of proper records (including proper financial statements) hinders the participants in dealing with FIs and fBDSPs.

The staff of FIs need training to change their mindsets and better understand the needs of HDI SMEs. For the same reason, some changes in financing terms and conditions would be helpful.

From the input received from SMEs participating in the focus groups it can be concluded that more information and training on all aspects relating to the registering of businesses, the Labour Relations Act and BEE legislation is required. More specifically training is needed on what the business opportunities are that arise out of the BEE legislation. There is also a need to locate more public institutions within the communities of historically disadvantaged SMEs. These institutions also need to be given greater support to enable them to strengthen the business and community associations.

It is recommended that the information needed by SMEs be published in a handbook. More intensive media campaigns can also be developed on the topics described above. This may well require the development of programmatic material and holding intensive discussions with appropriate media groups. Further research could be done on mechanisms of establishing effective associations and forums in disadvantaged areas that can address the specific needs of small businesses. Finally, there is also a need to conduct research into problems associated with the BEE policy and its procedures.

Generally small businesses are not sharing their experiences and learning with one another. As a consequence there is little evidence of their being a benefit. However, they are unanimous in acknowledging the value of knowledge and information as well as ICTs to their businesses. It is for this reason that there is a call for the greater support of forums and workshops as well as training so that business owners can reap the benefit. Cognisance must be taken of the needs and challenges of small businesses in using knowledge and information management approaches (e.g. literacy, language).

It is also recommended that a knowledge portal be developed that will enable the sharing of knowledge and learning amongst SMEs in South Africa. One of the things that the knowledge portal would contain is a database of all Chambers of Commerce, associations and forums that enable the sharing of knowledge and learning amongst SMEs. The value of the knowledge portal is that it provides a single repository for information and handbooks on policies and regulations, SME practices, tax and registration, access to finance and financial business development services. It could also be a place where training events, workshops and business Expos could be advertised. The knowledge portal would also provide access to accredited on-line training courses for SMEs. It could also feature articles by prominent business people on different aspects relating to managing and running small businesses.

## CHAPTER 1: BACKGROUND

### 1.1 Introduction

South Africa has made significant progress during the past 10 years in consolidating democracy and in creating an environment in which economic growth can take place. The period before 1994 was characterized by high levels of political violence, undemocratic governance structures and a general disrespect for human rights. The economy was characterized by high inflation, large fiscal deficits, declining investments and negative growth.

Since 1994 the country has made significant progress in establishing and deepening democracy. Three national elections and two local government elections have taken place and governance structures have been established which are regarded by the vast majority of the population and the international community as legitimate. In fact, South Africa's transition to democracy is regarded as a model for several other countries that currently suffer under the yoke of undemocratic systems of government and civil strife.

On the economic front South Africa has achieved a higher degree of macro-economic stability and fiscal robustness. The recent past has seen improved GDP rates, a decline in inflation and an improving investment climate. By 2005 foreign direct investments to South Africa appear to have reached record levels. The latest estimate for FDI inflow to South Africa is US\$ 7.2 billion. This is a significant increase compared to the annual average for the period 2002-2004 of US\$ 700 million.

In spite of this, South Africa faces considerable socio-economic and socio-political challenges. These include the sustainability of economic development, the reduction of absolute and relative levels of economic inequality and the social and political vulnerability of the poor. At the same time the South African Government and partners need to mitigate the impact of the HIV/AIDS pandemic. In order to both deliver on the skills needs of the country and to become globally competitive in the long term - while addressing the legacy of underdevelopment - particular attention had to be given to these priority areas much of which have been captured in the South African government's Program of Action, the Millennium Development Goals, and country strategy papers of several donors that provide ODA support to South Africa and the SADC region.

For all these reasons it has become imperative that South Africa develop a coherent and structured strategy that:

- Provides for the poor and disenfranchised;
- Is responsive to the ever-changing influences of the external environment;
- Promotes the development of a nation that is committed to sustained development; and
- Strengthens democratic governance at all levels of government and civil society.

Policy development and appropriate implementation strategies to support the above are key for the success of government's priorities. Such policies need to be underpinned by

sound research that asks the right questions in order to address key priority areas. The continued involvement of a range of stakeholders in such endeavours is imperative for their success.

Much of the progression since 1994 across sectors has benefited from sustained support from the international community of donors. Currently Official Development Assistance (ODA) amounts to slightly less than 2% of the country's budget and about 0.3% of GDP. Together some 30 donor countries and multi-lateral organisations provide financial and technical support to the South African Government in its efforts to achieve the country's developmental goals with the European Union being the largest single donor to South Africa.

Donor support from the United States is directed at the education and health sectors as well as the advancement of democratic consolidations and economic growth. The financial commitment of the United States for the period October 2007 to September 2009 comes to about \$740 million<sup>1</sup>. The Financial Sector Programme, with a budget of \$14 297 997, is part of this commitment.

## **1.2. The Financial Sector Programme**

The Financial Sector Program (FSP) is a USAID/Southern Africa financed program designed to support the accomplishment of the U.S. Government's Economic Growth Objective in South Africa.

The objectives of FSP are to expand access to financial services and lower financing costs for small and medium enterprises (SMEs) through reforming the legal and regulatory framework affecting the financial sector and business environment and improving the commercial viability of lending to historically disadvantaged SMEs in South Africa, thereby expanding SME access to a range of high quality and affordable financial services. The FSP has the following four project work streams:

- Financial business development services (BDS);
- SME finance;
- Legislative and regulatory reform; and
- Knowledge management.

The FSP project team in consultation with USAID/South Africa agreed to produce an interim work plan focusing on the first three months of the project to be followed by a 12-month annual work plan at the end of this period. During this initial period, one of FSP's goals is to complete a thorough needs assessment and an inventory of stakeholders and partners in the four project components.

## **1.3. The context of SMEs in South Africa**

One of the key characteristics of the South African economy is the relative high level of SME activity compared to similarly situated economies of the world. A recent World

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<sup>1</sup> Information supplied by International Development Corporation (IDC) Unit, National Treasury.

Bank study suggests that among upper-middle-income countries for which data is available, South Africa had 58 SMEs per 1 000 inhabitants in 2006. The results suggest that only Mauritius has a higher level of SME activity ó just above 60 per 1 000 inhabitants ó than South Africa. The remarkable growth in small business activity is highlighted by the fact that the survey conducted in 1997 showed that there were only 22 small businesses per 1 000 inhabitants at the time. These results suggest that small business activity in South Africa has more than doubled in ten years.

The South African government recognised the important role small businesses can make to the economy. This is, among others, demonstrated by the National Small Business Act (No. 102 of 1996) which makes provision for the establishment of a National Small Business Council as well as the Ntsika Enterprise Promotion Agency. The functions of the Agency are to expand non-financial support to small businesses and to provide financial support to service providers to small businesses.

The Financial Sector Charter represents another initiative by various stakeholders in the financial sector to improve its engagement and service to small businesses ó in particular BEE related businesses.

A general view is the small businesses play an important role in a growing economy ó especially in terms of its contribution to job creation. Some suggest that small business account for as much as 42 percent of all employment in the private sector.

An important reality of the South African economy is what some have referred to as the dual economy. Businesses in the first economy (the formal sector) have relatively easy access to credit. Their counterparts in the second economy ó characterised by its informal nature ó lack such easy access. In fact the results of several research studies suggest that access to finance is one of the most significant problems faced by small business owners.

#### **1.4. The AfricaScope brief**

It was against this background that the FSP team approached AfricaScope with the request to conduct a study in the Gauteng province to gather and analyze key information on the four components of the FSP project.

FSP is trying through the AfricaScope study to collect and analyze a broad range of detailed information on the financial needs of BEE SMEs, in order to accurately design and implement the next year work plan and determine the targets of the Performance Management Plan. This study will build on the 2006 FinScope small business survey, which delivered a comprehensive understanding of the small business market in the Gauteng province.

Since the mandate is to only focus on BEE SMEs and not on micro-enterprises, only businesses belonging to the BSM (Business Sophistication Measure) 6 and 7 categories have been included in this study. Some of these businesses fit under the Banking

Association SME definition<sup>2</sup> (annual turnover between R500 000 and R20 million). However, since the results of the 2006 FinScope survey showed that most of the HDI SMEs fall below the minimum threshold of R500 000, it was decided to set the bottom threshold for this study at R200 000, thus excluding micro enterprises from the study. This will enable the FSP team to gain a better understanding of those SMEs that find themselves just below the Banking Association's bottom threshold. It is expected that initiatives directed at this group will enable them to progress into the higher turnover band.

The AfricaScope study was designed to add more granularity to the FinScope survey for BSM 6 and 7, and will provide important answers to specific questions raised by the FSP team about financial needs and products, business development services, and regulatory constraints affecting the growth of BEE SMEs.

#### **1.4.1 Project activities**

To accomplish the study within the timelines provided by the FSP team several activities needed to be executed. They are:

- The analysis of the FinScope SME survey data and the writing of the report.
- The production of the maps and the areas where respondents for the focus groups are to be selected need to be identified.
- The criteria for the selection of individuals to form part of the focus groups needs to be finalized.
- The piloting of the approach to identify suitable candidates for focus groups needs to be undertaken.
- The development of a discussion guide for the focus groups.
- The recruiting of suitable participants in the identified areas in Gauteng province.
- The focus group discussions;
- The transcription of the focus group discussions.
- The preparation of a report which highlights the results of the focus groups.

#### **1.4.2 Project deliverables**

The project has the following deliverables:

- Implementation Plan, BSM concentration Maps and Discussion Guide.
- A detailed report on the quantitative analysis of the 2006 FinScope SME survey for BSM 6 and 7, based on the questionnaires prepared by the FSP team.
- A series of short reports on the results of the different focus groups that will be organized for the qualitative analysis.
- A comprehensive report that will present a synthesis of the qualitative analysis, with conclusions and recommendations, and a complete set of maps of the areas of high BSM 6 and 7 concentration in the Gauteng province.

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<sup>2</sup> The same definition was used in to Financial Sector Charter.

- A Power Point presentation of the FSP/AfricaScope SME study that will encapsulate the main findings of the qualitative and quantitative analyses, with the appropriate maps.

### **1.5. Organisation of this report**

The next chapter of this report provides a brief discussion of the methodology followed in this assessment. Key challenges that were encountered are also highlighted. Chapter 3 reports the most significant results of an analysis of the 2006 FinScope small business survey. This is followed in Chapter 4 by a description of the GIS analysis of the 2006 FinScope results that was used to locate the target areas in which focus groups were conducted. Chapter 5 provides a brief description of the demographic characteristics of the focus group participants. The results from the focus group discussions pertaining to BDS are discussed in Chapter 6. Chapter 7 addresses pertinent results pertaining to banking and financial services. Chapter 8 provides an analysis of the issues raised during the focus group discussions pertaining to legislative and policy matters. Knowledge and information management is addressed in Chapter 9. The report is concluded with a summary and recommendations in Chapter 10.

## CHAPTER 2: METHODOLOGY

### 2.1. Approach to the study

As mentioned in Chapter 1 above, the brief required two research activities. Firstly, to conduct an analysis of the results 2006 FinScope Small Business Survey that was conducted in Gauteng, and secondly to conduct focus group interviews with owners of small businesses with an annual turnover of more than R200 000. In both cases the study focused on HDIs only.

The first activity was fairly straight forward to undertake since the survey results were already available. While the results of this analysis are the subject of a detailed separate report, we do provide a brief summary of the main findings in Chapter 3.

The second research activity required that new primary research be designed and conducted. The unique focus of this study required an approach that would enable the research team to not only locate and access small business owners that fall within the scope of the study, but also to ensure that the results to be obtained would enable the FSP team to develop its work plan and activities in an adequately targeted fashion.

The brief required that focus group interviews be conducted across Gauteng with business owners that fit the selection criteria. Since no data set of this nature existed and given the relatively small numbers of HDI business owners in the province, it was like finding a needle in the haystack. This challenge was overcome by employing GIS technology. More specifically detailed maps were developed based on the results from the FinScope survey to identify those areas in Gauteng with the highest concentration of small business owners that needed to be interviewed, i.e. business owners in the BSM 6 and BSM 7 categories (see Chapter 4 for a more detailed discussion of this approach).

### 2.2. Selection of areas in Gauteng

The above analysis enabled the research team to identify the areas in Gauteng with the highest concentration of BSM 6 & 7 businesses. The target group in each area was decided in consultation with the FSP team. Focus group interviews were arranged in the following areas:

Area	Target group	No of participants
Alexandra	African	8
Eersterust	Coloured	22
Eldoradopark/Florida	Coloured	12
Laudium	Asian	12
Lenasia	Asian	7
Mamelodi	African	10
Pretoria CBD	African	12
Soshanguve	African	9
Soweto	African	10
Tembisa	African	8

A more detailed profile of participants is provided in Chapter 5.

### **2.3. Selection criteria for focus group participants**

Participants were selected by way of the following strategy. Recruiters were deployed in the selected areas where they systematically worked through the area by approaching individuals who appeared to be operating a small business. This could be either from a formal business premises or from a house or other property.

Once it was confirmed that the individual is indeed a small business owner he/she was informed about the background and objectives of the study and were invited to participate. If the individual agreed to participate the recruiter completed a short selection questionnaire (see Annex A) which recorded basic information about the business such as years in operation, number of employees, sector of the economy, turnover and contact details of the owner. The owner was subsequently informed of the location of the focus group meeting and transport was provided in some instances. In some cases participants were recruited with the assistance of the local business forum.

The following served as the primary selection criteria for focus group participants:

- The participants should be a HDI that owns a business;
- The business's annual turnover should be more than R200 000.

### **2.4. Discussion guide**

The focus group discussion was conducted with the aid of a discussion guide. This document was developed by the research team in collaboration with the FSP team so as to ensure that the relevant areas of concern are covered during the discussion (See Annex B). The discussion guide was structured along the four workstreams of the FSP mentioned earlier in the report. The initial document was revised after a pilot focus group in Pretoria.

### **2.5. Practical matters in the field**

Research of this nature often provides the research team with significant challenges. This project was no exception ó especially given the unique approach and focus of the study.

The most significant matters that were encountered were:

Identifying business owners who met the requirements for participation

Individuals who were recruited often could not take time out from their businesses due to the fact that they managed the business themselves on a fulltime basis. This meant that focus groups as a rule had to take place after hours and over weekends.

Prospective participants often did not present themselves on the agreed time and at the venue. This resulted in some focus groups being cancelled and/or rescheduled on more than one occasion.

A total number of 173 participants were required. Of these 106 participated in the focus groups.

## **2.6. Focus group proceedings**

The focus group discussions were facilitated by a member of the research team by following the structure as set out in the Discussion Guide. Proceedings were recorded electronically and transcribed for further analysis by the research team.

Members of the FSP team also attended the focus group discussion and asked questions throughout.

## **2.7. Conclusion**

Since the approach followed did not present the research team with unexpected challenges that may undermine the credibility of the results, the team is of the opinion that the findings in this report provide a fair reflection of what transpired during the research process. It should also be pointed out that by the very nature of focus groups, the results cannot be regarded as representative of all HDI SMEs. Rather, they provide a first cut understanding of the reality in which these businesses operate.

## CHAPTER 3: THE 2007 FINSCOPE SMALL BUSINESS SURVEY<sup>3</sup>

### 3.1. Introduction

Although the role of small business has been recognised as very important, the SME market place has to date been too poorly monitored and understood to be effectively managed and developed. The lack of information and understanding means that servicing, assisting and measuring this sector of the economy is a virtual impossibility.

A key implication is that small businesses require specifically tailored products, services and assistance programmes, which need to go beyond simply targeting a single parameter of defining small businesses for example informal and formal or small and micro, but need to consider the possible overlap of other parameters.

The FinScope Small Business survey was commissioned by the FinMark Trust in 2006. The primary objective of the research was to size the small business market in Gauteng. The FinScope Small Business Survey aimed to address the various parameters of small business activities with the explicit intention of sizing, benchmarking and segmenting the market for the first time. The survey findings suggest that the total number of small business owners in Gauteng comes to about 1 053 818.

Small businesses have traditionally been classified based on one characteristic for example whether it was registered or not, i.e. formal vs. informal, the number of employees or according to business turnover. The Business Sophistication Measure (BSM) was developed by AfricaScope with a view to provide a more comprehensive composite measure of businesses. The BSM is a measure based on a range of variables which include all of the above but also goes beyond incorporating variables such as use of ICT, record and bookkeeping, registration for taxes, whether banked or not, partners and shareholders, and business insurance to name but a few.

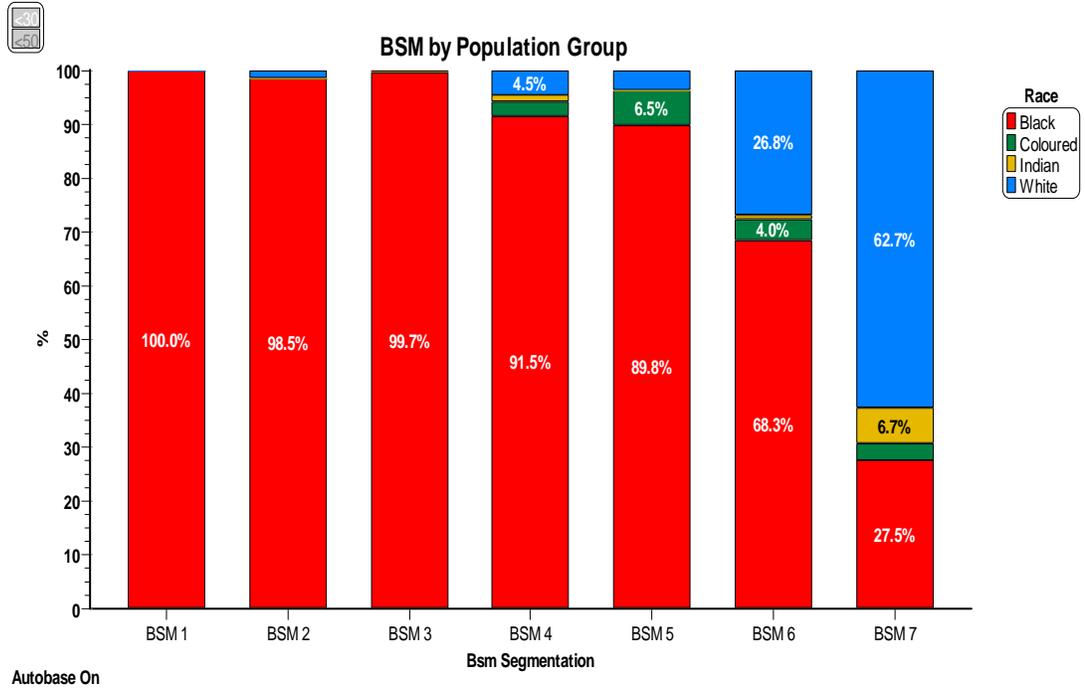
This measure enables the classification of businesses from BSM1 up to BSM 7 with BSM 1 being the least sophisticated and BSM 7 the most sophisticated.

### 3.2. Overview of BSM 1 to BSM 7

The information presented in Figure 1 clearly shows that African ownership of small businesses decreases as we progress from BSM 1 to BSM 7. For its part, white, coloured and Indian ownership becomes more prominent from BSM 5 and higher. This suggests that these groups are able to structure their businesses in a much more formal way than Africans. This is obviously the result of historical reasons which limited access to the adequate education and the business sector.

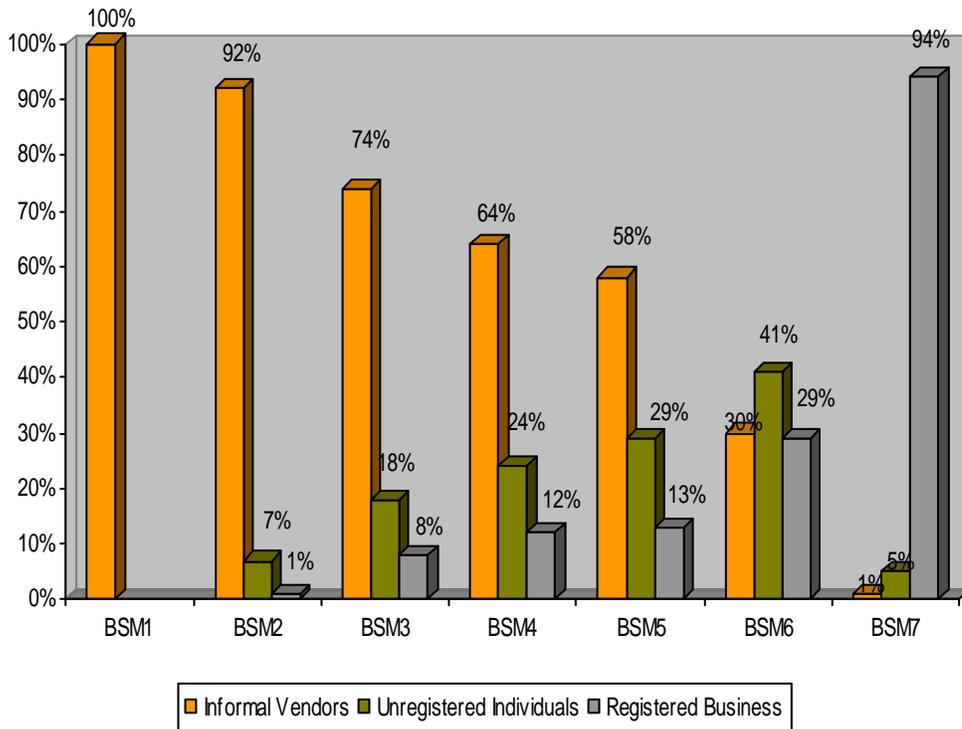
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<sup>3</sup> See Annex C for the Complete Survey of BSM6 and BSM7



**Figure 1: BSM by population group**

A similar trend is evident when one considers the degree of business registration. The lower BSM categories tend to be informal traders while those in the higher BSM categories are increasingly more formal ó either as individuals or registered businesses.



## Figure 2: BSM by type of registration

When one considers BSM 6 and BSM 7 only, significant differences come to the fore. The results in Table 1 show that about 29% of businesses in the BSM 6 category are registered compared to 94% in BSM 7. In the case of BSM 6 73% are owned by HDI compared to 37% in BSM 7. Less than one in five (18%) in BSM 6 have partners or shareholders in their businesses. The comparable number for BSM 7 is 40%. The use of ICT increases significantly from BSM 6 to BSM 7 as do the keeping of financial records.

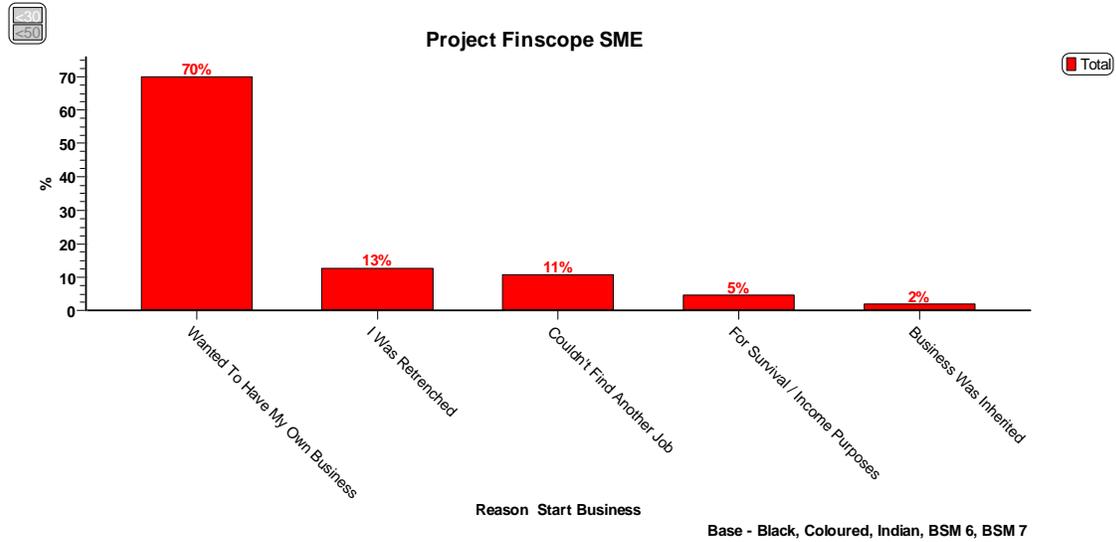
**Table 1: BSM 6 and BSM 7 by selected variables**

	<b>BSM 6</b>	<b>BSM 7</b>
Registered	29%	94%
HDI owned	73%	37%
Self taught	46%	26%
Full-time	92%	96%
Banked (personal or business)	81%	97%
Aware of support organisations	52%	85%
VAT registration	26%	83%
Cost of compliance too high	70%	43%
Shareholders/partners	18%	40%
Financial records	67%	96%
Bookkeeper member of staff	50%	7%
Business plan	18%	55%
Telephone/landline	36%	78%
Computer	20%	73%

### 3.3. Results from the survey pertaining to BSM 6 and BSM 7

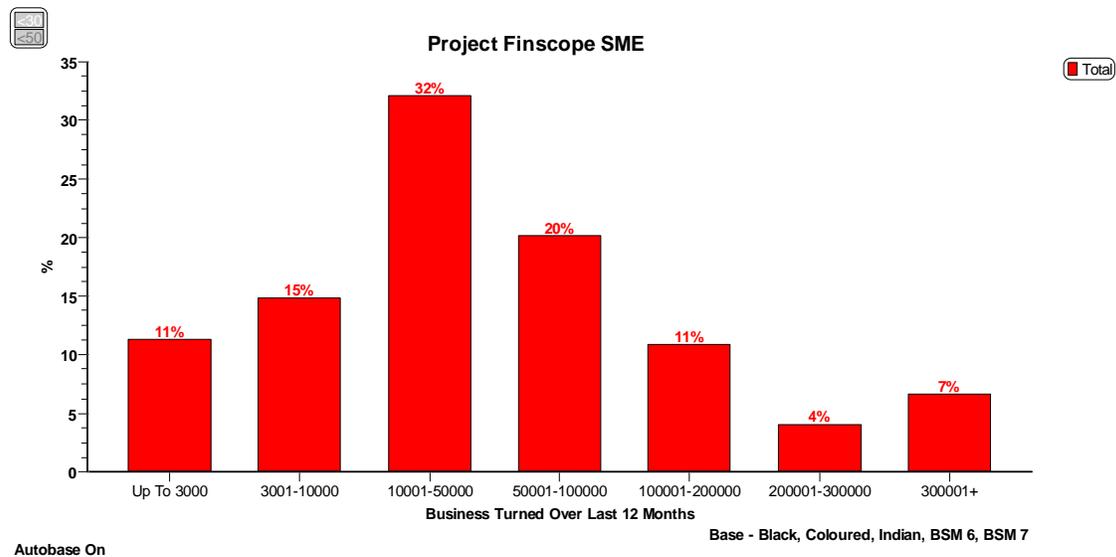
The remainder of this section presents the result from the 2006 survey pertaining to HDI business owners in the BSM 6 and BSM 7 categories only. The FinScope survey showed that there are an estimated 109 000 previously disadvantaged individuals in BSM 6 and 7 in the province of Gauteng who own and run their own businesses.

Unlike the 'lower' BSM groups, the target segment started their own businesses because they have always wanted to run their own business rather than through necessity.



**Figure 3: Reasons for having a business**

One of the major drawbacks to interest in and the overall development of the small business sector as a whole has been the size of the businesses. The declared turnover of the HDI businesses in BSM 6 and 7 in the last 12 months is not particularly high with only 7% declaring income of over R300 000 while 78% declared income under R100 000.



**Figure 4: Turnover**

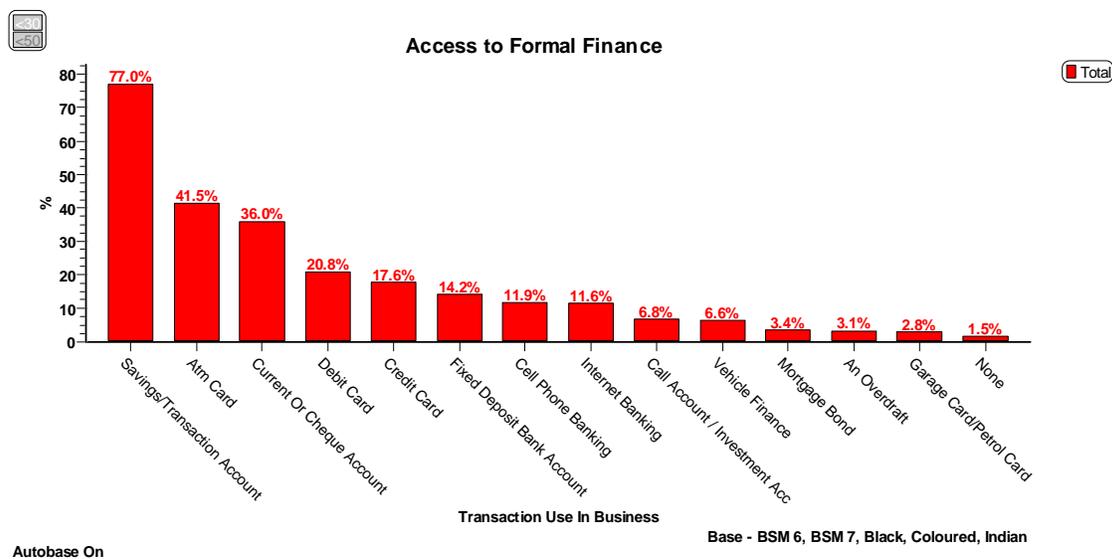
The majority of HDI individuals in BSM 6 and 7 have either a personal bank account or a business bank account or even both of these, however, only 2% of this group claimed to have a loan.

The fact that only 2% claim to have a loan means that the base sizes in this survey are very small and the analysis of the reasons for not having a loan should rather be handled

in the qualitative focus group work. Having said this, the lack of financial record keeping on the part of the business owners does complicate matters from a formal financial institutions perspective in the ability to access the viability of the business and the soundness of the loan repayment.

The approach to the market by financial institutions needs to change and a better understanding of the needs and challenges faced by small businesses obtained. Innovation in terms of product offering and revised credit scoring approaches needs to be developed ó this will not be helped by the stringent controls placed on banks by the new Credit Act.

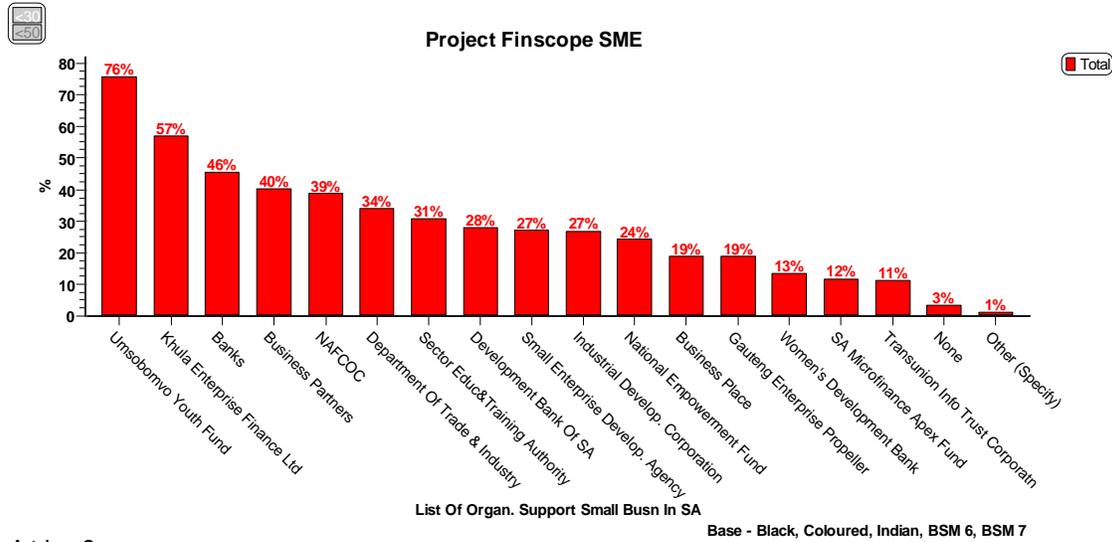
The savings account has the highest level of penetration of all financial product options available, with only around a third having a cheque account.



**Figure 5: Access to finance**

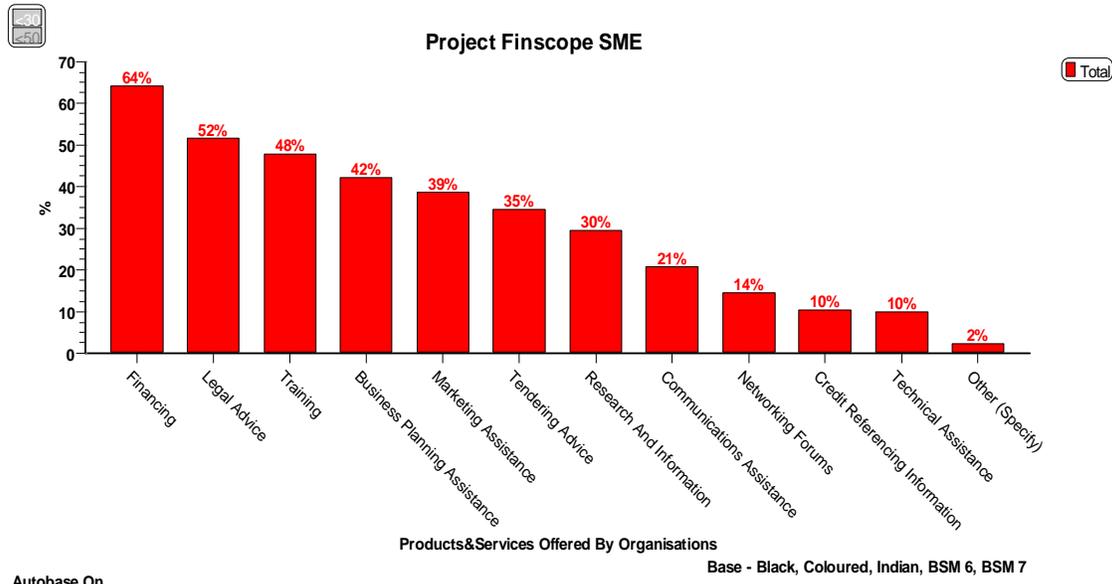
The survey showed that the business owners experience numerous problems when starting out and access to finance is a significant obstacle.

In terms of support for small businesses, there is significant awareness of institutions established to support small businesses.



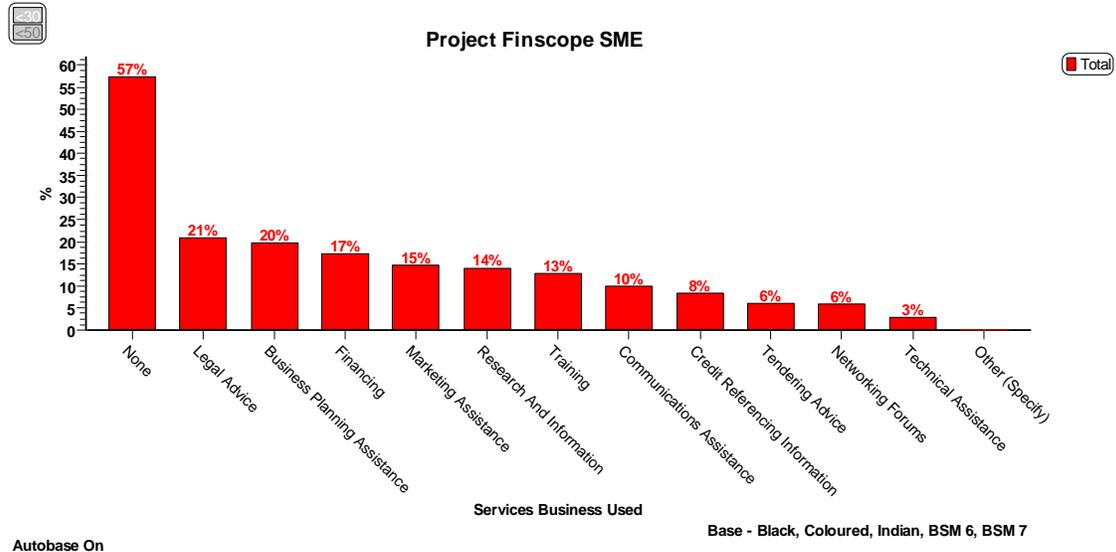
**Figure 6: Awareness of business support institutions**

The awareness of products offered by these institutions is also significant with finance being top-of-mind.



**Figure 7: Awareness of products**

The usage of these services does not match the awareness with 57% claiming never to have used the services.



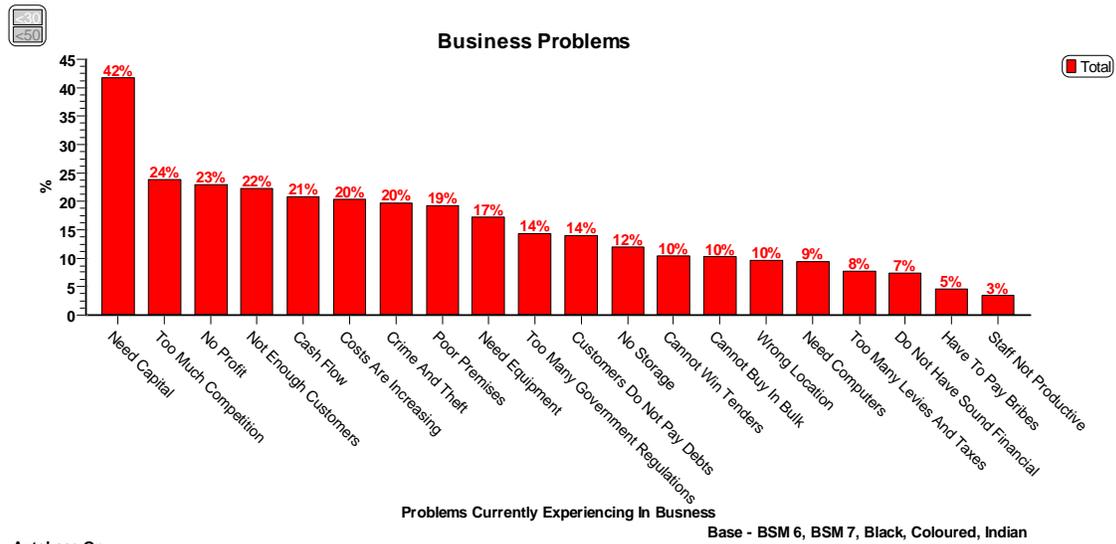
**Figure 8: Usage of services**

Clearly there is a need for the business support institutions to segment the small business market and to individually structure their approach to the market to become more relevant and effective within their defined segment, rather than all having a catch all approach.

The importance of the small business sector to the growth of the economy overall will be significant if this sector can be further developed as a sustainable and vibrant market. Much has been done up to now but there is clearly a need for improvement. The policy framework within which the businesses operate needs up-dating, financial institutions need to become more innovative in this segment and the level of skill within the segment needs to be improved.

In many instances the personal bank account is used in preference to opening a business account and the reasons why HDI businesses use their personal accounts are largely for reasons like: their business is too small, or they don't need a special business account, it's too complicated to open a business account, the costs are too high, their business and personal affairs are one and the same or that they simply haven't registered the business. In many cases the financial institutions could overcome these attitudes via more selective marketing and targeting of businesses that show greatest potential.

The overwhelming problem faced by businesses in the target category is the need for capital.



**Figure 9: Problems experienced**

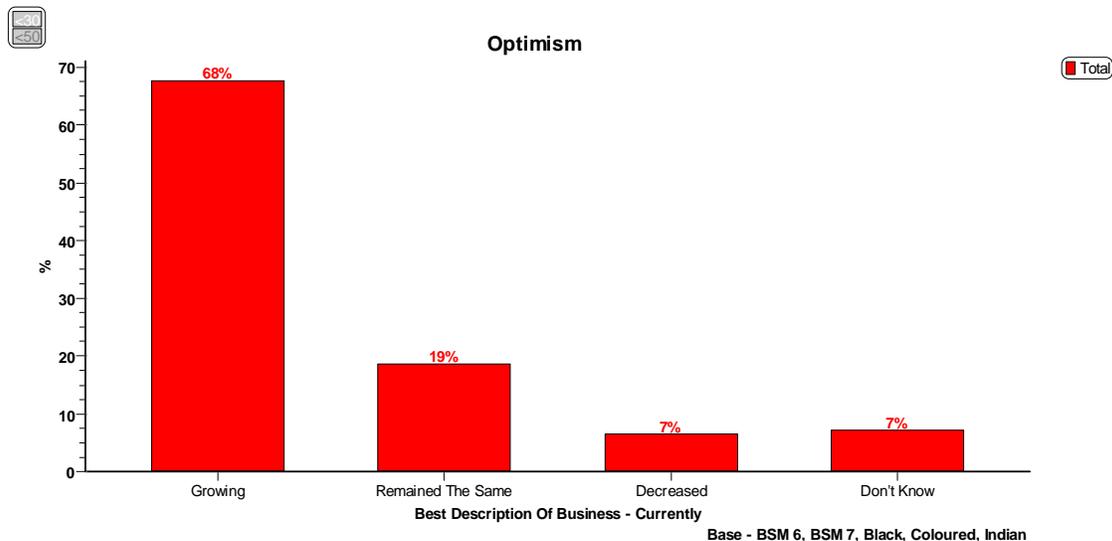
The chief challenge going forward is to devise plans that will assist the growth businesses to capitalize their businesses. There needs to be innovative thinking around:

- the creation of partnerships with investors;
- capital provision linked to mentorship in company;
- government subsidies;
- tax relief on money ploughed back to capital projects;
- low cost/low hassle loans

This is not an easy solution when the levels of financial literacy, education in general and levels of business sophistication and governance remain low.

The institutions that have been established by Government departments are not functioning properly because they are not focussed enough or single minded in their approaches. GEP for example states that their mandate is to 'help everybody in business'. These are noble ideas but totally impractical to implement. Each support institution needs to define what it does best, who its chief targets should be and go for these, ignoring the rest and leaving them to other, better focussed institutions.

Despite the obstacles out there it is remarkable to observe the optimism of small business owners in Gauteng. Nearly 70% said that their businesses were growing.



**Figure 10: Levels of optimism**

The lack of sophistication of the target market in general points to the need for business education and financial literacy to be placed high on the development agenda.

The relatively small numbers of businesses that are of significance and their wide distribution across the province linked with their general lack of visibility in the market place means that they will be difficult to find and work with. What will be important going forward is a strategy that brings the businesses to the institution set up to provide assistance rather than that institution going out after the market.

It is important for AfricaScope to interface with USAID in order understand the organizational framework which is to be followed going forward in order to optimise the effectiveness and impact against the target audience.

### 3.4. Recommendations

The following are key recommendations from analysis of the FinScope survey results:

- There is a need to re-design collateral scoring techniques. Consideration should be given to "non-western" forms of collateral
- There is a need to relaxation of re-payment holidays, interest rate capping, and extended re-payment periods
- There is a need to develop the third tier banking system, i.e. the creation of Micro Banking Divisions for granting smaller loans with shorter repayment periods
- Linked to this will be the need to encourage formal banks to finance third tier banking
- Consideration should be given to develop market access programs for SMEs
- Donor/Support Agencies should be encouraged to segment their support against specifically targeted SME segments by using the BSM.

## CHAPTER 4: GIS ANALYSIS

### 4.1 Introduction

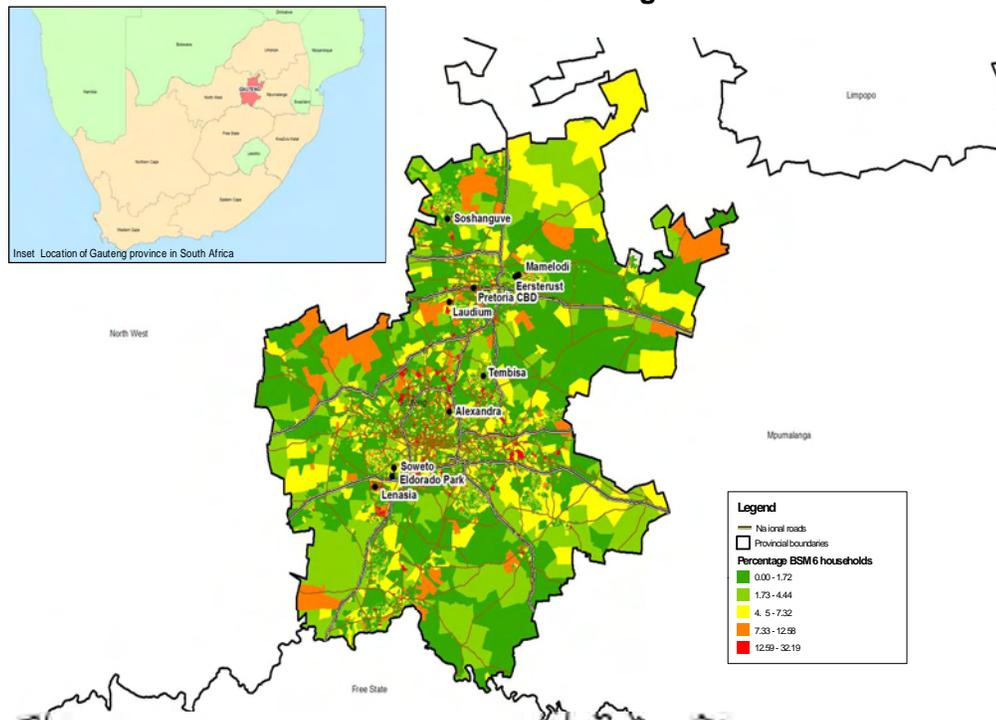
The purpose of the GIS analysis and mapping was to identify areas where historically disadvantaged small business owners within the BSM 6 and 7 categories could be located. A further purpose of the GIS analysis was to enable the field teams to enter into these identified areas so that they could select a sufficient number of small business owners to form part of the focus groups. The use of GIS was felt to be necessary because it would facilitate the identification of a small number of historically disadvantaged business owners within the total population of Gauteng. In other words it would facilitate the finding of the proverbial 'needle in a haystack'.

### 4.2 Creating the BSM maps

The BSM data was created from the 2006 FinScope SME survey. Small area estimation techniques were used to model the survey data to all enumeration areas in Gauteng. Thus, at an enumeration area level one has access to data for the BSMs 1 to 7. For purposes of this study, maps were produced for BSM 6 and 7, which are the categories where small and medium enterprises or SMEs can be found. Examples of these maps are presented in Figure 1 and 2.

What the maps show is an estimate of the percentage households falling into BSM 6 and BSM 7 categories in each enumeration area. Knowledge of the areas where historically disadvantaged business owners could be located was used in combination with the BSM maps to identify areas where participants for the focus groups could be found. What the BSM 6 map shows is that the highest concentrations of this category are largely found within the black and coloured township areas. Most of the focus group areas were selected using the BSM 6 map which has the highest concentration of historically disadvantaged small businesses in it.

**Figure 1: Distribution of BSM 6 households in Gauteng**



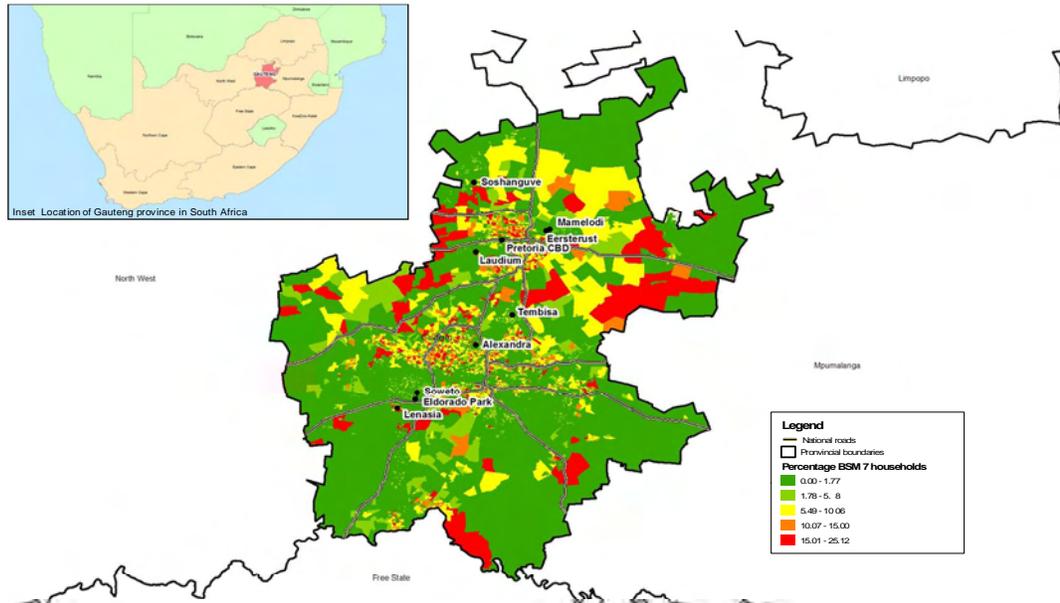
Using a combination of the BSM 6 and BSM 7 maps the focus group areas illustrated on the maps and presented in the Table 1 below were selected in the Pretoria and Johannesburg areas. In selecting these focus group areas, cognisance was taken of the differences found in communities in the metropolitan areas of Pretoria and Johannesburg in terms of cultural, ethnic and urbanization characteristics. The dominant population group/ race of areas were also taken into consideration.

**Table 1: List of focus group areas in Pretoria and Johannesburg**

PRETORIA	JOHANNESBURG
É Pretoria CBD ó African females	É Eldoradopark ó Coloured mixed
É Eersterust ó Coloured males	É Florida ó Coloured mixed
É Mamelodi ó African males	É Lenasia ó Asian males
É Soshanguve ó African females	É Soweto ó African females
É Laudium ó Asian males	É Alexandra ó African males
	É Tembisa ó African males

In Figure 2 below one can see that there are higher concentrations of BSM 7 households in the Asian areas of Laudium and Lenasia. Thus, suggesting that small businesses in these areas seem to be slightly more advanced than in black and coloured areas. Once the high concentrations of BSM 6 and 7 areas within historically disadvantaged communities had been identified the enumeration area boundaries were extracted and overlaid in Google Earth.

**Figure 2: Distribution of BSM 8 households in Gauteng**



### 4.3 Creating the focus group areas maps in Google Earth

Once the enumeration area boundaries had been imported into Google Earth a series of maps for each of the focus group areas was produced. An examination of the focus group area maps shows that the selected enumeration areas are generally located in the more commercial and industrial centres. It is in these areas where one would anticipate finding small business owners. The areas are often characterised by having large institutions located in them, including soccer stadiums.

**Figure 3: Mamelodi focus group area map**



Within black communities the focus group areas tended to be smaller in extent than those in the Asian and Coloured areas. However, in some of the larger black communities like Alexandra, Soweto and Tembisa, several separate areas or epicentres where SMEs could be found were identified. It is known that the black communities across Gauteng differ from one another in terms of their historical development, extent of urbanization, culture and ethnical background. These communities also differ in relation to the employment market that they service and as a consequence, the SMEs that are located within them may differ from one area to another.

The extent of the focus group areas in Asian and Coloured communities is generally larger than those in the black communities. Thus, suggesting that SMEs in BSM 6 and 7 categories are more commonly found in these communities. The comparison of the focus group areas in the Asian and Coloured communities shows that the SME community tends to be more widespread in the Asian community. Within this community the businesses tend to form part of the BSM 7 category more than that of the BSM 6 category.

**Figure 4: Alexandra focus group area map**



**Figure 5: Laudium focus group area map**



For a more detailed review of all the focus group theory maps referred to Annexure 1.

#### **4.4 Conclusions**

From the feedback received from the field teams that had the responsibility of identifying and recruiting SMEs they found that the focus group area maps provided them with an important starting point. On entering an area the field teams were able to systematically move through the area and identify the premises of small businesses on the side of the road or within residential properties. Where necessary, the field teams would systematically approach residences to identify small business owners within them or use snowball approaches to identify other small business owners.

This innovative approach of using the BSM and focus area maps has enabled a potentially difficult task of identifying historically disadvantaged business owners within BSM 6 and 7 categories to be accomplished. Consequently, the needle in a haystack could be found even though it was very mobile. What we mean by this is that the small businesses could be found within the focus group areas but because they are so busy it was not always possible to get them to participate in the focus groups as effectively as was originally intended.

## CHAPTER 5: DEMOGRAPHICS

### 5.1. Introduction

This chapter provides a brief description of the characteristics of the focus group participants. As such it provides an understanding of the profile of participants that is necessary for a better understanding of the results that are presented in later chapters.

### 5.2. Participants by population group and gender

The results in Table 1 show that 106 individuals participated in the 11 focus groups. Of these 73 were male. As regards population group, 57 participants were African, 20 coloured and 19 Asian/Indian participants.

**Table 1: Participants by population group and gender**

Population group	Male	Female	Total
African	28	29	57
Coloured	25	4	29
Indian/Asian	19	0	19
White	1	0	1
Participants (TOTAL)	73	33	106

The one white male participant was allowed to participate since his business subcontracts some of his work to BEE enterprises. He could as a result provide important insights to the research team.

### 5.3. Years in business

The information in Table 2 shows that most of the participants have businesses that existed for more than two years. Close to half of the businesses existed for more than 5 years, indicated that they have survived the critical first three years in a business life span.

**Table 2: Years in business**

Years in Business	Years
Less than 12 years	11
12-24 months	12
2-5 years	39
Greater than 5 years	43 (44)
TOTAL	105 (106)

### 5.4. Company turnover

The results on turnover (Table 3) show that about three in four of the participants own a business with a turnover of between R200 000 and R500 000. Recall that the bottom threshold of the Banking Association's definition was lower to this amount since it was expected that this group would benefit most from the FSP interventions to enable them to progress into the Banking Association's definition of an SME.

Twelve participants owned businesses with a turnover of more than R1 million and 9 a turnover of between R100 000 and R200 000. This latter group was allowed to participate given the fact they attended on their own volition and the team was concerned that others may leave if they were asked to leave.

**Table 3: Company turnover**

Turnover per annum	Total
R100K-R199k	9
R200k-R499k	76
R500k-R999k	8
> R1m	12 (1)
<b>TOTAL</b>	<b>105 (106)</b>

Analysis of turnover by population group and gender close to 9 out of 10 African females' businesses had a turnover of R200 000-R500 000. The comparable number for African males was just below 8 out of 10. It is also evident from the results in Table 4 that male participants were more likely to own businesses with a turnover of more than R1 million.

**Table 4: Company turnover by population group**

Turnover	African		Coloured		Indian	
	Male	Female	Male	Female	Male	Female
R100K-R199K	1	2	6	0	0	0
R200k-R499k	22	25	11	3	15	0
R500k-R999k	1	1	3	0	3	0
>R1m	4	1	5	1	1	
<b>TOTAL</b>	<b>28</b>	<b>29</b>	<b>25</b>	<b>4</b>	<b>19</b>	<b>0</b>

It should also be noted that there were no Asian/Indian female participants in the focus groups.

### 5.5. Business sector

Table 5 provides an overview of the sector in which participants' business were operating. The majority were in retail followed by community, social and personal services. The new tear includes businesses in manufacturing, transport and catering and accommodation. The results in Table 5 show that there was indeed a good spread across the various sectors of the economy.

**Table 5: Business sector**

<b>Sector</b>	<b>Number</b>
1.Mining	0
2.Manufacturing	10
3.Electricity, gas & water	1
4.Construction	8
5.Retail Trade	29
6.Tourism	0
7.Wholesale Trade	6
8.Catering & Accommodation	9
9.Transport	10
10.Finance, insurance & business services	8
11.Community, social & personal services	19
12.Professional accounting, medical, engineering	5 (1)
<b>TOTAL</b>	<b>105 (106)</b>

## **5.6. Conclusion**

The overview in this chapter shows that the research team was able to secure the participation of a good spread of HDI business owners in Gauteng. The result should therefore provide the FSP team with important pointers to the types of initiatives that are required to strengthen and support SMEs.

## CHAPTER 6: FINANCIAL BUSINESS DEVELOPMENT SERVICES

### 6.1 Introduction

Business development services have generally referred to non financial services which support business development. For the purpose of this study, reference is made to financial business development services (fBDS) to focus on those services intended to improve or support the financial performance and management of small businesses. One of the factors contributing to limited access to finance is weak supply and demand for finance related (and other) business services. One of the key issues on the demand side is whether small businesses are aware of what fBDS are available to them, and what the reasons are for their use and non-use of the services that exist.

The purpose of this chapter is, therefore, to understand what financial support/advice services respondents are *aware* of and have *used*, be they provided by government, NGOs, private sector and/or financial institutions. Given the relationship between information and uptake of services, it will also explore what information SMEs have access to and need on fBDS. This chapter also explores whether these services have addressed the needs of small businesses, especially when it comes to providing relevant, affordable and accessible fBDS. It further explores what type of assistance/support small businesses most need access to, to improve their performance/productivity and their financial management.

It is generally accepted that in order to access finance, applicants need to produce business plans, as well as evidence of sound financial management. The research investigated to what extent businesses had developed business and/or marketing plans. Small business owners were also asked whether they keep business records, and whether in developing the above plans or keeping records, they needed or had used - assistance. Finally, the small businesses attending the focus groups were asked if information and communication from government and financial institutions was adequate in defining what support/advice services are available and what the requirements were to access them.

### 6.2 Information and awareness of fBDS

The fBDS provider that SMEs were most aware of was Khula Enterprise Finance. Khula was mainly mentioned by SMEs that were trying to access loans from them. A few of the focus group participants indicated that they had approached Khula for fBDS. The Small Enterprise Development Agency (SEDA) of the Department of Trade and Industry (DTI) was mentioned quite frequently as a potential fBDS provider.

The other service provider mentioned quite frequently was the Sector Education and Training Authority (SETA). The SETAs have been set up by government to provide sector specific advice, training and skills development. It is in this role that focus group participants have engaged with them and requested assistance in terms of the development of business plans as well as in developing marketing and advertising plans. Other less commonly mentioned support/advice service providers were Umsobomvu Youth Fund, National African Federated Chamber of Commerce (NAFCOC), Gauteng

Enterprise Propeller (GEP), Development Bank of Southern Africa (DBSA), the financial institutions and the National Empowerment Fund (NEF).

Many of the focus group participants indicated that they knew of them through their advertising campaigns, their offices being nearby, through forums and through their consultants approaching the SMEs. However, in most instances the SMEs indicated that they were not using their services. Some of the participants indicated that they had approached these institutions for support but for various reasons were not helped. What is interesting to note is that in most instances small businesses immediately thought of these institutions from a financial loan perspective rather than from the business development services side that many of them offer. Consequently, it makes one wonder how effective these institutions are in making their business development services known to small businesses

A review of the resources, including the Internet, will show that there is no shortage of information on the fBDS, however, begs the question why this information or these services are not being used as effectively as they could be by SMEs

### **6.3. Use of fBDS**

From the focus groups it could be concluded that there was limited knowledge and infrequent use of fBDS providers and their services both in the past and in the present. There were business people that had been given support and were happy with it, while there were many others that had major problems

This raises questions about the decision of the financial institution to provide financial assistance in the first place, whether the small business was made aware of the conditions of the loan and what sort of debt support could be given to businesses in this position. Another small business woman from Pretoria approached a SETA for assistance with training on marketing and advertising. She was asked to write a test, which she did and when requesting the results was informed that the person had gone on maternity leave and she would need to wait six months until she got back. Underlying many of the responses to questions on whether especially public sector service providers were addressing their needs was this type of answer.

Clearly, service providers need to be consistent in providing timely feedback to SMEs. SMEs felt that the fBDS were giving them the run-around and that they really did not care. Clearly, there is a need for better training of service provider staff so that they are more responsive to the needs of small businesses, which was reiterated by several focus group participants. A key fact that needs to be remembered when providing fBDS to SMEs is that many of them have low levels of literacy and as a consequence, information and mechanisms of providing them with fBDS must be kept as simple as possible. To address this particular issue one recommendation would be to consistently provide support/advice in the language of the SME owner.

When it comes to the use of fBDS, such as bookkeeping and accounting services, the larger SMEs (i.e. with turnovers greater than R500k) have these services in place and they are using them. In comparison, the smaller SMEs (i.e. with turnovers less than

R500k) do not have these systems in place. This is because of their low levels of literacy and their businesses mainly being cash based. Other reasons mentioned by focus group participants as to why they are not keeping records is because they are too busy or have not been trained to do so.

The affordability of bookkeeping services was clearly an issue amongst the smaller SMEs. In many instances, SMEs use family members to keep records or they do it themselves rather than using external professional services. Most of the SMEs that have bookkeeping systems in place use manual methods and have not progressed to using computerised systems.

The value of business plans was clearly understood but many business owners indicated that they did not develop business plans because they were 'too busy'. Business owners indicated that they used their business associates, financial and legal advisors and families to develop their business plans. In some instances, people mentioned that they needed to approach professionals to help them with their business plans so that they could get the financing they needed. One male participant from Mamelodi commented that this was not very useful because he could not operationalize the business plan.

#### **6.4. Reasons for non-use of fBDS**

One of the main reasons why SMEs are not using fBDS is because of the poor communication between the two parties. A common communication problem raised by participants is their inability to get hold of service providers and the right person to deal with their issue. It is for this reason that many focus group participants indicated that the only way to get help is by knowing somebody within the institution. To get hold of a government department is often very difficult. As one woman from Pretoria put it, you can try and contact them and the 'phone will ring until hallelujah.

After making contact, the time that it takes for the issues to be addressed can be lengthy or may not be addressed at all. A Laudium businessman suggested that both government and private service providers should 'advertise' where to go to and who to speak to in order for specific problems to be addressed. If one did not know somebody at that institution you could be sent from pillar to post and still not get any help. They also complained that it took the institution a long time to give them feedback.

One participant felt that it was a waste of time trying to communicate with government departments. A second businessman from Laudium felt that government service providers needed to be trained to deal with customers as they were often unfriendly. They did indicate that some of the service providers did get hold of them on occasion but in most instances did not give them feedback. Bureaucratic processes and a lack of capacity within especially the government service providers is resulting in many small business owners deciding to do it on their own and not to use the services or support of these institutions. This has also resulted in some businesses having to close down because they could not get support in time.

Several Eersterust focus group participants raised the issue of them having to develop business plans before being assisted. This placed them in a 'catch 22' situation as they

were approaching these support services to assist them develop their business plans in the first place. The opinion of many focus group participants was that the documents (and deposits when seeking financial loans) required before being provided with assistance were restrictive. Many of them felt that there was an unrealistic expectation, especially as they were being asked to develop these 'big' and 'beautiful' documents that were very costly to produce.

Another issue raised by the SMEs was that the fBDS should be located closer to where their business premises are located. This is because SMEs are so busy running their business that they do not have time to travel long distances into city centres to access these services. Another suggestion was that an integrated approach be followed by service providers operating in the different areas.

An Eersterust businessman working in the hospitality industry felt that many of the support services were unsuccessful and not up to standard. This was because too few people were being assisted and those that were assisted needed to be helped systematically and over a period of time. He questioned whether some of the government service providers were fulfilling their mandate and whether they were keeping pace with the needs of small businesses. He feels that much more assistance needs to be given and that simple information products need to be provided on the availability of support services that can be used to run the small businesses.

#### **6.5. Financial BDS needed by SMEs**

It is important to emphasize that the main support needed by SMEs is to enable them to get financial support from fBDS providers. Many of the participants indicated that they needed advice and training on how to start and run their businesses. More specifically, what are the step-by-step procedures that should be followed? For example: how do I determine if the business is viable, how do I secure financing for the business, what legal vehicle should I use, where should the business be located and how do I secure and maintain customers? Financial support was mentioned as one of the most important needs that they had. They recognized that the type of advice needed to be sector specific. Thus, they recommended that sector specific mentors be identified that could be used by institutions to provide them with advice.

Bookkeeping services were clearly identified as a need. They are needed to keep control of the finances and records of the business. This would give businesses an understanding of their income, expenditure and profit. Bookkeepers were seen as critical in dealing with SARS and other government institutions (e.g. VAT, PAYE, SDL, UIF). They would assist the businesses in issuing invoices and following up on payments.

A concern was raised by the small businesses that they cannot afford these services. An area where small businesses also need assistance is in preparing their tax invoices. Many of them do not put all the information that is needed on the tax invoice. This is required when doing tax returns for SARS.

Other participants indicated that they needed help with their business plans and company profiles. The business plans are needed to register with potential clients and with

financial institutions. A businessman from Laudium felt that government needed to approach financial institutions so that they could put together a plan as to how they can better provide support services to small businesses. One reason for this is that small businesses generally have few staff and they do not have the luxury of being able to go to service providers and spend a lot of time there.

An Eersterust businessman said that he needs professional services that can develop the business plans for him. Another businessman emphasized that there is also a need for assistance in how a small business is set up and structured. Although business plans are not common the need for them seems to be increasing as they become a requirement to access finances, support services and in tendering for work. Several other business owners said that having put together the business plans and presented them to the institutions it took an inordinate amount of time for them to get a response.

Most of the people participating in the focus groups indicated that they developed their business plans to get access to finances and work. One businessman from Mamelodi said that his business plan was there to grow the business and to enable someone else to steer the business if he was not at the helm. Marketing plans were less common than the business plans. Most participants did recognize the importance of marketing strategies in reaching their potential customers but emphasized that they needed to be workable for small businesses.

They were quick to add that their turnover limited the type of marketing that they could do. For example, advertising in newspapers, on the radio and on billboards were out of the reach of most small businesses. Consequently, small businesses use signage, adverts on their premise walls, pamphlets and one-on-one marketing as they feel it is better to show your services/products in maintaining your customers. Location of businesses was seen as critical in positioning the business.

There was a unanimous response from focus groups that there is the need for more training in the development of business and marketing plans, financial management and the day-to-day management of the business. Focus group participants systematically emphasized that once they had had their training, there needed to be follow-up and sector specific mentoring needs to be provided.

## **6.6. Conclusion and recommendations**

The overall conclusion is that there is awareness amongst small businesses of fBDS providers. However, very few SMEs are using their services because they feel that their needs are not being met. It is recommended that more in-depth research be done on the support services provided by private and public fBDS in terms of what they offer, the effectiveness of their services and how they communicate these services to potential customers.

Simple information products, possibly in the form of a booklet or pamphlet, should be provided on the services offered by the various institutions. They should also be used to show how to set up and manage small businesses. A key area to focus on is communication. This includes how service providers should communicate with small businesses in terms of addressing their specific needs and in giving them feedback. It is important to remember that many of the business owners have lower levels of literacy and consequently, communication should be through simple messages and in their own language.

Training workshops to address the needs of small businesses is also a recommended approach and is already used quite widely. Cognisance must be taken of the concerns of small businesses in terms of the time that they have available and the limited financial resources they have to pay for them. One area that should be investigated further is the development and implementation of effective sector specific mentoring programmes for small business owners.

There are many fBDS providers in both the public and private sectors in South Africa. There is also much information available on services that they can provide. A strategy needs to be developed to improve awareness of the support provided by fBDS and to ensure that SMEs use them more effectively. To accomplish this there is also a need for more communication and advertising. One of the recommendations coming out of the focus groups is for an integrated and co-ordinated approach to the provision of fBDS in the different sectors. Another recommendation is that the fBDS providers be located closer to where the historically disadvantaged SME business premises are situated. There is also a clear need for fBDS staff to be better trained in being more responsive to the needs of small business owners.

## CHAPTER 7: BANKING AND FINANCIAL SERVICES

### 7.1 Introduction

The purpose of this chapter is to explore the extent and conditions under which small businesses presently use finances from formal and informal institutions. The focus groups would be used to examine the suitability of financing to SMEs from various perspectives including the amount provided and the repayment schedule. The chapter also includes information on the needs of SMEs for financing and the sources available to them.

The chapter explores past experiences of SMES in putting in applications for loans, the suitability of the loans to the business needs and the refusal of loans. What it also investigates is whether banks informed the businesses of the reasons for the refusal. Finally the chapter looks at the reasons why business owners have never applied for a loan.

### 7.2 Access to Finance

According to focus group participants, access to finance for small businesses is absolutely vital to their growth. The SMEs emphasized that financing was needed to improve workplace conditions, to enable them to buy stock and equipment and to allow them to obtain bigger and better premises. Financing was also seen as a mechanism by which they could improve their cash flow. This is most forcefully illustrated by a comment from a respondent in Laudium, Pretoria:

*“Yes, we are always short of cash flow. The more money you have the more stock you can buy. In a business you can never have enough money”*

The majority of respondents in the focus groups reported having some form of bank account, be it a personal bank account, a business bank account and in some instances both. As was found in the FinScope quantitative study, the majority of respondents hold either a savings account or and and/or ATM card. Cheque accounts are a lot less common. It would appear, therefore, that financial institutions are prepared to issue the ösaferö products from a bank perspective but make things difficult for businesses where current accounts and loan finance are concerned.

There are also marked differences in the level of access to finance by female respondents as well as black respondents compared to their Asian and Coloured counterparts, the latter enjoying greater access in general. However, all historically disadvantaged SMEs face obstacles in getting access to finance.

### 7.3 Obstacles to accessing Finance

There are many obstacles in the way of small businesses reaching the goal of having sufficient finance. The reasons for respondents not being able to obtain loans from outside sources are numerous. One reason given is that they have no account with the institutions where they are applying for a loan. In some instances focus group participants indicated that they needed to have a bank account with an institution for at least six months before they can get a loan.

Other reasons given for SMEs not being able to get a loan included having no or a poor credit history, lack of security/collateral, not having enough cash flow, not having enough equity in the business, not being in business long enough and inadequate financial records. Some of the focus group participants indicated that their businesses needed at least three years worth of financial statements before they could be considered for a loan. If the SMEs took a personal loan then they would need bank deposit account statements for a shorter period of between 3 to 6 months (the period of six months was mentioned often and therefore appears to be a "magical number" on the part of banks – why six months?).

Poor financial literacy remains a major stumbling block in small business owners getting access to finance. This is because they do not have the most basic understanding of how to approach financial institutions and get the necessary support needed to complete an application for financing. Several SMEs indicated that their loan applications were turned down because they were blacklisted by credit bureaus. This reason was mentioned by a number of respondents across the spectrum. This situation forced them to use informal money lenders who charged very high interest rates. In addition to this, these money lenders do not report "good payers" to the credit bureau and, therefore, even if the respondent was using informal methods and paying back on time, there is no formal credit record being built.

Others indicated that because of their "identity" and their being intimidated by the financial institutions they were not able to get loans. One Tembisa businessman explained it like this:

*"They [financial institutions] have a fear when you dress like that [in a suit and tie with a briefcase]"*

Banks in most cases will only provide savings accounts to start-up businesses. No financial statements are required for a savings account, which means they cannot get a loan and, therefore, it becomes a vicious cycle. Business owners also indicated that the high interest rates charged by financial institutions for loans were a major obstacle. Many of the institutions approached were only interested in funding large projects and projects in specific sectors. This attitude or mindset on the part of the financial industry that the smaller loans are not worth the trouble when considering risk and return is problematic.

*"With Umsobomvu you have to understand that they are interested in big projects, like manufacturing. They will send you to Gauteng Shared Services, the DTI, or Gauteng Growth something. They'll tell you that those people will be able to help you with those small funds, but they are not interested in those projects."*

Most indicated that they received no concrete response from the bank when the loan was refused. However, a few respondents admitted that they had received a declination letter, although the reasons for the declination were not clear to them.

#### **7.4 Sources of finances used by SMEs**

Many of the participants indicated that they did not have financing from external organizations because it was too hard to get. They would rather save up to finance their purchases for the business or they would secure finance from family and friends, retrenchment packages, pensions and other savings. These responses point to the fragile nature of small businesses and in many cases resulted in start-up businesses being undercapitalized from the beginning. All these factors lead to frustration with the system.

*“ ... I have tried, but it hard getting it (finance). You try the business way, they tell you stories and you just decide “why not do it my way, the way I know?” Then put money in a money box until you get enough money to get whatever you want.”*

To start up their businesses some took out a bond on their homes. Others used their property as surety to get a loan. The loans were taken in a personal capacity or using their personal accounts rather than their business account because those accounts had longer track records. Where individuals had no fixed assets to rely on, they resorted to friends and family, savings, pensions and retrenchment packages. Those who could provide collateral were in a clear minority.

The complexities of loan applications are not confined to banks. The government support institutions have many of the same complexities in the loan application processes as banks and are not easier places to go to for loans. There is a lot of frustration in the marketplace about the surety requirements, the length of time application processing takes, their time being wasted and the loan amounts not covering their financial needs.

*“ ... I am aware of all of those, I am in business for a long time now, I went to KHULA and they told me that they will provide a loan, but they want security. It is a long process. When you go to them they will assist you and then they send you there and then they decide if your business is worth it, it is a waste of time. Maybe it is where we come from and we are used to struggling to make ends meet and then maybe in the end we will grow.”*

*“What happens here is that they all have different names, they but they all want the same. If you have a bad experience with one of them, you look at them as just another one.”*

*“Umsobomvu, yes, but it's not more of a financial assistance if you are in services. They are also not interested in something less than R60 000. If you come up with a need for a small amount like R45 000 they say go to a financial institution. You must remember they are a bank themselves and need to make a profit. Even Khula is also not funding on a small scale”.*

For those who do not have loans from banks, the route to external finance is through a number of different means. These could be through the industry bodies.

*“I do not have loans from the financial institutions the only loans I have, are the ones that we run ourselves in the industry where we help members with loans which are limited.”*

There is a clear recognition of the need to have collateral if loans are to be obtained.

*“Maybe a house, if you want to borrow money from a bank. If you have a house, you can give it as security.”*

Part of the problem with the historically disadvantaged community is that they often do not hold proper title deeds to their real estate. A project to ensure freehold title for township houses and to put people in a position to have an asset base would make major strides forward in developing access to finance and small business development.

*“If I may come on that one, on the issue of the banks, it’s difficult to get support because in most cases they look for an assurance. And mostly as Blacks we are not used to this thing of using Auditors“.*

Therefore, a clear direction forward for the industry and the development of easy to use information guidelines to assist people in gathering the correct information prior to making the first application is needed. This should be a community led initiative.

There is an awareness of but confusion over the interpretation of the national credit act as well. As one respondent put it:

*“... if they loan you money now and in the future and for any reason you cannot pay it, and then if you say to them fifty rand per month, they have to accept it . So they do credit checks, so you have to be careful ...”*

On the one hand that participant was saying that the national credit act is there to protect the borrower if too many loans are granted but at the same time cautions that the banks will conduct checks prior to a loan and the extent of borrowing will be uncovered making loans more difficult. This too could force borrowers to the informal market.

## **7.5 Support from financial institutions**

Some respondents reported that they filled in applications and worked through consultants from the institutions but could still not get access to finances. They had to provide three months worth of bank statements and were informed to come back later; in some cases they were told to return after six months. One questions the role and nature of the consultants and the extent to which these are either middle men for the banks or individuals exploiting the situation of desperate business people.

Some participants wished that institutions would visit their business premises so that they could see and have the potential explained before making a decision on giving them a

loan. The lack of a site visit indicates that the banks tend to rely on the paper trail rather than on the quality of the person, the viability of the business in the trading environment and other soft supporting arguments to support a loan application.

## 7.6 Opinions on financial institutions

Many of the SMEs had strong opinions on financial institutions and their ability to service their needs. A select few are presented below. Some respondents feel that there are cultural/racial issues in banking relationships. As one Black female respondent in Soweto recalled:

*“There was a white relationship manager at the bank ... I needed a cheque that had been deposited into my bank account cleared urgently ... there was a big problem ... if I had a Black relationship manager there would not have been a problem.”*

*“Mostly they don’t look at your track record, but more your collateral, and the cash flow in your account; how active is your account. On how long you’ve been in business, they want six months bank statements.”*

*“It’s a problem for me, I don’t do banking everyday or every week; I do it once a month. Most times I keep it at home.”*

Banking is for the good times only! One Black female respondent in Soweto encapsulated the feeling of frustration by saying:

*“.....for a long time my account was okay and then I ran out of money, so I went to the bank to ask them for money and they said no”.*

Word of mouth plays an important role in creating negative perceptions towards taking credit. Many females in the township environment have seen firsthand how others have had their property repossessed after failure to repay the bank for a loan and they are scared off.

Even though access to finance from banks is difficult, the bank is perceived to be a good place to go for finance, as one female respondent in Pretoria put it:

*“We normally approach the bank because it is the trustworthy party.”*

The thinking of some participants was that if you have got money in the bank then you don’t need a loan. Financial institutions don’t consider small businesses important and as one participant put it:

*“I suppose I am a small thing”.*

There is also a perception that banks do not take into account or are not willing to advance the full amount of the loan required. This is most likely to do with credit limits and or security but the facts are not communicated to individuals.

*“Yes I had an account, I still remember I borrowed only five thousand Rand; they didn’t give me more and couldn’t cover everything.”*

It is evident from these comments that communication between the banks and historically disadvantaged SMEs is very poor.

## **7.7 Conclusion and Recommendations**

While respondents reported that in general they were able to open and operate bank accounts, they generally found that obtaining access to finance from outside sources for their business is extremely difficult. The challenges were not confined to formal financial institutions alone but included the support institutions as well. This has resulted in much of the external funding for business being secured from informal sources (i.e. family and friends) and to a larger degree from personal savings, pensions etc.

Black males and to a larger extent female respondents were more challenged than their Asian and Coloured counterparts when it comes to financial access and in the majority of cases these sentiments were more forcefully expressed in the Black groups.

The focus group findings support to a large degree what was learnt from the FinScope Small Business study in that there are deficiencies on both the demand and supply side.

To some extent, rejections of loan applications are being blamed on racial prejudices due to a large extent the inability of the banks to communicate effectively with loan applications. This was very well illustrated by a respondent from Eersterust:

*“I don’t think it is based on colour, it is based on risk but they don’t go to the level where they explain to you what makes you a high risk.”*

This situation compounds the communication problems between the banks and their clients as well as the friends of those who have been rejected. Proper training within banks will help to alleviate the problem and could lead to lower tensions between the clients and the banks.

The deficiencies from the demand side lie in the following:

- Lack of financial education and literacy;
- Lack of business training;
- Highly competitive and undiversified markets;
- Lack of record keeping;
- Inability to present formal business plans;
- Poor credit ratings;
- Lack of collateral/security for loans;
- Limited capital bases and ability to grow capital;
- Misconceptions about the risk analysis process.

The deficiencies from the supply side lie in the following:

- Rigid credit scoring policies;
- Rigid collateral requirements;
- Reluctance to provide small loans;
- Rigid repayment schedules;
- Support organisations acting like banks;
- Lack of understanding of cultural differences;
- Poor report-back to applicants on loan refusals;
- Poor communication of services offered;
- Lack of differentiation of product and approach offered to clients
- Restrictions placed on lending via the National Credit Act.

To improve the provision of finances to historically disadvantaged SMEs and to address the deficiencies listed above, a number of key recommendations were made. One of the main recommendations is to develop step-by-step guidelines on what is needed to secure finances from institutions. It is also felt that guidelines on how financial institutions and government organizations communicate with historically disadvantaged SMEs should be established. One component of this would be to train staff within financial institutions to understand the characteristics and needs of small businesses better.

Clearly there is a need for formal banking institutions to change their mindset as to how they engage and communicate with small businesses. One mindset change that financial institutions should consider is making the "business plan" requirement process much simpler. There should also be a redesigning of collateral scoring techniques with "non-western" collateral being considered. Another recommendation is that more flexible repayment schedules be considered for SMEs.

To facilitate better engagement between SMEs and financial institutions extensive financial literacy training programs should be also developed and presented within the communities where the small businesses are located.

## **CHAPTER 8: LEGAL AND REGULATORY MATTERS**

### **8.1. Introduction**

In this chapter the focus will be on legal requirements and compliance, relationships with public institutions, knowledge of the BEE legislation and membership of associations and advocacy. Under legal requirements and compliance issues relating to SMEs knowledge of benefits and liabilities associated with different types of companies will be discussed. This section will also look at the registration of SMEs and what advice was received in deciding on the legal vehicle. It will also look at the compliance of the SMEs to various regulatory requirements including tax, VAT, PAYE and SDL.

A further focus will be on SMEs knowledge of regulatory requirements and their need for legal/regulatory training. In the next section the value of and assistance public institutions can provide to SMEs at the different tiers of government (i.e. national, provincial and municipal) will be examined. This chapter will also look at whether SMEs are registered as BEE enterprises and how aware they are of the business opportunities and benefits associated with this legislation. In this section the needs of SMEs for information and training on BEE will also be reviewed.

Finally, the participation of the SMEs in advocacy, business or professional associations will be looked at and the need for support in this area determined.

### **8.2. Legal requirements and compliance**

The focus groups showed that many small businesses in the different areas were registered as Closed Corporations (CC) or as sole proprietors. What one sees is that it is the SMEs with larger turnovers that generally register as CCs. They formed a CC because owners saw the benefit from a business perspective and they were required to do so to access finance and government work. To do business or to tender for government work businesses need to be registered so that they can get a VAT number and tax clearance certificate.

On the other hand many of the SMEs were not aware of the benefits associated with registering their business. Only one SME knew that by registering their business as a CC they reduced the risks and liabilities of the business. In making a decision about the registering of the business SMEs took advice from business associates, family members and their accountants.

There were also many SMEs that were not registered at all. One of the reasons that SMEs gave for them not being registered is that they had limited time to do so. They also indicated that they did not know how to go about the registration process, even though it is felt not to be too complicated or expensive. In a few instances focus group participants indicated that they were too small an enterprise to register.

Some of the businesses indicated that they did not see the benefit of registering. However, many focus group participants indicated that they would like to be registered.

Most SMEs emphasized that they respected their obligations towards SARS, but were not aware of the new VAT threshold for 2009.

Nearly all the focus group participants emphasized that they needed more information and training, especially in relation to the legal issues associated with the different legal vehicles for businesses. It was emphasized that there is a need for a handbook that provides information on all aspects relating to the different types of legal vehicles.

Most of the focus groups indicated that as employers they knew they had to register their employees for UIF as part of the Labour Relations Act. However, it was not clear how many of the SMEs participating in the focus groups had registered for UIF. An interesting perspective given by the moderators of the focus groups was that they perceived that SMEs did not want to comply as they saw compliance as them paying out their money. The perception is that SMEs were more likely to comply by paying income tax and PAYE than UIF and SDL. SMEs indicated that if they did not comply it was because of a lack of knowledge.

Some of the participants felt that the regulatory bodies (e.g. SARS, Dept of Labour, Dept of Trade and Industry) should advertise and develop programmes on the radio and TV that would explain the registration and compliance requirements for SMEs. They also felt that government should provide a prominent call centre service that people can phone when they have queries.

### **8.3. Relationship with public institutions**

Participants felt that the public institutions that were there to help them were not accessible and not very useful. This is because they were located in the major urban centres and did not have offices in the township areas. They also felt that public institutions did not understand the needs of SMEs and that they needed to do so in order to help them. Small businesses also felt that public institutions should communicate with them better and provide them with information in their own language on how to run their businesses and on what work opportunities are available.

Some of the other focus groups indicated that they did not know where to find these public institutions. Their suggestion was that government should use the media (i.e. radio, newspapers and TV) to advertise their services and provide an understanding of how they could be contacted. Information on these services should also be put on the Internet and there should be call centres that they can contact. Some of the focus groups raised concerns about public institutions being bureaucratic, not being transparent and them practicing nepotism. Staff at these public institutions also needed to be properly trained to deal with customers and to have a better understanding of policies.

One of the major failures identified by SMEs of public institutions is that their staff did not follow up after their initial engagement. It was suggested by one participant that these public institutions should be privatized and monitored for their ability to produce good small businesses. Although SMEs did indicate that they saw a role for government in facilitating access to loans from financial institutions, they could also facilitate training and education in the setting up of the SMEs.

Focus group participants also felt that the government could provide them with access to business premises. A key role that they could also play is in providing access to relevant information in various local languages.

*“Most important thing is that they must make information more easily accessible in all the languages; some of us have difficulty in finding the right information”*

#### **8.4. Knowledge of BEE legislation**

SMEs generally do not know the BEE legislation. Many of the businesses when asked about them being registered for BEE stated that they initially thought that being black meant that they were BEE. Some discovered that their businesses needed to be registered but that they had not done so. This was because they were too busy running their businesses and saw BEE as a mechanism by which white companies could get access to government work.

*“Yes, I haven’t register for it, I thought being black you are automatically registered as BEE”*

They also felt that the BEE legislation was biased and reserved for big companies. Almost all the SMEs that participated in the focused groups were not registered as a BEE company and most of them did not know how to go about it. Most of them did not see how they could benefit from the BEE legislation. Others felt that as they did not do work for government and did not want to work for them that they did not need to be registered.

One focus group participant indicated that to be a BEE business you had to be registered and to qualify you had to meet criteria in relation to ownership, management, procurement, employment equity, enterprise development and social investment. It was emphasized that there are government agencies (e.g. EMEX) that reviewed the businesses and gave them their BEE rating and certificates. The SMEs all indicated that they needed more information and training on what the benefits of a BEE company were.

In terms of the advantages, participants indicated that they felt there were financial benefits and it made small businesses more viable. However, one participant pointed out that small BEE companies located in township areas were possibly overlooked when it came to large contracts. This is because the procuring companies screened them out as they felt that they would not have the financial means and capacity to deliver on the contracts. It was for this reason that they felt that BEE legislation only benefited the larger companies.

There was also the feeling that small BEE companies were being misused to enable other companies to get business. Participants from the Asian community felt that BEE only benefitted Africans.

*“BEE is a waste of time for us, for me, myself because first of all it hasn’t been marketed properly. We - I’m talking as a young Indian businessman – we haven’t been educated as to what resources we can get w.r.t. BEE. I think to be quite*

*frank it is only beneficial to the Black man in the country. In the old government I wasn't white enough, now I am not Black enough. That's my view."*

### **8.5. Association Membership or Professional Associations**

Participants in several of the focus groups indicated that they were part of business or professional associations. However, most indicated that these associations did not fulfil an advocacy role. Although they recognized the potential of these advocacy associations they also indicated that they did not have the time to participate in them. It was found that women, Coloured and Asian SMEs were more likely to participate in business associations.

One focus group participants indicated that the way that they communicate with government about their concerns was to strike. Another focus group participant indicated that there was break in communication between SMEs and the government because there is always a messenger in between.

*"I think communication is a problem, especially in the taxi industry. The only time we communicate with them is when we strike."*

*"On the issue of communication between the community and the government, the communication does reach us, and it goes back to them. The problem is that there is a messenger in-between, so there is a break-down, so it's not sufficient."*

### **8.6. Conclusion**

From the input received from SMEs participating in the focus groups it can be concluded that more information and training on all aspects relating to the registration of businesses, the Labour Relations Act and BEE legislation is required. More specifically training is needed on what the business opportunities are that arise out of the BEE legislation. There is also a need to locate more public institutions within the communities of historically disadvantaged SMEs. These institutions also need to be given greater support to enable them to strengthen the business and community associations.

It is recommended that the information needed by SMEs be published into a handbook. More intensive media campaigns can also be developed on the topics described above. This may well require the development of programmatic material and holding intensive discussions with appropriate media groups. Further research could be done on mechanisms of establishing effective associations and forums in disadvantaged areas that can address the specific needs of small businesses. Finally, there is also a need to conduct research into problems associated with the BEE policy and its procedures.

## **CHAPTER 9: KNOWLEDGE/INFORMATION MANAGEMENT**

### **9.1. Introduction**

The purpose of this chapter is to look at how small businesses use information, knowledge and past experience in improving their businesses. More specifically, the chapter looks at the mechanism by which businesses share knowledge and learning. An attempt was also made to see how the impact or benefits of sharing experiences and learning could be systematically done using evidence based approaches.

A particular focus was on sharing information on how the business environment is changing, especially in relation to government policies and how they affect businesses. The focus groups tried to determine what support government could provide, especially in the exchange of ideas and business best practices. The research also tried to determine what capacity or challenges small businesses had in sharing knowledge and learning.

The chapter looked at whether the business owners felt that their culture, identity and religion influenced the way the financial sector dealt with them. Finally, insight was sought on how information and communication technologies (e.g. computers, Internet, cellphones, radio, TV) could support or inhibit the sharing of knowledge or learning.

### **9.2. Sharing of knowledge and learning**

What was clear from the focus groups is that SMEs are generally not sharing their knowledge and learning with one another. This can be attributed to there being no active and effective forums in place as well as the SMEs having limited time available to participate. Consequently, the main way in which SMEs have learnt their trade is from the experience they gained while working for their previous employers. SMEs believe that knowledge sharing and learning can be transferred not only through the holding of forums and workshops mentioned above but through the regular production of bulletins and pamphlets that can be distributed to small businesses.

The focus of many of these knowledge sharing and learning initiatives would be to provide simple step-by-step procedures in a handbook on how to address many of the issues being faced by small businesses. A participant from Laudium indicated that one of the ways he shared ideas is through the use of the Internet. Asian business people indicated that the other way that they shared experiences and learning was by attending business EXPOs.

### **9.3. Mechanisms of sharing of knowledge and learning**

Within Gauteng and in every large community in the province (e.g. Soweto, Mamelodi, Tembisa, and Alexandra) there are Chambers of Commerce and associations that provide mechanisms for businesses to engage with one another. However, in terms of the small businesses that formed part of the focus groups most of them are not participating in these forums. This is mainly because as small businesses they are not aware of them and they are often too busy to attend such forums. The small businesses that had attended such forums also indicated that they were a waste of time.

Some of the owners indicated that businesses attending these forums were normally the ones that were awarded contracts. This is possibly a consequence of these forums being targeted towards larger businesses. Although the need for sharing of knowledge and experiences amongst similar businesses, especially in relation to success stories and providing advice, was clearly articulated. Several of the focus groups emphasized the need for forums or workshops where people could exchange ideas and talk about problems relating to their businesses.

Business people generally indicated their willingness to share ideas about running businesses. They also emphasized that the forums and workshops must cater specifically for the needs of small businesses. Some of the participants felt that because small business people are so busy, effort should be made to hold the forums and workshops close to where their business premises are located and at times which would allow them to attend.

#### **9.4. Government support**

In general the small businesses were critical of the role that government is playing in supporting them. However, they felt that there were areas that the government could play a role. The first was in cascading information down to them on all aspects relating to the running of small businesses. For example, most of the small businesses were not aware of the new VAT and BEE benefits for small businesses. This included providing information on who to contact and where to go, especially in relation to the regulatory matters associated with small businesses.

In essence small businesses want a handbook or pamphlets that would guide them on what they should be doing, how they can do it and what support they can get from both public and private sector institutions. The small business owners also felt that government could help organize the forums and workshops. However, a common request from participants was the need for follow-up to see how they were doing and to provide them with hands on training.

Government could also develop a database of small businesses. This database could then be used by companies seeking the products and services of small businesses. What is also important is that government could monitor the use of small businesses on the database to see if they are being used. Government could also provide financing for small businesses to get access to ICTs.

Some of the focus groups indicated that government could give them subsidies to assist them get access to ICTs. They also felt that government could help them with advertising on radio, TV and in newspapers.

#### **9.5. Needs, capacities and challenges**

There are many areas where small businesses have needs and where their capacities need to be developed. This is from developing managerial skills to having knowledge about growing their business. One area where there is a great need, is understanding the legislation pertaining to small businesses and BEE. Other areas included marketing,

financial management and bookkeeping. These needs can be met through forums and holding workshops but participants emphasized that they also need on-site support.

Small businesses also emphasized the need for basic literacy training on computers. This was to enable them to use the Internet to find out about other businesses and to use e-mail in communicating with clients and suppliers. In more recent years the use of computers and the Internet to register and submit tax returns has become a prominent use of this technology.

Small businesses face challenges when it comes to sharing experiences and learning because of the limited time they have available to attend such forums. As a consequence, participants requested that such forums are held closer to where their premises are located. Another option is to use ICTs but the challenges that they have here is that they do not necessarily have the finances to purchase computers or software for this purpose. The allocation of finances to purchase ICTs could be an option while the other option is to provide such facilities free of charge within public institutions (e.g. libraries, schools, clinics, etc).

#### **9.6. Culture, identity and religious influences in the financial sector**

From one focus group to the other there were quite different experiences. Black business women in the township area of Soshanguve felt that culture, identity and religion did not played a role in the financial sector assisting them in the development of their business.

*“We never come across it at all.”*

In contrast some black women in central Pretoria felt that white people are more likely to get loans than black people. However, what was often stated by participants in the focus groups was that through knowing someone in a financial institution it often helped in them opening a bank account and getting assistance.

*“....through knowing the people at the bank we were able to open a bank account.”*

Concerns were raised in some of the Asian focus groups that they were being discriminated against because they were not white or black enough.

*“We need advice on how to grow as a business and how to become a BEE? We don't know the procedures. How do we qualify, first we are not white enough now we are not black enough”*

#### **9.7. ICTs in sharing knowledge and learning**

Several of the focus groups acknowledged the importance of ICTs in their businesses. Many of the larger SMEs acknowledged that their businesses used computers or were beginning to do so. Computers were not being used necessarily for financial management purposes (e.g. bookkeeping) but owners did indicate the use of the Internet for banking purposes.

A small business owner from Laudium showed how advanced computer use could be with it being used for bookkeeping, income and expenditure, tracking profits, monitoring sales and doing stock taking. Some of the participants complained that the cost of software was prohibitive and that they needed a cash injection to purchase them.

E-mail is being used more and more to communicate with clients and suppliers. The web was also being used to access information on businesses and to place orders with suppliers. The web could also be used to hold teleconferences. Cellphones are also a powerful tool for use by small businesses of all sizes. They can be used to do banking and through SMSs businesses can be sent relevant information and be educated. SMSs were also being used to monitor bank transactions and to get their bank balances.

Focus group participants suggested that radio stations could present short programmes in appropriate time slots (e.g. after 8pm) on the running of businesses. This could include inviting guest speakers to present on a particular topic and afterwards people could phone in to ask questions and get further advice. The emphasis here was to get successful businesses like Midas, Nandos and Pick n Pay to present their views on how to make businesses successful in their specific sectors. It was indicated that these sorts of programmes were already being presented on certain radio stations. Similar programmes could also be presented on TV.

## 9.8. Conclusion and recommendations

Generally small businesses are not sharing their experiences and learning with one another. As a consequence there is little evidence of their being a benefit. However, they are unanimous in acknowledging the value of knowledge and information as well as ICTs to their businesses. It is for this reason that there is a call for the greater support of forums and workshops as well as training so that business owners can reap the benefit. Cognisance must be taken of the needs and challenges of small businesses in using knowledge and information management approaches (e.g. literacy, language).

One of the main recommendations would be for government to develop a small business handbook that would explain policy and regulatory matters and provide step-by-step approaches in managing their businesses and getting support. It will be important to have this handbook translated into local languages. Government could also provide small grants to these businesses to enable them to capacitate themselves when it comes to ICTs. The Universal Service Access Fund (USAF) could possibly be used as a source of these funds and in this regard the Universal Service Access Agency for South Africa (USAASA) should be approached.

More radio and television programmes could be developed using the handbook as the basis to address the many needs and challenges of small businesses. It is important to emphasize that a systematic communication campaign should be developed and implemented using the various commercial and community radio stations as an example. It is also recommended that a knowledge portal be developed that will enable the sharing of knowledge and learning amongst SMEs in South Africa. One of the things that the knowledge portal would contain is a database of all Chambers of Commerce, associations and forums that enable the sharing of knowledge and learning amongst SMEs.

The value of the knowledge portal is that it provides a single repository for information and handbooks on policies and regulations, SME practices, tax and registration, access to finance and financial business development services. It could also be a place where training events, workshops and business Expos could be advertised. The knowledge portal would also provide access to accredited on-line training courses for SMEs. It could also feature articles by prominent business people on different aspects relating to managing and running small businesses. SMEs would also be able to become a member of the knowledge portal and a web page provided where they can provide a profile of the businesses. To ensure the effective use of the knowledge portal a 'pull' and 'push' approach should be used in accessing relevant information for the knowledge portal and sending it out to registered SMEs.

## **CHAPTER 10: CONCLUSIONS AND RECOMMENDATIONS**

### **10.1. Introduction**

The unique approach followed in this study enabled the research team to uncover a number of key challenges faced by small business owners in Gauteng. Some of these can be addressed by interventions by the FSP team, others need initiatives from other role-players, still others require collaboration between various stakeholders that include government, financial institutions, the private sector, and business itself. What is clear from this research is that business owners themselves should take more responsibility and ownership for their own destiny. It will not be in the interest of small business to create and maintain a dependency relationship between small business and support institutions that will ultimately stifle SMEs ability to grow.

Below we highlight some of the key conclusions and recommendations that emanated from this study. It is evident that these require a focused approach designed to address some of the key blockages that have been identified.

### **10.2. Results and recommendations**

#### **10.2.1. Financial business development services**

While there appears to be a good awareness amongst small businesses of the existence and what fBDS providers provide, it is clear that few SMEs are using them. The reason being that business owners are of the opinion that their needs are not being met by what is being offered. It is recommended that more in-depth research be done on the support services provided by private and public fBDS in terms of what they offer, the effectiveness of their services and how they communicate these services to potential customers.

Simple information products, possibly in the form of a booklet or pamphlet, should be provided on the services offered by the various institutions. They should also be used to show how to set up and manage small businesses. A key area to focus on is communication. This includes how service providers should communicate with small businesses in terms of addressing their specific needs and in giving them feedback. It is important to remember that many of the business owners have lower levels of literacy and consequently, should be communicated with using simple messages and in their own language.

Training workshops to address the needs of small businesses is also a recommended approach and is already used quite widely. Cognisance must be taken of the concerns of small businesses in terms of the time that they have available and the limited financial resources they have to pay for them. One area that should be investigated further is the development and implementation of effective sector specific mentoring programmes for small business owners. A key area of focus should be financial literacy.

There are many fBDS providers in both the public and private sectors in South Africa. There is also much information available on services that they can

provide. A strategy needs to be developed to improve awareness of the support provided by fBDS and to ensure that SMEs use them more effectively. To accomplish this there is also a need for more communication and advertising. One of the recommendations coming out of the focus groups is for an integrated and co-ordination approach to the provision of fBDS in the different sectors.

Another recommendation is that the fBDS providers be located closer to where the historically disadvantaged SME business premises are situated. There is also a clear need for fBDS staff to be better trained in being more responsive to the needs of small business owners.

### **10.2.2. Banking and financial services**

While respondents reported that in general they were able to open and operate bank accounts, they generally found that obtaining access to finance from outside sources for their business was a challenge. The challenges were not confined to formal financial institutions alone but included the support institutions as well. This has resulted in much of the external funding for business being secured from informal sources (i.e. family and friends) or to an even larger degree from personal savings, pensions etc.

Black males, and to a larger extent female respondents, were more challenged than their Coloured and Indian counterparts when it come to financial access and in the majority of cases the sentiments were more forcefully expressed in the Black groups.

There is a great deal of frustration in the small business sector when it comes to access to finance from both the banking and other support institutions that have been established.

The focus group findings support to a large degree what was learnt from the FinScope Small Business study in that there are deficiencies on both the demand and supply side.

To a large extent, rejection of a loan application is being blamed on racial prejudices due to a large extent by the inability of the banks to communicate effectively with loan applications. This was very well illustrated by a respondent from Eersterust:

*“I don’t think it is based on colour, it is based on risk but they don’t go to the level where they explain to you what makes you a high risk.”*

The results of this study suggest that there is a need for formal banking institutions to change their mindset as to how they engage and communicate with small businesses. Proper training within banks will help to alleviate the problem and could lead to lower tensions between the clients and the banks.

One mindset change that financial institutions should consider is making the "business plan" requirement process much simpler. There should also be a redesigning of collateral scoring techniques with "non-western" collateral being considered. Making more flexible re-payment schedules available to SMEs and interest rate capping should also be considered.

### **10.2.3. Legal and regulatory matters**

From the input received from SMEs participating in the focus groups it can be concluded that more information and training on all aspects relating to the registering of businesses, the Labour Relations Act and BEE legislation is required. More specifically training is needed on what the business opportunities are that arise out of the BEE legislation. There is also need to locate more public institutions within the communities of historically disadvantaged SMEs. These institutions also need to be given greater support to enable them to strengthen the business and community associations.

It is recommended that the information needed by SMEs be published into a handbook. More intensive media campaigns can also be developed on the topics described above. This may well require the development of programmatic material and holding intensive discussions with appropriate media groups. Further research could be done on mechanisms of establishing effective associations and forums in disadvantaged areas that can address the specific needs of small businesses. Finally, there is also a need to conduct research into problems associated with the BEE policy and its procedures.

### **10.2.4. Knowledge and information management**

Generally small businesses are not sharing their experiences and learning with one another. As a consequence there is little evidence of there being a benefit. However, they are unanimous in acknowledging the value of knowledge and information as well as ICTs to their businesses. It is for this reason that there is a call for the greater support of forums and workshops as well as training so that business owners can reap the benefit. Cognisance must be taken of the needs and challenges of small businesses in using knowledge and information management approaches (e.g. literacy, language).

One of the main recommendations would be for government to develop a small business handbook that would explain policy and regulatory matters and provide step-by-step approaches in managing their businesses and getting support. It will be important to have this handbook translated into local languages. Government could also provide small grants to these businesses to enable them to capacitate themselves when it comes to ICTs. The Universal Service Access Fund (USAF) could possibly be used as a source of these funds and in this regard the Universal Service Access Agency for South Africa (USAASA) should be approached.

More radio and television programmes could be developed using the handbook as the basis to address the many needs and challenges of small businesses. It is important to emphasize that a systematic communication campaign should be

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The value of the knowledge portal is that it provides a single repository for information and handbooks on policies and regulations, SME practices, tax and registration, access to finance and financial business development services. It could also be a place where training events, workshops and business Expos could be advertised. The knowledge portal would also provide access to accredited on-line training courses for SMEs. It could also feature articles by prominent business people on different aspects relating to managing and running small businesses. SMEs would also be able to become a member of the knowledge portal and a web page provided where they can provide a profile of the businesses. To ensure the effective use of the knowledge portal a 'pull' and 'push' approach should be used in accessing relevant information for the knowledge portal and sending it out to registered SMEs.

## ANNEX A

### SME BUSINESS RECRUITMENT QUESTIONNAIRE

Date August 2008

Questionnaire Number:		
Interviewer Name:		
Supervisor's Name:		
Date Supervisor Checked:		
Area:		

#### INTRODUCTION

Good Morning / Afternoon / Evening. My name is í í í í í . (SHOW ID) I am from a market research company called **DYNAMIC RESEARCH**. We are conducting a survey to try to understand how small businesses operate in South Africa. May I please speak to the owner of the business / manager or partner? Any information you provide will be treated in the strictest confidence.

#### COMPANY DEMOGRAPHICS

1. For demographic purposes please indicate your annual turnover (excluding VAT) for 2007/2008 (this information will remain confidential and used purely for segmentation purposes)

R 100,000 to R 200,000	1
R 200,000 to R 499,000	2
R 500,000 to R 999,000	3
R 1 million to R 2,999,000	4
R 3 Million to R 4,999,000	5
R 5 Million and Above	6

2. Number of full time employees - % split between management and non-management in the business.

Up to 5	1
6 to 10	2
11 to 25	3
26 to 50	4
51 to 100	5
101 to 200	6
More than 200	7

3. For how long has your company been in operation?

Up to 12 Months	12 to 24 Months	2 to 5 years	More than 5 years
1	2	3	4

4. Please indicate which industry sector your organisation falls under? SINGLE RESPONSE

Mining	1		
Manufacturing	2		
Electricity, Gas and	3		
Construction	4		
Retail Trade	5		
Tourism	6		
Wholesale trade	7		
Catering and accommodation	8		
Transport	9		
Finance, Insurance and Business Services	10		
Community, social and personal services	11	Professional:	
Specific industry sectors:		Accounting	1
Professional business	1	Medical	2
Traditional business (in operation longer than 2 years)	2	Engineering	3
Start-up business (in the last 24 months)	3		

5. Language

1. Which language do you speak most often?	Language	
	Zulu	
Ndebele		
SiSwati		
South Sotho		
North Sotho		
Tswana		
English		
Afrikaans		
Venda		
Xhosa		
Tsonga		

## 6. Respondent Information

Name of the Business	
Formal / Informal	
Type of Business (CC, PTY, LTD or NGO)	
Title:	
First Name:	
Surname:	
Business Physical address:	
Home Telephone No:	
Work Telephone No:	
Cell number:	

### ASK ONLY FOR

Terminate if business run in any of:	<ul style="list-style-type: none"> <li>• From A Container</li> <li>• A Stall / Market</li> <li>• On A Footpath</li> <li>• Car Boot / Truck / Bakkie</li> <li>• No Fixed Location</li> </ul>	<b>If other, Specify</b>
--------------------------------------	---	--------------------------

**Arrange to attend the focus group:**

**Date**

**Time**

**Venue**

## **ANNEX B**

# **FOCUS GROUP DISCUSSION GUIDE**

## **QUALITATIVE RESEARCH ON SMALL AND MEDIUM ENTERPRISES IN GAUTENG**

# QUALITATIVE RESEARCH ON SMALL AND MEDIUM ENTERPRISES IN GAUTENG

## 1. Background to the study

The Chemonics Consortium has been contracted by USAID to conduct research on how small and medium enterprises (SMEs) gain access to finance, especially those owned by historically disadvantaged individuals. The objective of the USAID Financial Sector Program (FSP) is to improve SME access to affordable financial services. This is to be done by lower financial costs through legal and regulatory reform and improving the commercial viability of lending to historically disadvantaged SMEs in South Africa. The definition being used for SMEs is that of the banking association, which is businesses with a turnover of between R500 000 ó R20 million.

The research team wants to undertake further quantitative and qualitative research in order to gain a better understanding of SMEs in South Africa. This will enable them to make a more informed decision about which businesses can be considered to be small or medium enterprises. To this end it was decided to conduct a number of focus group discussions with individuals who own small businesses in Gauteng province. The results of focus group discussions will enable the research better understand the financial needs of SMEs. This information will be used to plan and implement a range of initiatives in collaboration with various local stakeholders over the next three years with a view to improve the conditions under which SMEs are established and do business. Since initial data analysis suggests that the threshold of R500 000 excludes large numbers of small businesses, it was decided that the study should focus on SMEs with a turnover of between R200 000 and R20 million.

During the focus group discussion we would like to gain a better understanding of both the opportunities and challenges that SMEs face. The ultimate objective will be to advise government and financial institutions on how they can better support small businesses in South Africa.

The following areas should be covered during the focus groups:

- The need and use of business development services;
- The use of banking/financial services;
- Legal/regulatory matters;
- Knowledge/information management.

Below we provide an outline of the areas that should be covered during the focus group discussion. The purpose of the outline below is to provide you with a list of issues that should be covered during the focus group discussions.

## 2. Ice-breaker discussion

Please tell me about yourself. How did you start your business?

**(Note to facilitator:** Here we would like to get a sense of the extent to which prior knowledge (as a result of either formal or informal training, e.g. parents' business, indigenous knowledge, and mentorship) played a role in the participants' decision to start their own business.

## 3. The need and use of business development services

- a. Please tell me what support/advice services are you aware of that are available to you from government, financial institutions, and other businesses to assist you in running your business?
- b. Which of these services have you used in the past? Did these address your needs?
- c. In your experience, what type of assistance/support does your business need most?

**(Note to facilitator:** Probe areas such as:

- i. Where and how can participants access financial support to start/expand their business?
  - ii. How to improve performance/productivity?
  - iii. Financial management, for example preparing financial statements, budgeting, costing/pricing, and taxation).
- d. Does your business have a written business plan? Do you need assistance in developing a business strategy/plan for your business?
  - e. How do you make potential customers aware of your business?
    - i. Is it important to have a marketing plan?
    - ii. Do you need support in developing a marketing plan for your business?
  - f. How do you keep your business's records? What kind of assistance do you need in this regard?

**(Note to facilitator:** here we would like to understand the extent to which SMEs use formal record keeping systems (such as bookkeeping, cash flow, invoicing, and keep track of stock. This record keeping may be either paper based or electronic (computer software))

- g. In your experience, is communication from government and financial institutions to you adequate to inform you on requirements and what support is available to you to run your business?

## 4. Banking/financial services

- a. Do you presently use any financing from outside your business operation?
- b. If no, do you need such outside financing?
- c. If you do need outside financing, where do you intend to apply for it?
- d. If the answer to question number one is 'yes', who provides that outside financing and what are the terms (interest rate, fees, repayment schedule, collateral, etc.)?
- e. Have you ever applied for a bank loan or financing from any other financial institution (FI)?
- f. If your bank or other FI loan application was denied:
  - i. Did the bank/FI tell you why the loan was not approved?
  - ii. If the answer to 6a. is 'yes', what reasons for the declination did the bank/FI give? (examples: insufficient collateral, insufficient equity contribution, insufficient cash

- flow, business is a start-up with no track record, no enough financial information on the business, etc.)
- iii. Did the bank/FI specify what you needed to do to get your application approved? If they did specify, what were those conditions that you needed to meet to get the loan approved?
  - iv. Did you then apply for financing to a non-bank financial institution (FI), such as a finance company, an auto dealer, a supplier, or a government FI (such as Khula)?
  - v. If the answer to 6d. is *õyesõ*, was your loan approved and if so which FI approved the loan and what were the terms?
- g. If your bank/FI loan application was approved, did the bank provide a loan that met your needs?
- i. Was the loan amount big enough?
  - ii. Was the repayment schedule appropriate (for example, an overdraft or 6 months loan would not be appropriate for a loan to finance machinery or equipment)?
  - iii. Did the bank allow you enough time to repay?
- h. If you have never applied for a loan from a bank or other FI:
- i. Why haven't you?
  - ii. Have you ever applied for a loan from a non-bank FI?
  - iii. Ask the same questions as in 6e. above.

## 5. Legal/regulatory matters

### *5.1 Legal requirements and compliance:*

- a. Is your business formally registered as a business with the Department of Trade and Industry? If no, why not? If yes, as what is your business registered?
- b. When you started your business, did you receive any advice on the best (legal) vehicle (i.e. a Closed Corporation, a Pty, a partnership, or a sole proprietor.)
- c. Why did you select the current legal vehicle for your business?
  - i. Do you know what a close corporation is?
  - ii. Do you know that being registered as a close corporation can protect your personal assets against liabilities?
  - iii. Do you want to have more information and training on legal requirements and opportunities?
  - iv. If you are registered, did you find the registration process simple and easy? How can it be improved?

**(Note to facilitator:** Here we want to establish whether participants understand the various options mentioned above and the obligations and liabilities associated with each?)

- d. What are you current responsibilities regarding tax (VAT, company tax, PAYE, etc.)
- e. Do you know that businesses with an annual turnover less than 1 million Rand won't pay VAT as of 2009?
- f. Are you an employer, in other words, do you have any employees that work for your business?
- g. Are familiar with the requirements of the Labour Relations Act?
- h. How do they manage staff? Compliance to the LRA, etc.

- i. Do you need training regarding the legal requirements as an employer? In what aspects?

#### *5.2 Relationship with public institutions*

- a. In your experience, what are the most important things that government should do to assist small businesses? Do you have contact with public institutions?
  - i. At the municipality level?
  - ii. At the province level?
  - iii. At the national level?

- b. Are public institutions useful? Do you think that they should have more presence in your neighbourhood?

**(Note to facilitator:** We would like to identify the most important areas that would address small business needs. For example policy/legislative, tax reform, finance availability, simplification/streamlining of processes (at national, provincial and local level)?

#### *5.3 Knowledge of BEE legislation*

- a. Is your business a Black Economic Empowerment (BEE) enterprise?
- b. Is your business registered with Department of Trade and Industry (IMEX) as a BEE enterprise?
  - i. Do you know the BEE legislation? Would you like more information and training on this theme?
- c. If yes, what are the advantages? E.g. preferential procurement and enterprise development, and others.
- d. In your understanding, what do you need to access BEE benefits? Financial, technical support, etc.
- e. Do you think that your business could grow thanks to the BEE legislation? How? What kind of support do you need to take advantage of BEE opportunities?

#### *5.4 Association membership and Advocacy*

- a. Are you a member of a business or professional association?
  - i. If so, does this association adequately defend your interests and express your concerns with public and financial institutions?
  - ii. If not, how do you communicate with government and financial institutions regarding your needs/concerns?
  - iii. What kind of support would you like to better express your needs and expectations to the government concerning your business (at the municipality, province and national levels?)

**(Note to facilitator:** This question about advocacy applies to all components of the study)

## 6. Knowledge/information management

In this last part of our discussion, we would like to know how you use past experience, either your own or that of others, to improve your business.

- a. How do you share your experience with other businesses or learn from the experience of others?

**(Note to facilitator:** Here we want to gain a better understanding of the mechanisms that do exist for inter-organizational knowledge sharing and learning)

- b. In your view, how can government and other organizations support the exchange of best practises among SMEs?

- c. In your view, what are the knowledge and learning needs, capacities and challenges of/for businesses like yours?

**(Note to facilitator:** This question has dual functions/areas of focus: intra-knowledge and learning needs; inter/extra-knowledge and learning needs in response to environmental stimuli. In other words, how do you know about changes in your business environment, changes in government policies which affect your business?)

- d. In your experience, how does information sharing and learning take place within the financial sector in order to provide the best support to "BEE" SMEs?

- e. In your experience, do issues of culture, identity and religion influence the way in which the financial sector support small business development? How?

**(Note to facilitator:** culture does not only refer to customs, it is used a multi-descriptor for social heritage/tradition; generalized organizational/human behavior, structural patterns of inter-relations.)

- f. In what ways can the use of the benefits of experience and learning that takes place within the SME sector be best determined? How can these be made more systematic and evidence-based?

**(Note to facilitator:** here the focus is on their thoughts and perceptions on interventions like movements such as Reddingsdaadbond (our act of rescue), the Helpmekaar (help one another), communities of practice, peer assist.)

- g. In your view, in what ways can Information Technology (IT) systems (computers, internet, etc) support or inhibit the knowledge and learning in the SME sector?

**(Note to facilitator:** It is important to probe people's variable access to IT systems (the so-called "digital divide" impacts on SME ability to operate and grow - particularly in the financial sector?)

Thank you for participating in this study.

# **BSM PROFILE GAUTENG**

**August 2008**

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## LIST OF ACRONYMS

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BDS	Business Development Services
BEE	Black Economic Empowerment
BSM	Business Sophistication Measure
CC	Closed Corporation
CIPRO	Companies and Intellectual Property Registration Office
DBSA	Development Bank of Southern Africa
DTI	Department of Trade and Industry
FI	Financial intermediaries
FSP	Financial Sector Program
GEM	Global Entrepreneurship Monitor
GEP	Gauteng Enterprise Propeller
HDI	Historically Disadvantaged Individual
ICT	Information and Communication Technology
LRA	Labour Relations Act
MSE	Medium and Small Enterprises
NEF	National Empowerment Fund
PAYE	Pay-as-you-earn
SADC	Southern African Development Community
SARS	South African Revenue Service
SEDA	Small Enterprise Development Agency
SETA	Sector Education and Training Authority
SME	Small and Medium Enterprises
SMME	Small, Medium and Micro Enterprises
UIF	Unemployment Insurance Fund
USAASA	Universal Service Access Agency for South Africa
USAF	Universal Service Access Fund
USAID	United States Agency for International Development
VAT	Value Added Tax

# BSM PROFILE GAUTENG

## 1. Background

A review of key documents on SMME finance commissioned by the FinMark Trust found that there are various and differing definitions of the term 'SMME' in South Africa. South Africa differs from international categorizations that broadly define two categories, one at the lower end of the market grouped as micro and small enterprises (MSEs) and the higher end of the market grouped as small and medium enterprises (SMEs).

The primary objective of the FinMark Trust research was to size the small business market. The survey was weighted to the adult population of Gauteng province (16 years+) of 6 635 000.

The survey findings indicate that the total number of small business owners in Gauteng is estimated at 1 053 818. This means that approximately one in six individuals is involved in small business activities.

While South African definitions have been detailed, they have been varied and have not resulted in effective targeting of services to SMMEs.

The various definitions that have been used in South Africa are numerous:

- Survivalist enterprises;
- Micro enterprises;
- Very small enterprises;
- Small enterprises;
- Medium enterprises;
- Large enterprises.
- Ntsika State of Small Business Development in South Africa Annual Review identifies survivalist and single-person micro enterprises as constituting the informal sector. Medium and large enterprises constitute the formal sector. Micro enterprises employ less than 5 people. Very small and small enterprises are considered to be a mix of the formal and informal sector. Survivalist enterprises are described as pre-entrepreneurial (Ntsika 1999).
- Definitions have also been based on marginalization.
- The Small Business Strategy differentiates SMMEs in terms of the constraints they face.
- The Global Entrepreneurship Monitor (GEM) report 2002 makes the distinction of formal and informal enterprises in terms of economic contribution, education, resources and needs.

- Porteous (2002) makes the distinction of between formal and informal based on legal status (registration), tax registration, and the keeping and auditing of accounting records.
- The Micro Enterprise Alliance (MEA) conducted a study in 2000 distinguishing between "organized" and "unorganized" SMMEs in urban areas. Organized enterprises have salaried employees and fixed premises. Unorganized enterprises consist of artisans without fixed premises with few or no employees. No reference is made to legal status. (ECI, 2000)
- The National Small Business Act (South Africa, 1996) defines SMMEs according to the sector that the business is operating within. This is outlined according to number of employees, turnover and assets.
- GEM uses the distinction of "Opportunity" and "Necessity" Entrepreneurship based on the factors driving the entrepreneur to start a business.

The Global Entrepreneurship Monitor (GEM) Report (Foxcroft, et al 2002) indicated that there is a growing need for careful segmentation of different types of entrepreneurs to ensure the effective targeting of policies and services according to different needs. The report argued that the size categorizations are so wide that they are not helpful for targeted policy making.

Although the role of small business has been recognised as very important, the SME market place has to date been too poorly monitored and understood to be effectively managed and developed. The lack of information and understanding means that servicing, assisting and measuring this sector of the economy is a virtual impossibility.

A key implication is that small business requires specifically tailored products, services and assistance programmes, which need to go beyond simply targeting a single parameter of defining small business for example informal and formal or small and micro, but need to consider the possible overlap of other parameters.

The FinScope Small Business Survey aims to address the various parameters of small business activities with the explicit intention of sizing, benchmarking and segmenting the market for the first time.

The BSM measure was developed by AfricaScope to be used in the small business pilot study conducted in the province of Gauteng during 2006.

The model delivered a different way of studying the market based on variables other than pure turnover (which has proved in research to be an unreliable variable) and the number of employees.

Chemonics is interested in a greater understanding of the small business market generally but would like to focus initial efforts on the larger businesses and those run by historically disadvantaged individuals. In order to approach this sector, the BSM analysis was used as the base model.

## 2. The Landscape of Small Business

As stated above, previous investigations into the small business market have classified small business typically by 'informal' and 'formal' type business or 'registered' and 'unregistered' business. The following graph demonstrates this single dimension typology. Informal businesses are characterized by being a street vendor, a market or a stall trader or an individual that has not registered the business. Formal Business include those businesses that have registered their business with the Companies and Intellectual Property Registration Office (CIPRO) as a sole proprietor, a partnership, a co-operative, a close corporation or a (Pty)Ltd.

The table below is the question asked to determine business classification.

<p>ASK ALL SHOW CARD. On this show card is a list of options for you to choose from. In order to make the interview go faster and more smoothly, please just call out the numbers which apply to you when I hand you a showcard. If you can't understand what is on the showcard I will gladly assist you.</p> <p>What type of business is it? Just call out the number.</p> <p>ONE ANSWER ONLY</p>	<ol style="list-style-type: none"> <li>1. Informal / street / market / stall trader (small)</li> <li>2. Unregistered individual</li> <li>3. A sole proprietor / trader</li> <li>4. Partnership</li> <li>5. Co-operative</li> <li>6. A CC . close corporation</li> <li>7. A Pty Ltd</li> <li>8. Other: SPECIFY  <input type="checkbox"/> .</li> </ol>
---	--

It is apparent that the single parameter of 'formal' and 'informal' is not robust enough. A further breakdown of the standard criteria in the table below clearly indicates the need for an enhanced segmentation to support effective analysis.

### Characteristics

Informal street vendors, hawkers etc.	Unregistered individuals	Registered Businesses
<ul style="list-style-type: none"> <li>• Survivalist &amp; street market, stall market</li> <li>• Predominantly involved in the sale of goods</li> <li>• Operate in the informal sector of the economy</li> <li>• Won't employ others in the running of their business</li> <li>• Income generation below the poverty line &amp; average of R1 500 per month</li> <li>• No training, high school education</li> <li>• Approximately half have access to a bank account</li> </ul>	<ul style="list-style-type: none"> <li>• Many involved in sale of goods however activity seen in other sectors such as services or landlords</li> <li>• Not inclined to employ others</li> <li>• More inclined to run business from home</li> <li>• Never registered the business</li> <li>• For 30% income derived from business is not sole sources of income</li> <li>• Average monthly turnover R2 600</li> <li>• 55% banked</li> </ul>	<ul style="list-style-type: none"> <li>• Part of the formal economy</li> <li>• Registration of business a sole proprietor or a close corporation</li> <li>• 90% banked</li> <li>• Higher predominance of White and Indian business owners</li> <li>• More likely to be professionals</li> <li>• Skills learnt from post matric education or training programmes</li> <li>• Employ approximately 5 other people in the business</li> <li>• R21 500 average turnover of business</li> </ul>

### 3. Business Sophistication Measure (BSM)

The small business market is so diverse that it requires moving away from traditional and one-dimensional characterisations of the market that focus on homogenous units such as formality, size or legal status of the business. The survey results were used to develop a segmentation model that provides an enhanced way of viewing the market.

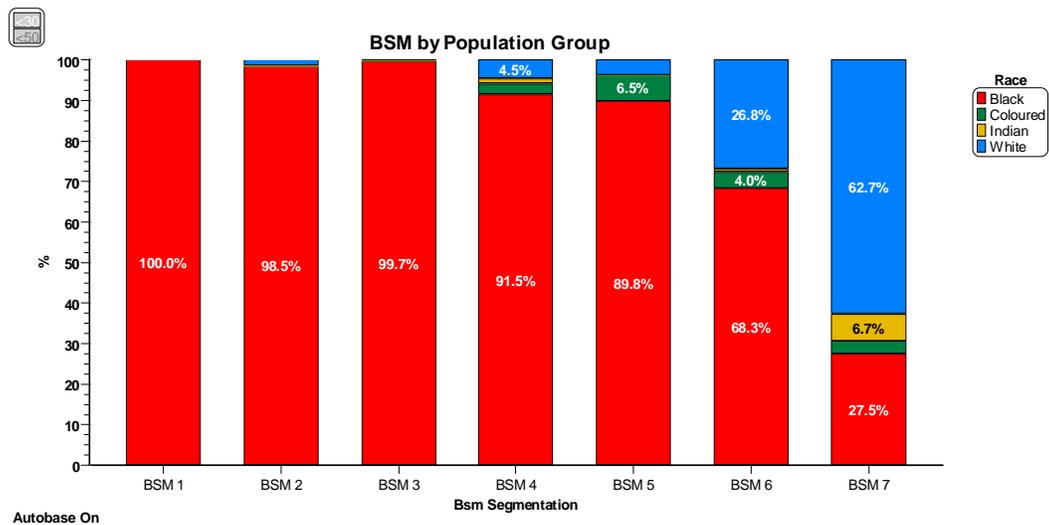
The Business Sophistication Measure was developed from a wide range of variables measured in the survey. As the name suggests the BSM assesses the degree of sophistication of small businesses operating in Gauteng, ranging from the informal street vendors to the more sophisticated and sustainable businesses. Sophistication of a business was gauged by a set of empirical variables that a business enterprise may or may not have. These variables ranged from the place where business is conducted such as a footpath or office block to whether the business keeps financial records, contracts of employment, access to finance and many more. Below are some of the questions used for the development of the Business Sophistication Measure.

Each variable was chosen in consultation with the FinScope Small Business Advisory committee.

- Type of Business;
- Does the business sell goods as they buy them or do they add value;
- Have a written employment contract for employees;
- Type of premises business operates from;
- Own, rent or use the place where business trades from;
- Services and equipment;
- Partners or shareholders;
- Written shareholders/partnership/ members agreements in place;
- Keep financial records or accounts;
- Keep financial records internally or have outside help;
- Auditing of financial records;
- Is the business a franchise;
- Business a subsidiary / part of another company;
- Affiliations with international companies;
- Import/ export/both?
- Offer goods or services on credit;
- Type of credit;
- Pay taxes;
- Compliance with regulatory acts;
- Professional services handled by staff;
- Banks used;
- Penetration of banking services;
- Loans in business;
- Place loan was obtained;
- Business insurance

It was considered that a measure of sophistication might be a better measure of the condition of a small business (rather than simply -informal or -registered) so as to guide whether that businesses was likely to grow or be a user of financial services.

An overview of the MSME market in Gauteng by BSM is as follows:

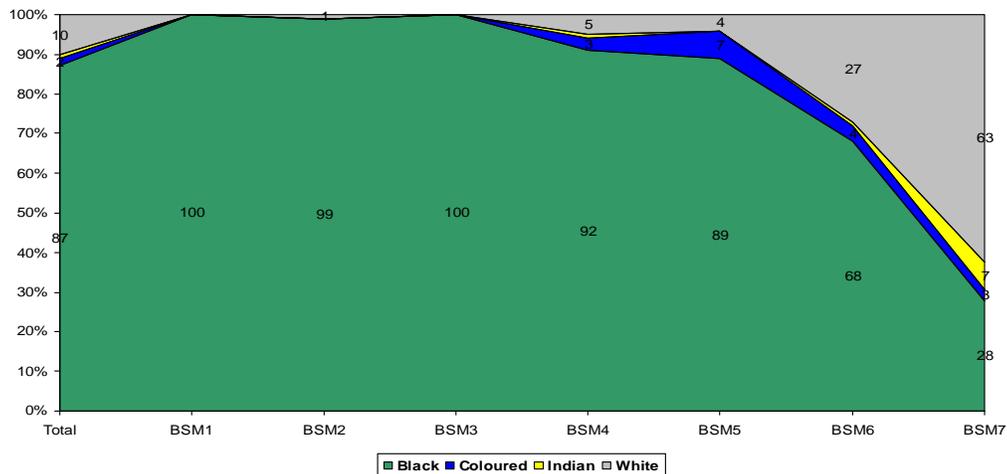


### 3.1 BSM and the formality of the business

Business enterprises in the lower BSM tiers are primarily informal vendors ó the majority of vendors and hawkers are found in BSM1. The upper BSM tiers have representation of formally registered businesses. In BSM 7, 94% of businesses are registered.

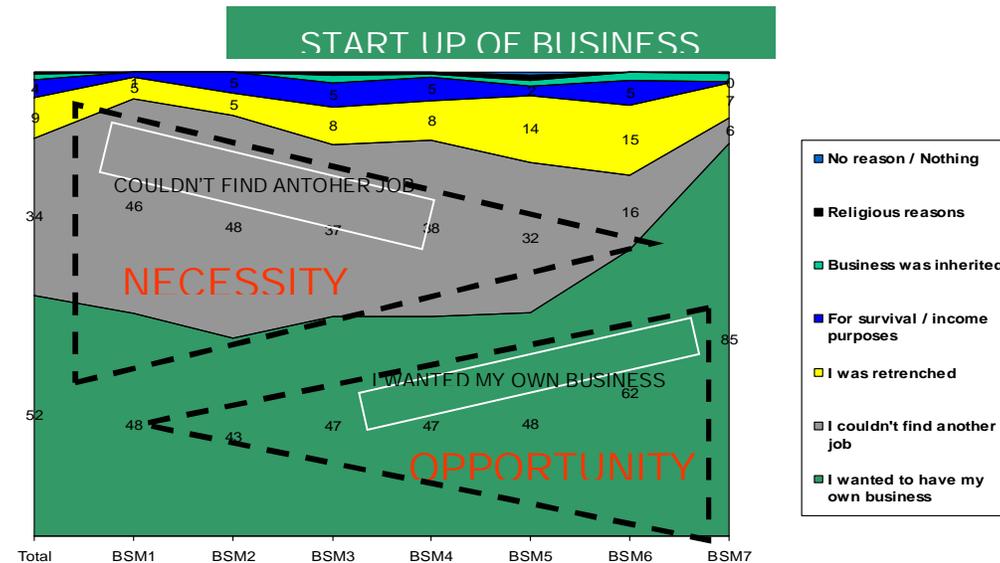
About 87% of all small businesses are owned and run by black owners. The majority of black owned business is found in the informal sector.

In BSM 7, 30% of small businesses are black owned, 1 in 10 coloured or Indian and 6 in 10 white owned businesses.



### 3.2 Reasons for start up

Looking at the Gauteng market overall, there is a clear continuum of reason to start a business.



Of the total market, over half of all respondents started their business because they wanted to. 34% started their business because they couldn't find another job. We classified these two reasons as necessity and opportunity based start ups. The necessity based businesses are individuals who have started a business because they could not find any form of formal employment. Their future survival is dependent on the income from these businesses. Opportunity based businesses however have seen an opportunity and this is something they wanted to pursue.

A look at reasons for starting a business is clearly illustrated across the BSM continuum.

The lower sector of the market is characterised by owners who started their business because they could not find another job. The higher BSMs however are opportunity based businesses.

### 3.3 Problems experienced during start up

No knowledge on how to start a business 58%	Finding Money to start my business 18% No knowledge of market conditions 12%	Finding Money to start my business 27%	Finding Money to start my business 28% Creating Awareness of Business 21%	Finding Money to start my business 43% Creating Awareness of Business 27% Finding a place to trade from 22%	Finding Money to start my business 44% Creating Awareness of Business 29% Finding a place to trade from 20% Finding right staff 17%	Creating Awareness of Business 43% Finding Money to start business 36% Limited Resources 24% Finding staff 24% Compiling business plan 23% Finding a place to trade from 20% Managing Finances 19% Registration Requirements 16%
BSM1	BSM2	BSM3	BSM4	BSM5	BSM6	BSM7

The most common problem experienced by all small business is finding capital to start a business. The most common problems experienced by the lower BSM tiers are 'not adequate knowledge on how to start a business' and 'no knowledge of the market conditions'. Marketing and differentiating ones business becomes significant in BSM 4 and up. More problems are experienced in the upper BSM tiers. This may be linked to protocol involved in the registration of the business or application for finance.

#### 4. A closer look at BSM 6 and 7

A quick overview of BSM 6 and 7 is as follows:

##### 4.1 BSM 6

<b>BSM 6</b>	<b>BSM 6 (n=184)</b>	<b>BSM 6</b>	<b>BSM 6 (n=184)</b>
<b>Race:</b>		<b>Type of Business:</b>	
Black	68	Informal	30
White	27	Unregistered	41
Coloured	4	Registered	29
Indian	1	<b>Area:</b>	
<b>Gender:</b>		City centre	9
Male	55	Suburb	34
Female	45	Township	43
<b>Age:</b>		Hostel	1
16-24	5	Informal area	7
25-34	32	Rural area	0
35-49	39	Small holding	6
50+	24	<b>Business Turnover over last 12 months:</b>	
<b>Level of Education:</b>		Up to R3000	11
No schooling	1	R3001-R10000	24
Some primary school	2	R10001-R50000	31
Primary school completed	3	R50001-R100000	19
Some high school	30	R100001-R200000	9
Matric	38	R200001-R300000	3
Post matric qualification	21	R300001+	3
Bachelor's degree	1		
Any post graduate degree	4		

#### 4.2 BSM 7

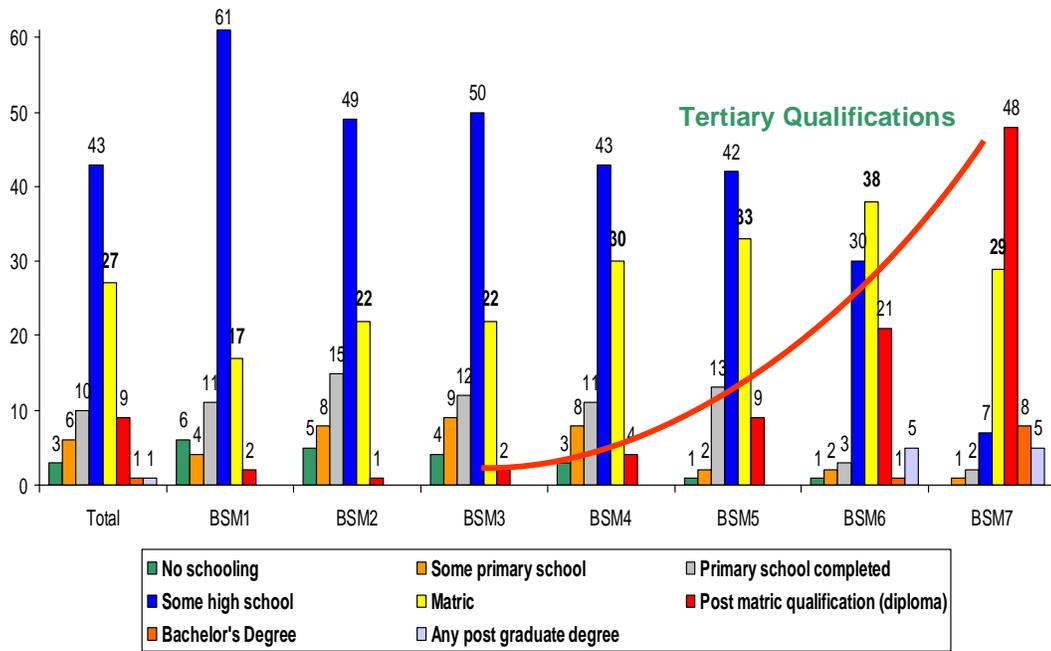
	<b>BSM 7 (n=123)</b>	<b>BSM 7</b>	<b>BSM 7 (n=123)</b>
<b>Race:</b>		<b>Type of Business:</b>	
Black	27	Informal	1
White	63	Unregistered	5
Coloured	3	Registered	94
Indian	7	<b>Area:</b>	
<b>Gender:</b>		City centre	19
Male	61	Suburb	53
Female	39	Township	14
<b>Age:</b>		Hostel	0
16-24	11	Informal area	2
25-34	20	Rural area	1
35-49	40	Small holding	12
50+	29	<b>Business Turnover over last 12 months:</b>	
<b>Level of Education:</b>		Up to R3000	6
No schooling	0	R3001-R10000	6
Some primary school	1	R10001-R50000	20
Primary school completed	1	R50001-R100000	18
Some high school	7	R100001-R200000	20
Matric	29	R200001-R300000	12
Post matric qualification	48	R300001+	18
Bachelor's degree	8		
Any post graduate degree	5		

#### 4.3 Significant Differences

The significant demographic differences between BSM 7 and 6 are:

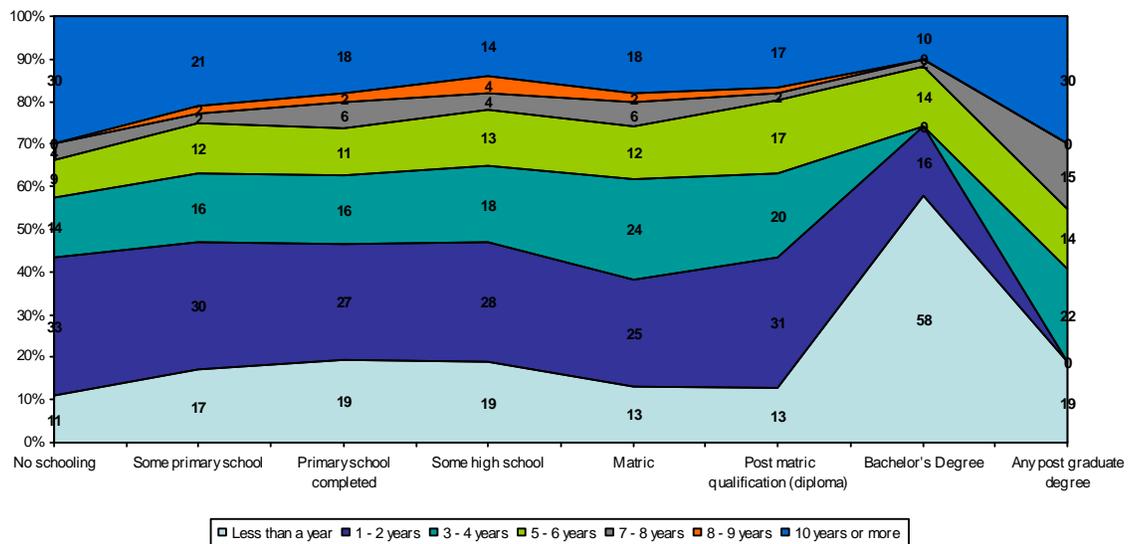
<b>PERSONAL DETAILS</b>	<b>BSM 7</b>	<b>BSM 6</b>
Home Language: English	26%	3%
Highest Level Of Education: Post Matric Qualification	43%	13%
Area: A Suburb	56%	22%
Areas Main Business Operates: A Suburb	49%	17%
Highest Level Of Education: Bachelor's Degree	16%	1%
Marital Status: Married	62%	43%
Home Language: Xhosa	11%	3%

#### 4.4 Education and the small business owner

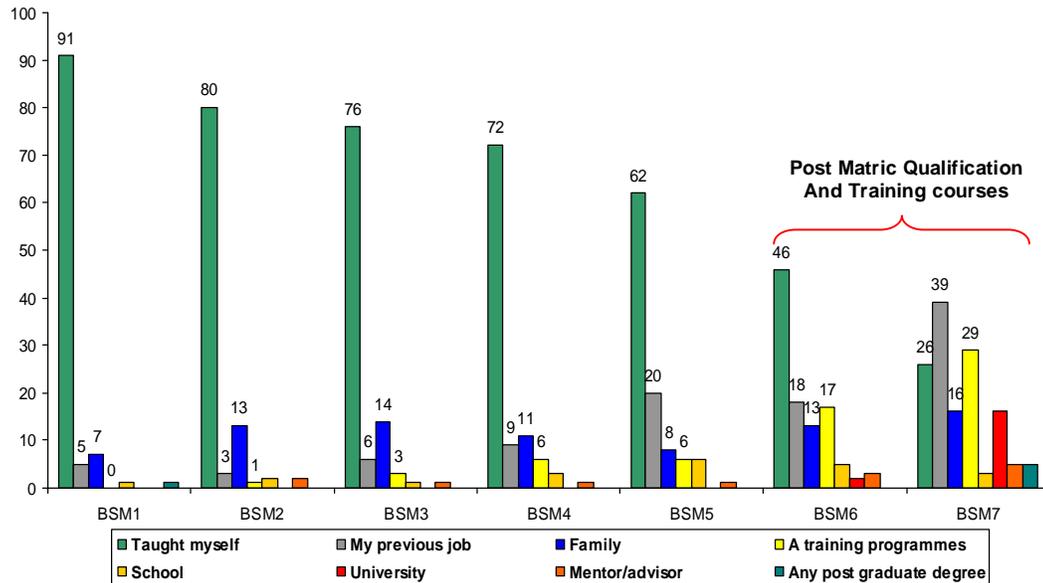


The majority of small business owners have achieved some high school education. The incidence of no schooling, primary school and some high school education achieved is higher in the lower BSM tiers. The number of business owners with a matric, post matric qualification (diploma), bachelor degree or post graduate degree is more apparent in the higher BSM tiers. Six in 10 business owners in BSM 7 have achieved a higher or tertiary education. The vast majority hold a post matric diploma.

Although there is a clear correlation between the level of education attained and the degree of business sophistication, there is no clear cut correlation between education attainment and longevity of the business.

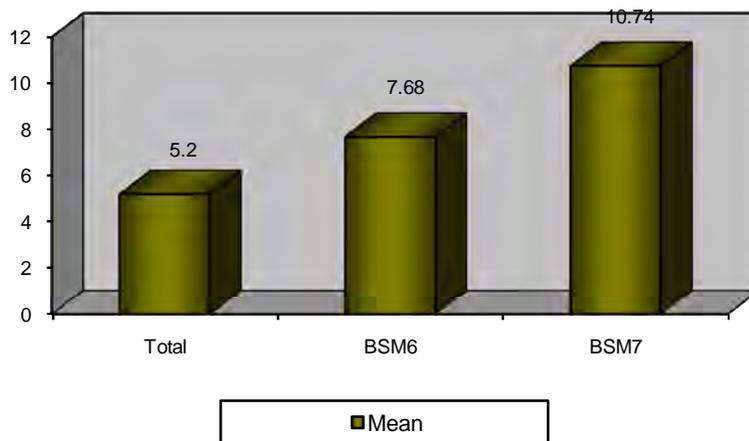


#### 4.5 Skills of the business owner



An overwhelming number of business owners have taught themselves the skills they use in their businesses. The incidence of self taught business owners decreases as business become more sophisticated. In BSM 6 and 7 there is clear evidence of higher education and training courses playing a role increasing the skills level of the business owner. The number of business owners who learnt their skills through previous work experience in the formal employment sector also increases with the level of business sophistication (BSM 5, 6 and 7).

Overall the average number of years work experience prior to opening ones own business is 5 years. The number of years increases as you look at the more formal types of business (7 years). Business owners in BSM 7 have on average 11 years work experience.

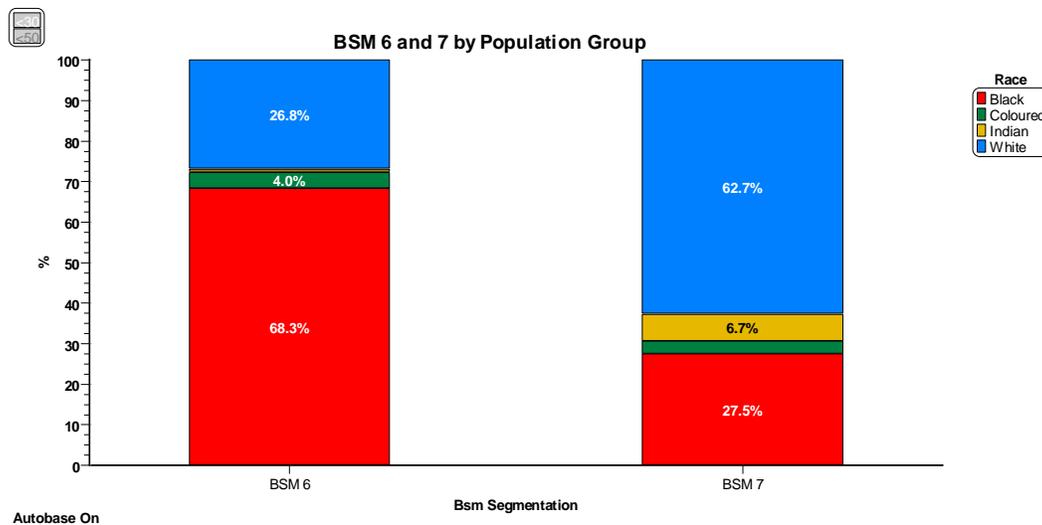


## 5. The USAID FSP brief

FSP is trying through the AfricaScope study to collect and analyze a broad range of detailed information on the financial needs of BEE SMEs, in order to accurately design and implement the next year work plan and determine the targets of the Performance Management Plan. This study will build on the 2006 FinScope small business survey, which delivered a comprehensive understanding of the small business market in the Gauteng province.

Given the contractual mandate to focus on BEE SMEs and not on micro-enterprises, we will only include in our target group businesses belonging to the BSM (Business Sophistication Measure) 6 and 7 categories. Some of these businesses fit under the Banking Association SME definition (annual turnover between R500 000 and R20 million). However most of them are below the minimum threshold but comprise the highest percentage of BEE enterprises.

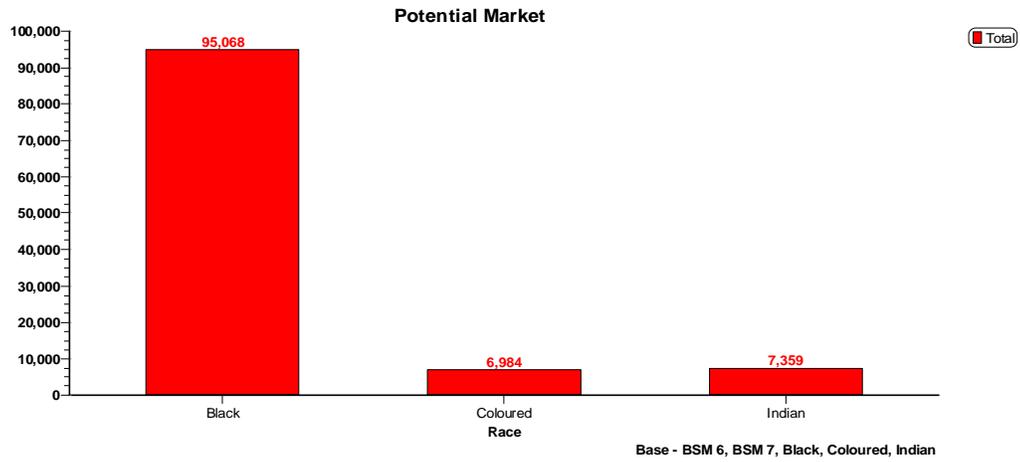
The brief requires that the initial study focus on the larger enterprises. In order to meet the turnover requirements in the brief; (HDIø with turnover in excess of R500 000) it has been decided to focus attention on BSM 6 and 7. The population group breakdown of BSM 6 and 7 is as follows:



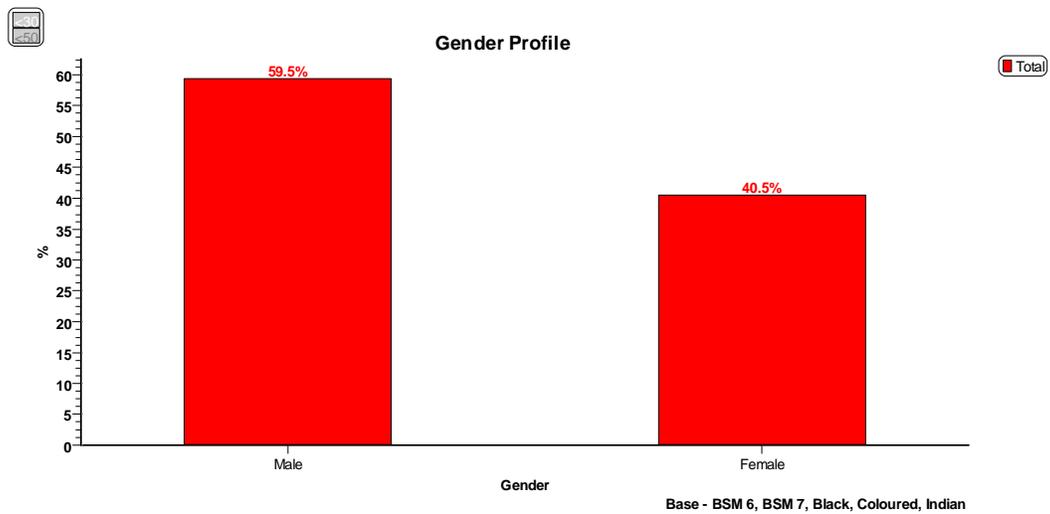
All further analysis in this paper is based on BSM 6 and 7 and filtered by Black, Coloured and Indian population groups. The income filter has not been applied in addition to the population groups for the overall analysis as this would render the respondent base sizes in most of the analysis too small to be valid.

## 6. Results

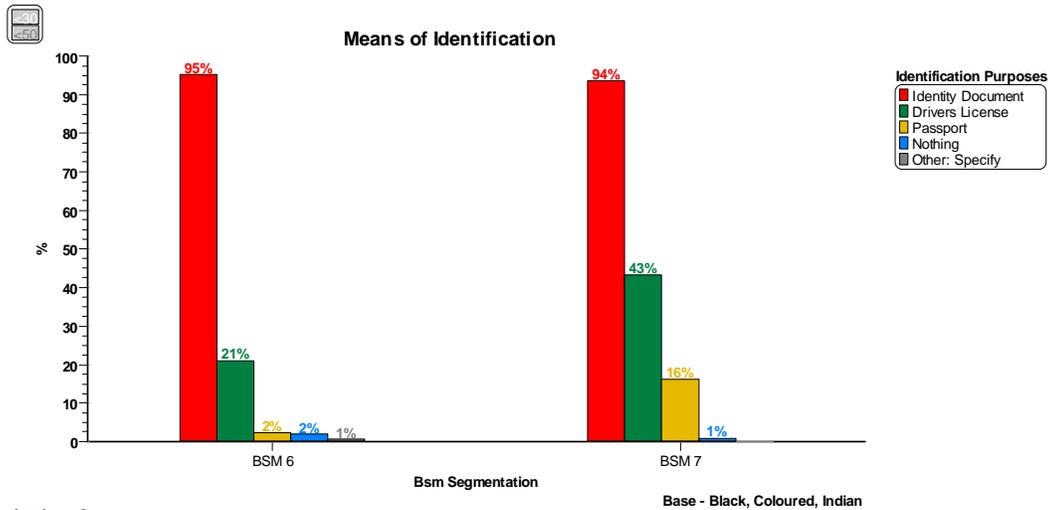
### 6.1 Size of the target group



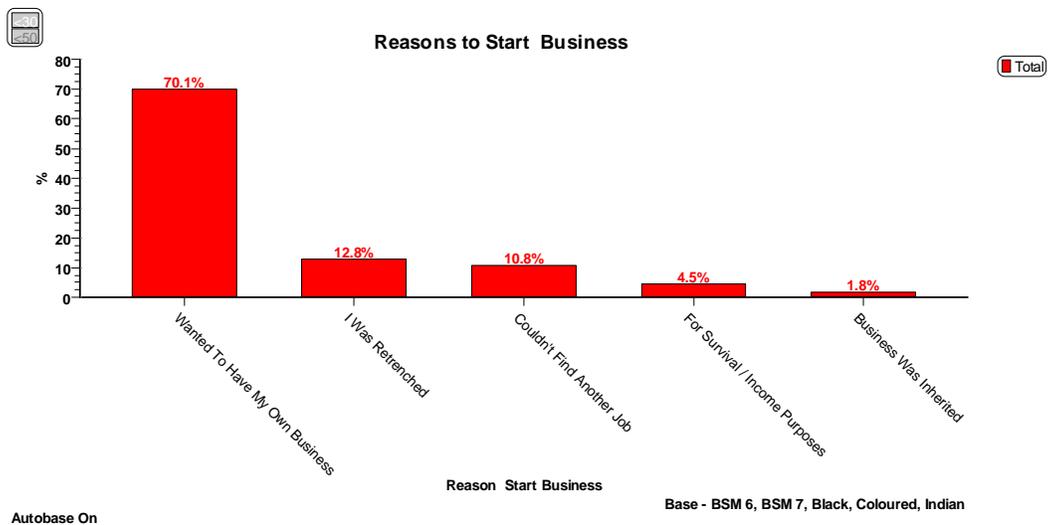
### 6.2 Gender profile



### 6.3 Means of identification



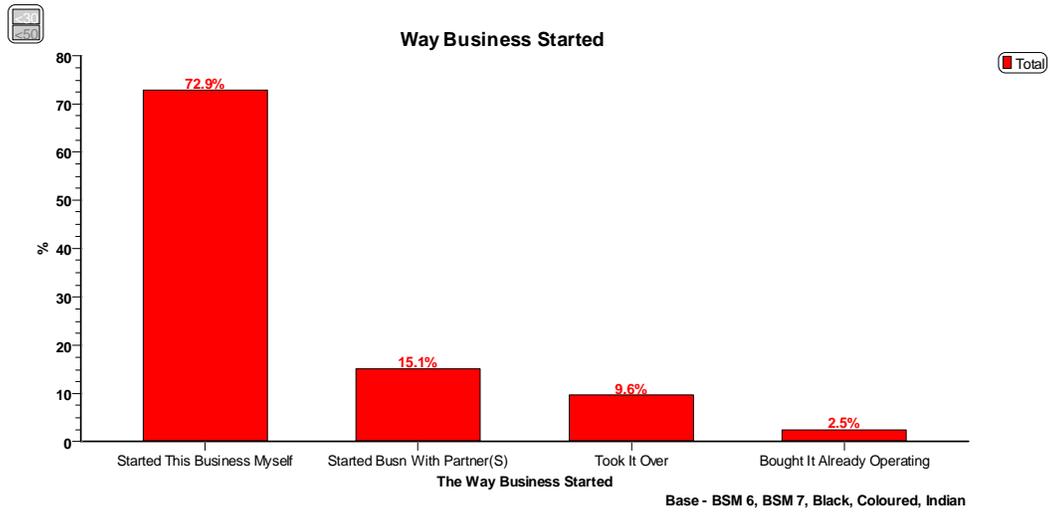
### 6.4 Reasons for starting business



Unlike the lower BSM groups the reasons for starting are strongly skewed towards always wanting own business rather than that they could not find any other work. This would tend to indicate a more sustainable group.

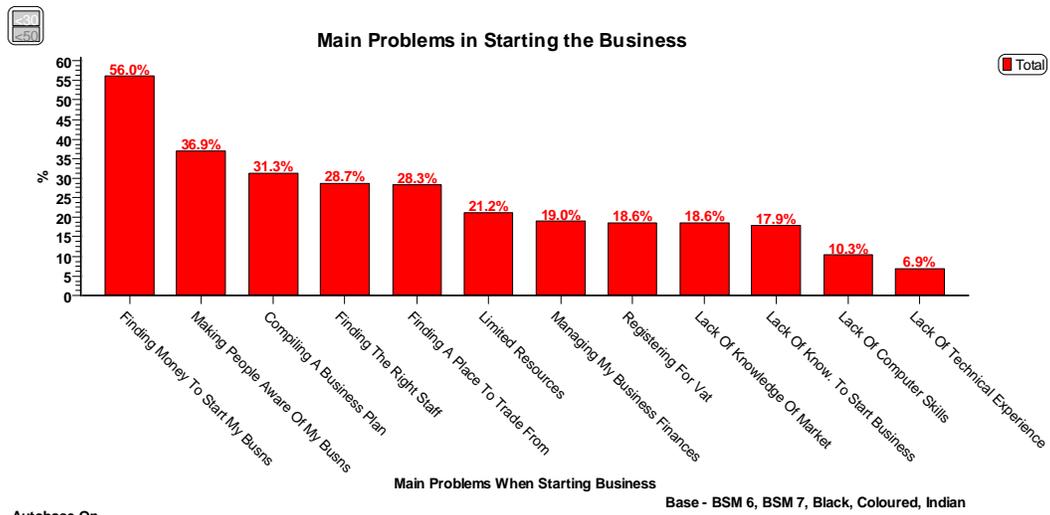
### 6.5 Way business started

The majority of businesses in BSM 6 and 7 were started by the current owners.



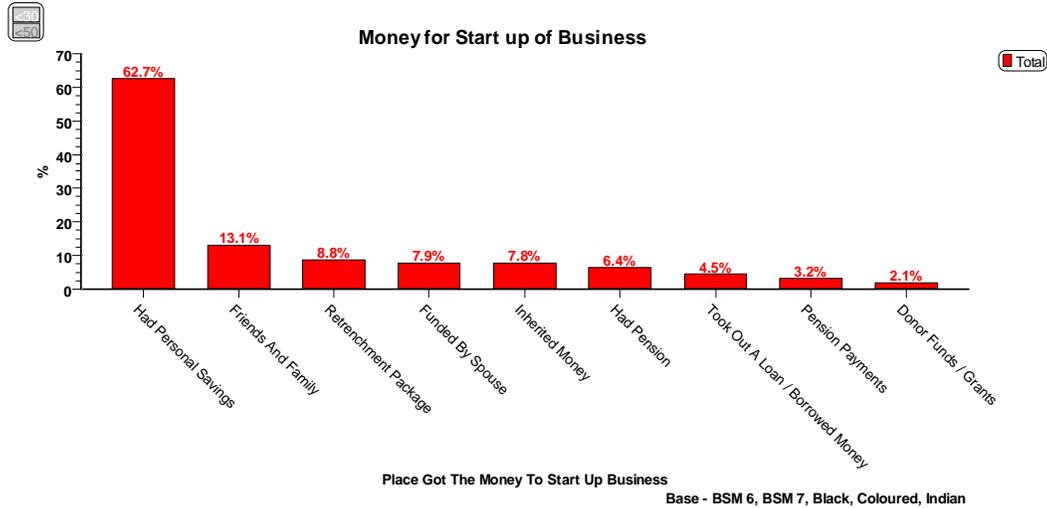
### 6.6 Problems starting business

Even in the top BSM groups, access to finance is an important issue when starting a business.



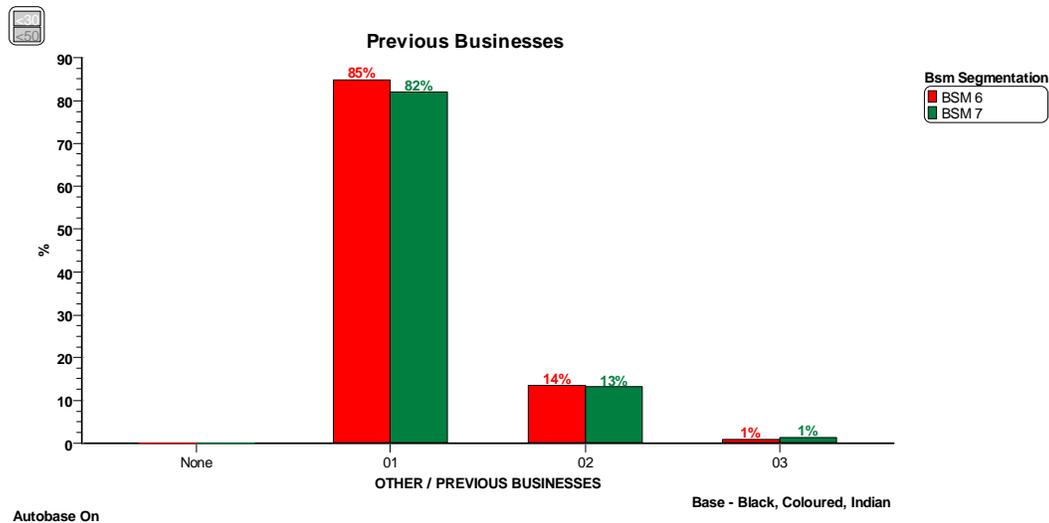
### 6.7 Money for business

In the target group, the majority of the money for the start-up of the business was already available via personal savings.



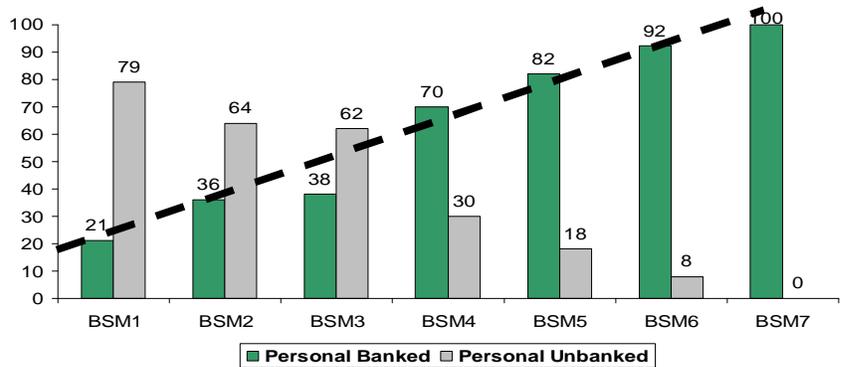
### 6.8 Previous business ownership

The pattern is similar for both BSM target groups with the majority having had one business prior to the existing business.

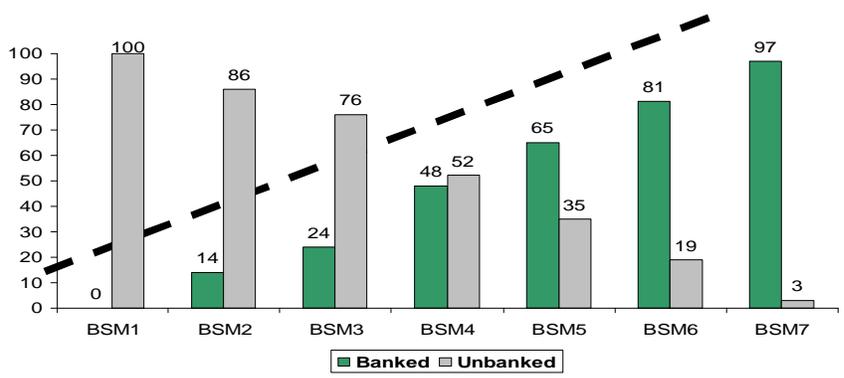


### 6.9 Current state of access to finance

The following chart looks at personal banking access by all small business owners in Gauteng. Overall 41% of business owners are currently un-banked, whilst 59% are banked. Only 21% of business owners in BSM 1 are banked in contrast to all business owners in BSM 7 having a personal account.

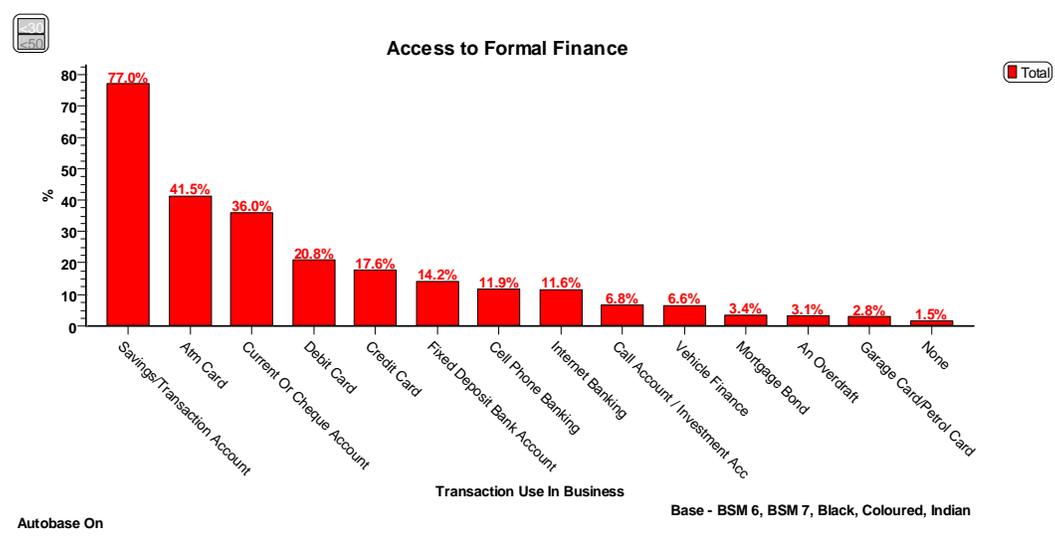


Small business enterprises that have a separate and specific business bank account stand currently at approximately 42%. Business bank account penetration in BSM 1 is zero, BSM 4 at 48% and BSM 7 at 97%.

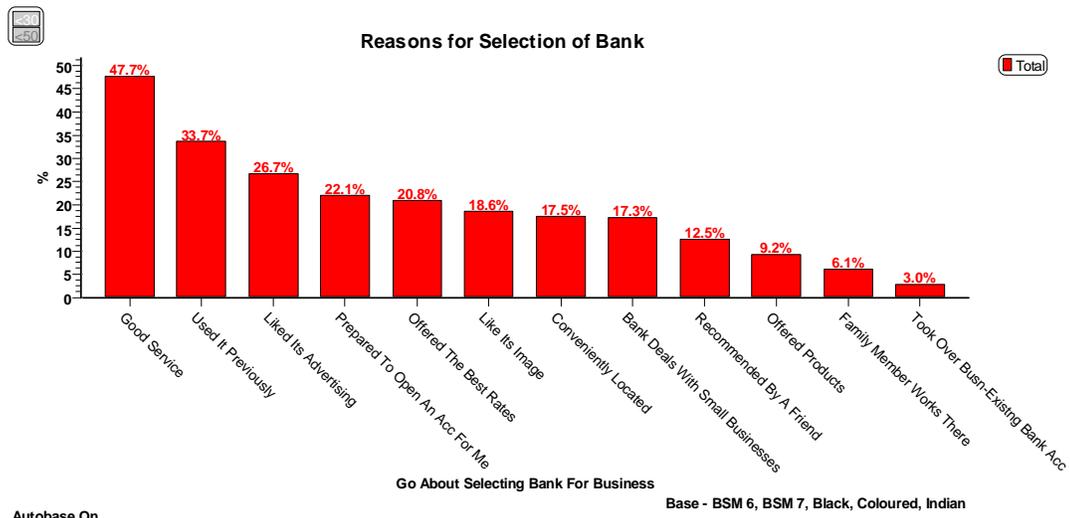


Of those businesses that have a personal bank account, but no business bank account, 57% use their personal bank account for business purposes.

The penetration of formal financial product in the BSM 6 and 7 HDI target groups is as follows:



The penetration of Savings accounts is significantly higher than any of the other financial products. Reasons for selection of a bank tend to be around imagery rather than the traditional access barriers of 'prepared to open account, proximity and cost':



### 6.10 Material differences in financial access

When it comes to financial transactions and sophistication, BSM 7 is very much more advanced than BSM 6. The significant differences in terms of banking and financial issues between BSM 6 and 7 HDI individuals is as follows:

#### 6.10.1 BSM 6

The most significant differences between BSM 6 and 7 are that individuals in BSM 6 do not conduct electronic bank transfers - 60%, do not draw cheques - 48%, and do not deposit cheques - 39%. When they go to the bank they go by taxi/minibus ó 30% and they also tend to walk to the bank - 5% to obtain bank statements in the branch - 86%. They do not perform money transfers between bank accounts - 24% and they do not currently use for a bank for business banking - 19%. 99% do not have a loan for their business.

On average they go into the bank monthly - 24%. They tend to use their personal account for business - 13%. They do not make electronic account payments to someone else - 11% and the account they use for business is the savings/transaction account - 76%

The average time they currently spend travelling to and from the bank is between 21-30 minutes - 29%

They request balance enquiry in the branch - 70% as well as making account payments to someone else in the branch - 83%.

### 6.10.2 BSM 7

Unlike BSM 6, BSM 7 have a rich repertoire of electronic transaction that make them significantly different to BSM 6. They perform balance enquiries the internet - 43%, perform account payments to someone else via the internet - 43% as well as obtaining bank statements via the internet -36%. They use internet banking - 37% and perform money transfers between bank accounts on the internet - 44%, electronic bank transfers via the internet - 46% and want banks to communicate with them via e-mail - 40%.

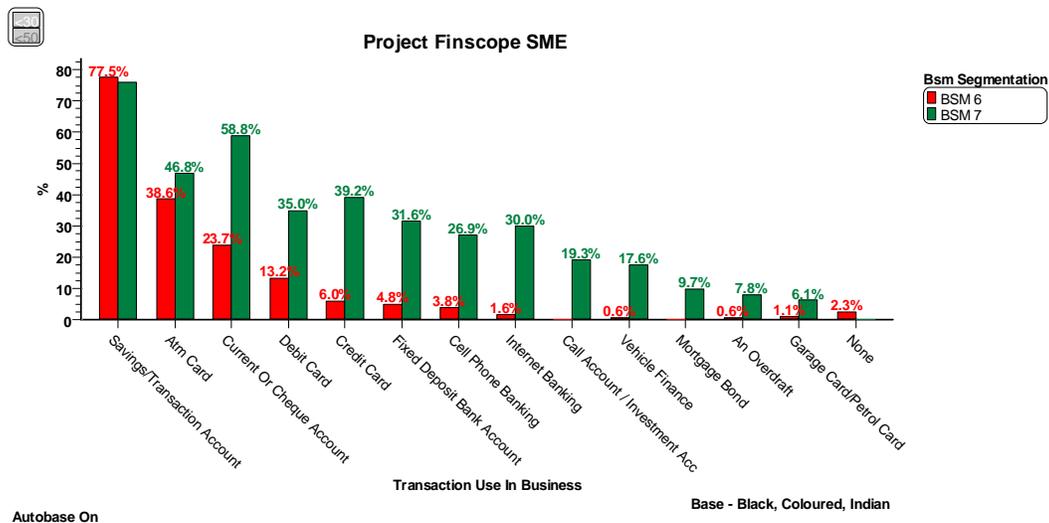
Transaction accounts used in business are credit cards - 38%, current or cheque account - 67%, an overdraft - 23%, garage card/petrol card - 21% vehicle finance - 19% and a call account / investment account -16%. None have debit cards for the business.17% use cell phone banking. They use the cell phone to make payments to other people's accounts - 9% as well as obtaining balance enquiry via a cell phone - 10%.

Cheque deposits are made in the branch - 91% and draw a cheque in the branch - 86%. They personally go to the bank in their own car - 84%.

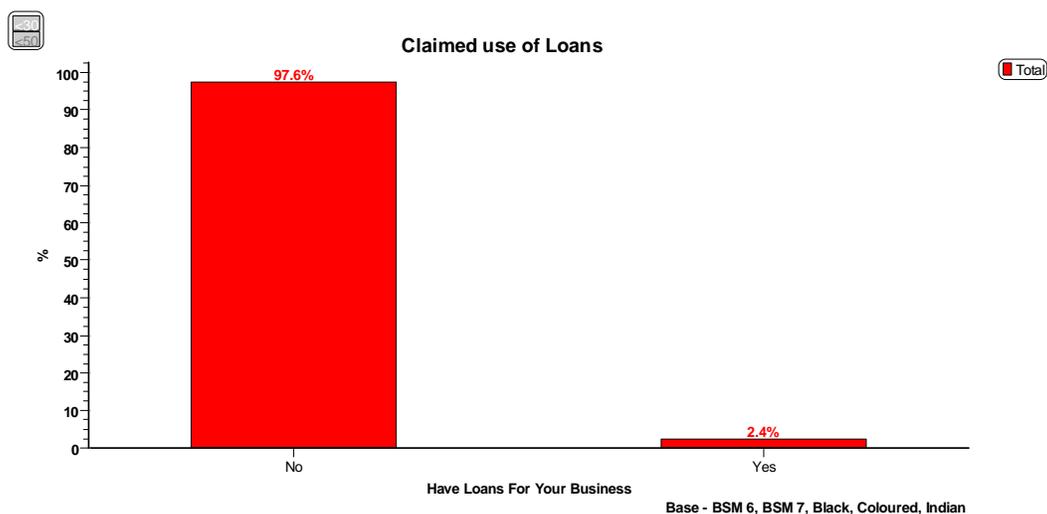
11% claim to have loans for the business.

On average BSM 7 go into the bank weekly - 37%. They go about selecting bank for business offered the best rates - 29%.

In terms of product, the usage patterns are as follows:



The majority of business owners in BSM 6 and 7 claimed not to have a loan in their business.



### 6.11 Overall banking differences

The significant differences between the two BSM groups in terms of financial behaviour are as follows:

<b>BANKING &amp; FINANCE</b>	<b>BSM 7</b>	<b>BSM 6</b>
Account payments to someone else: via the internet	32%	1%
Balance enquiry: via the internet	25%	0%
Transaction use in business: internet banking	30%	2%
Transaction use in business: credit card	39%	6%
Way Like Bank should communicate in future: By E-mail	36%	5%
Money transfers between bank accounts: via the internet	36%	6%
Transaction use in business: call account / investment account	19%	0%
Transaction use in business: fixed deposit bank account	32%	5%
Bank statements: via the internet	18%	0%
Transaction use in business: current or cheque account	59%	24%
Transaction use in business: cell phone banking	27%	4%
Cheque deposits: in the branch	86%	52%
Transaction use in business: vehicle finance	18%	1%
Draw a cheque: in the branch	79%	46%
Electronic bank transfer: via the internet	35%	9%
Banks currently use for business banking: First National Bank	51%	23%
Go about selecting bank for business: bank deals with small businesses	32%	9%
Personally go to the bank: go in my own car	74%	43%
Balance enquiry: via a cell phone	19%	2%
Bank statements: via a cell phone	12%	0%
Banks currently use for personal banking: First National Bank	49%	23%
Average time spend in the bank: less than 10 minutes	30%	9%
Go about selecting bank for business: prepared to open an account for me	36%	14%
Transaction use in business: debit card	35%	13%
Transaction use in business: mortgage bond	10%	0%
Go about selecting bank for business: offered the best rates	32%	14%
Money transfers between bank accounts: via a cell phone	9%	1%
Average time spend travelling to and from bank: between 11-20 minutes	55%	35%

Transaction use in business: an overdraft	8%	1%
Account payments to someone else: via a cell phone	7%	0%
Have loans for your business: yes	6%	1%
Way like bank- to communicate with you in future: by post	58%	43%

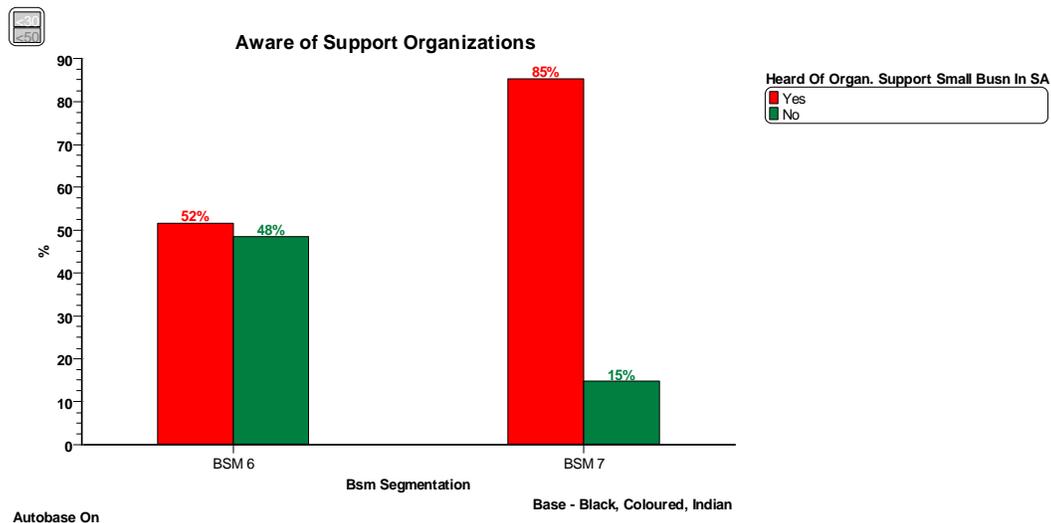
### 6.12 Insurance

BSM 7 are far more likely to have their businesses covered by insurance and to employ the services of a broker than BSM 6:

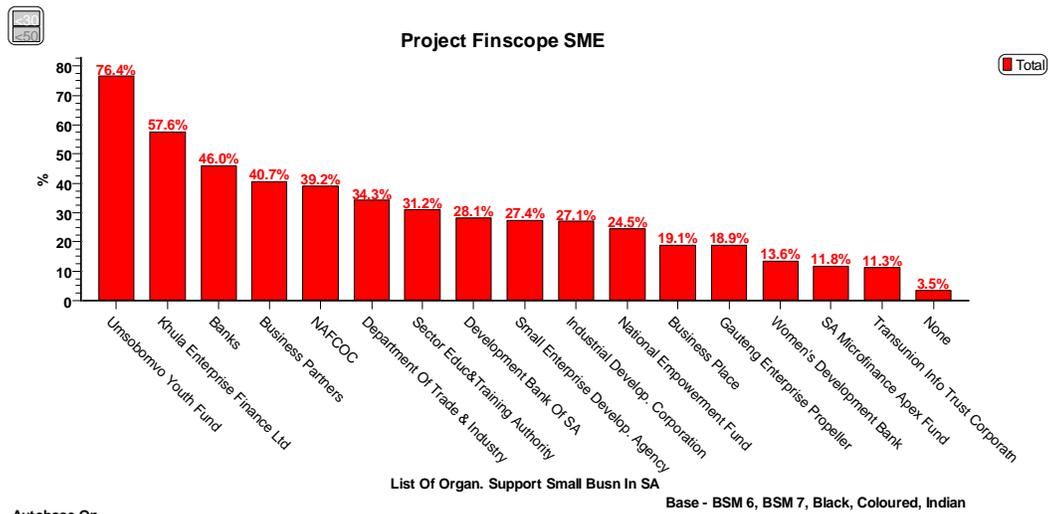
CLIENTS STATEMENTS	BSM 7	BSM 6
Types of insurance business pay: medical aid	38%	3%
Types of insurance business pay: property insurance	40%	4%
Types of insurance business pay: office equipment insurance	23%	0%
Types of insurance business pay: motor vehicle insurance	44%	14%
Types of insurance business pay: pension/provident fund	21%	4%
Types of insurance business pay: professional indemnity	10%	0%
Types of insurance business pay: legal insurance	23%	7%
Use of insurance broker for business insurance: yes	41%	
Types of insurance business pay: workman's compensation	9%	0%

### 6.13 Support for business

BSM target individuals are far more aware of support organisations for business than their counterparts in BSM 6. The BSM groups lower than 6 have considerably lower awareness:



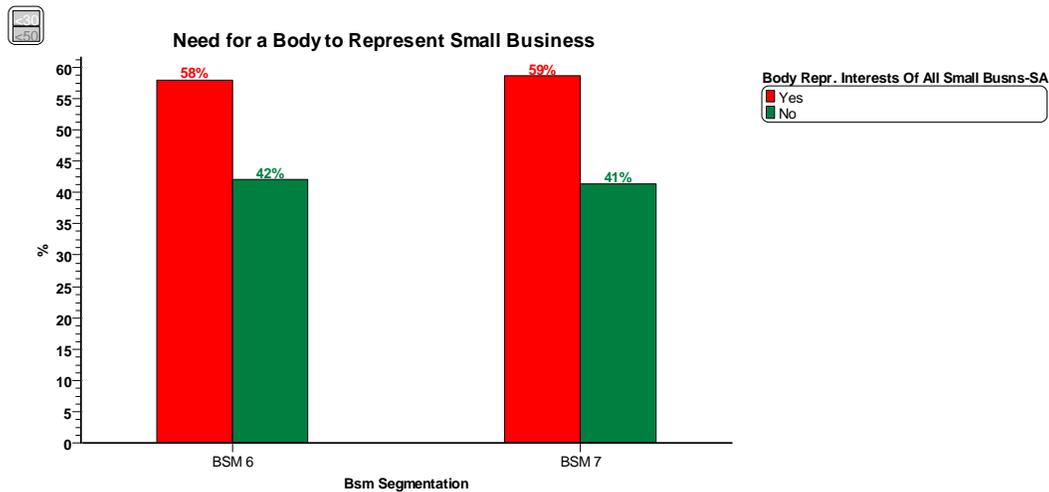
In terms of awareness of support organisations, the following are the awareness patterns (by those who said they are aware of any).



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#### 6.14 Need for a body to represent small business

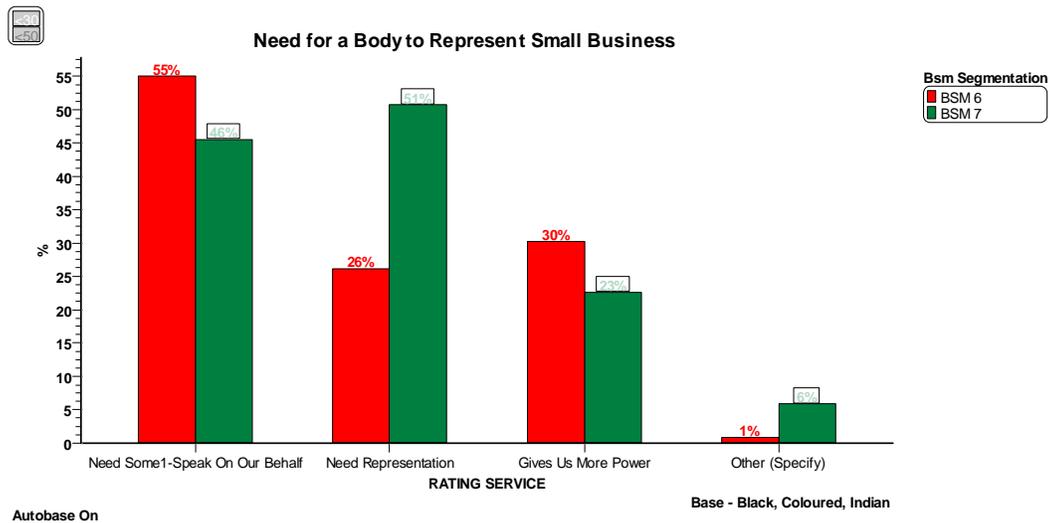
While the business owners do recognise a need for a body to represent small businesses, there is not overwhelming awareness that need.



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Base - Black, Coloured, Indian

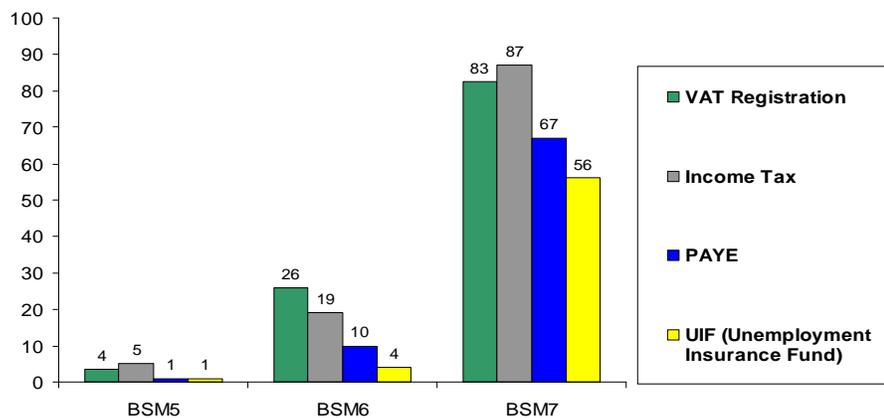
BSM 6 has some solid views on why there should be a body to represent business, the response rate in BSM was low and the percentages unreliable.



### 6.15 Laws, regulations and compliance

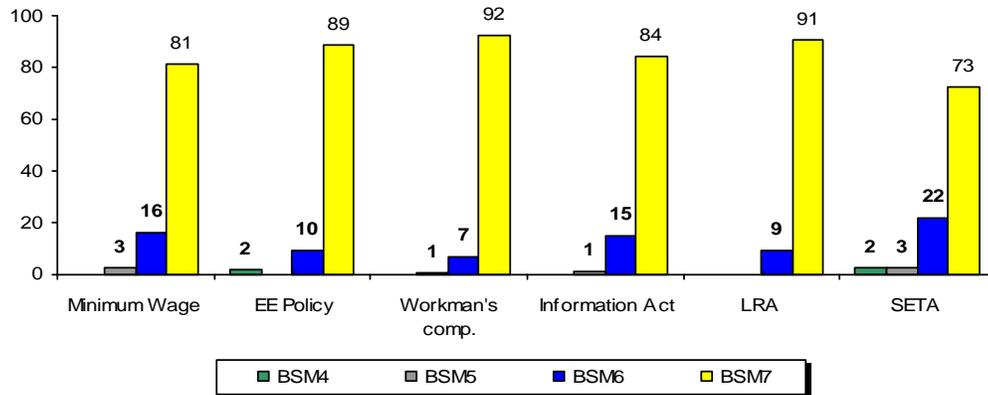
There are significant differences between BSM 6 and 7 when it comes to compliance.

LAWS / REGULATIONS & COMPLIANCE	BSM 7	BSM 6
Company Payments- Income Tax: Yes	80%	13%
Company Payments-PAYE: Yes	65%	9%
Registered For Vat: Yes	84%	27%
Company Payments-UIF: Yes	47%	3%
Comply With-Employment Equity Act: Yes	39%	5%
Comply With-Access To Info. Act: Yes	37%	7%
Comply With-Labour Relations Act: Yes	34%	6%
Comply With-Minimum Wage: Yes	39%	10%
Comply With-Return Of Earnings: Yes	26%	3%
Company Payments-SDL: Yes	21%	4%
Comply With-SETA: Yes	15%	5%



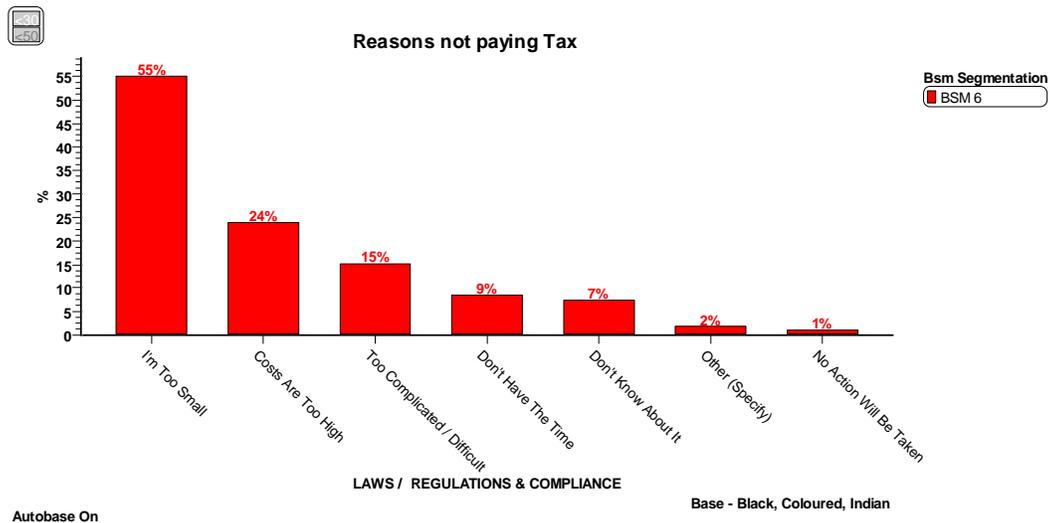
VAT registration starts in BSM 5. Lack of time and size of business are the primary reasons for non compliance.

VAT registration is compulsory for businesses with a turnover of more than R300 000 per annum. Ten per cent of small business have a turnover of R300 000+ and have formally registered their business. Seven out of these 10 have registered for VAT.

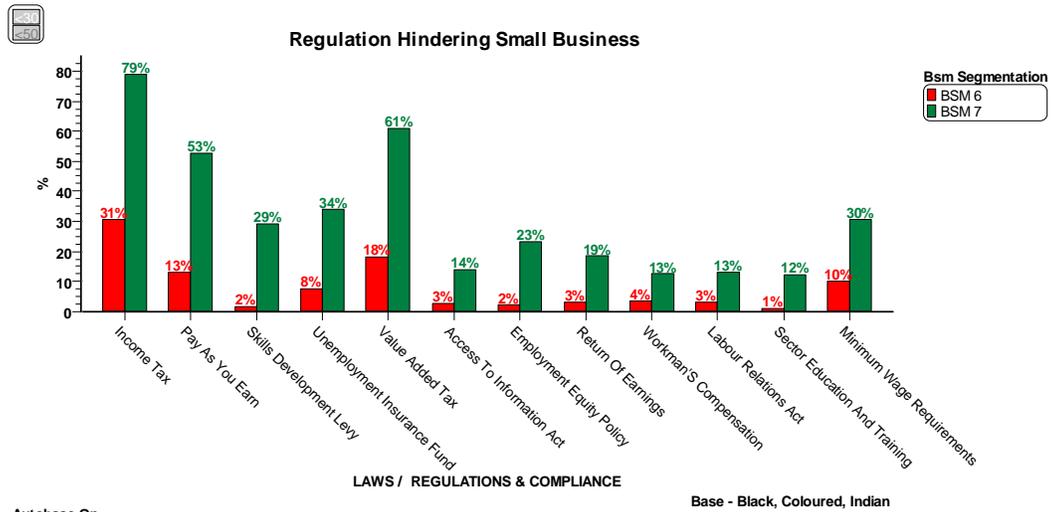


Regulations felt to most hinder business development are income tax (25%) and VAT (16%).

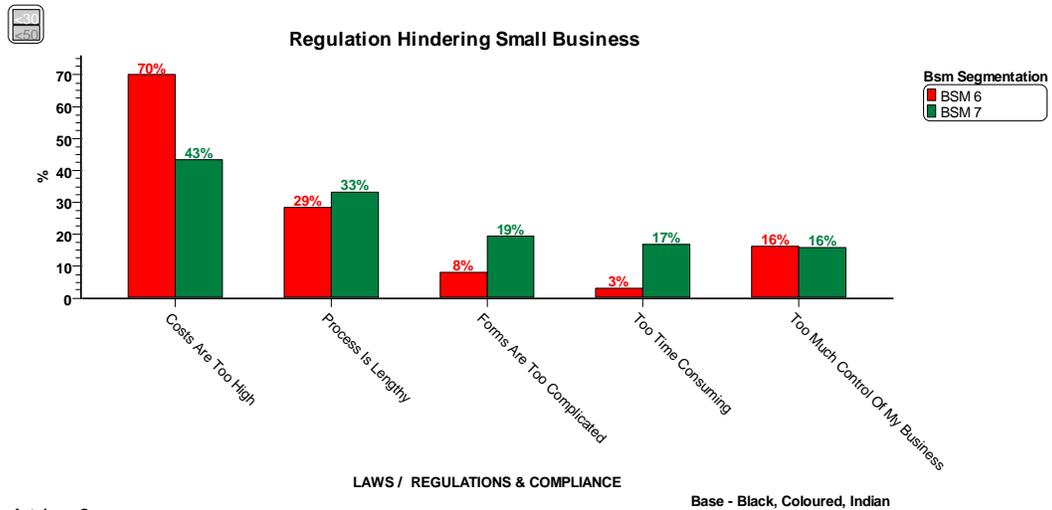
While BSM 7 complies, the reasons for BSM 6 not to comply are as follows:



Regulation is seen to be hindering small business by both BSM 6 and 7 and the compliance regulations most often mentioned are:



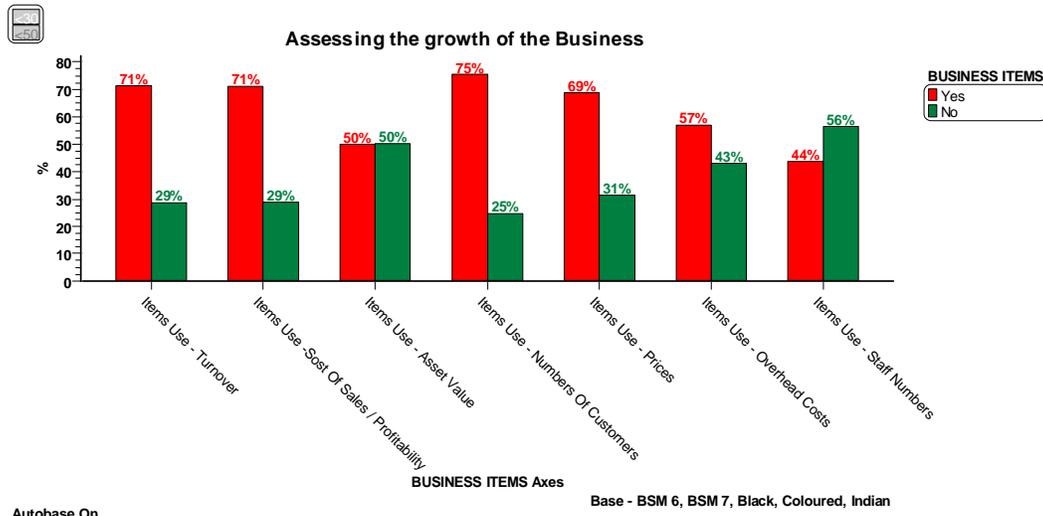
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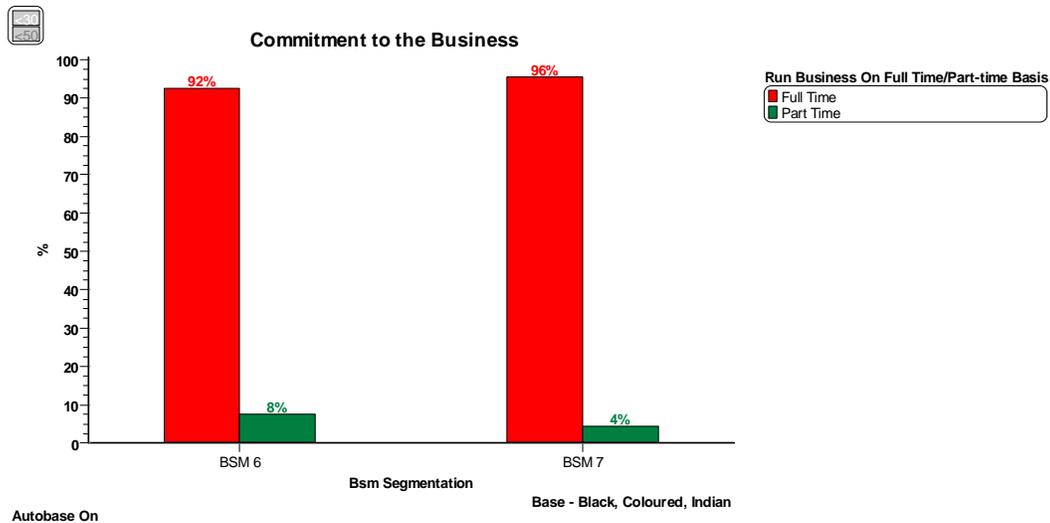
### 6.16 Measuring the growth of business

The ways in which business owners assess the growth of their businesses are varied but generally they rely on turnover, the profitability and growth in customer base. It is unclear what businesses owners meant when they used 'prices' as a measure of growth.



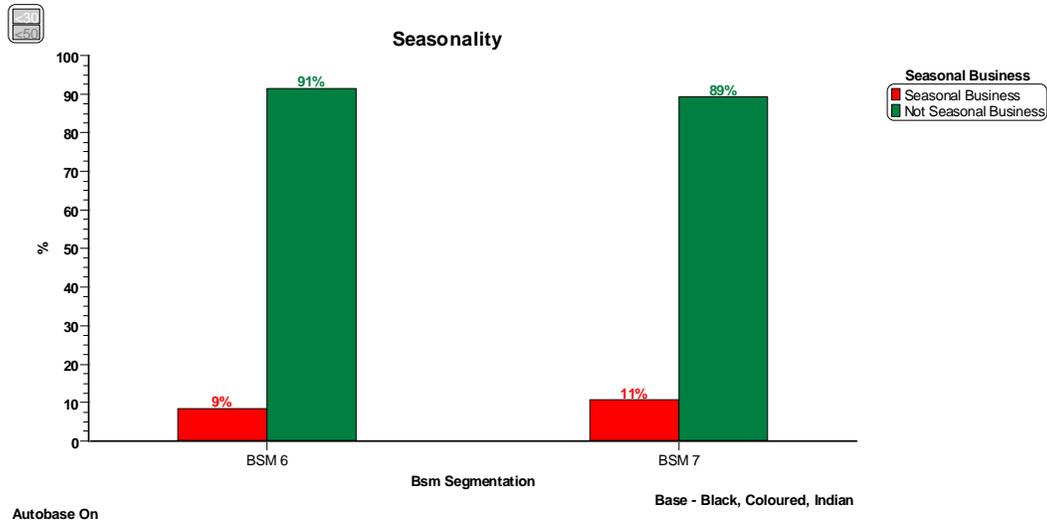
### 6.17 Commitment to the business

The majority of business owners in BSM 6 and 7 run the businesses on a full-time basis.



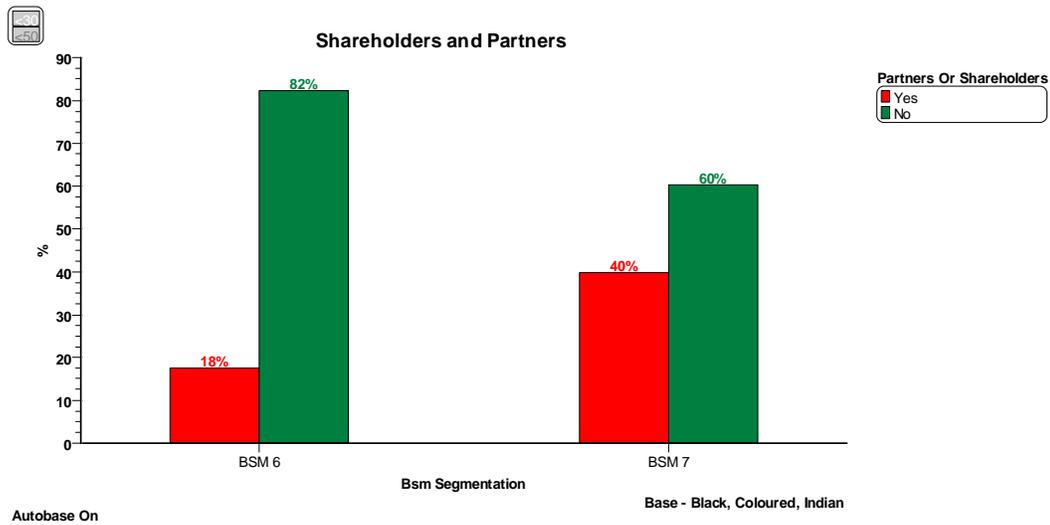
### 6.18 Seasonality

Little seasonality was found in businesses in Gauteng, largely due to the fact that the province is mainly urban (not rural) and not agriculture based. This would not be the case in a national study.



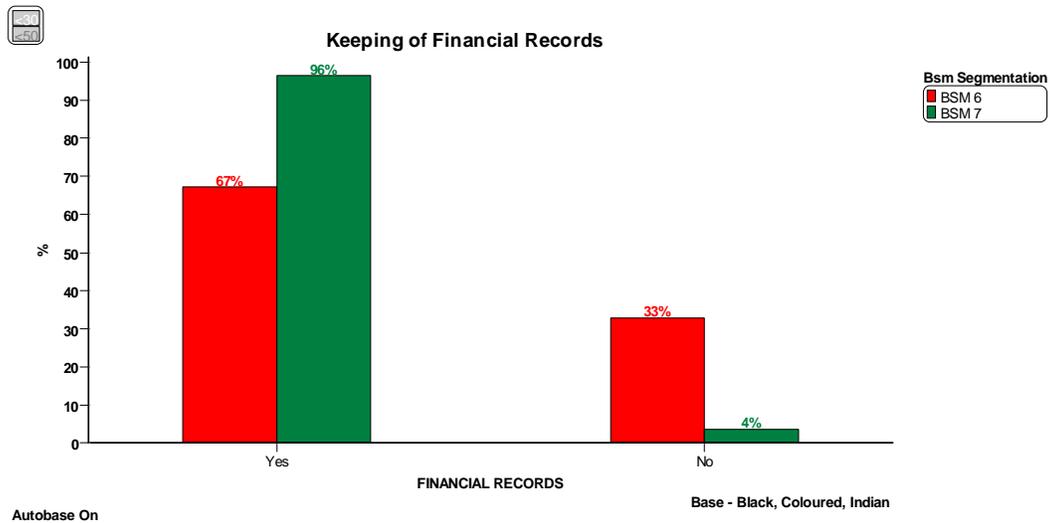
### 6.19 Shareholders and partners

The majority of business owners in BSM 6 and 7 are going it alone without other partners and shareholders.

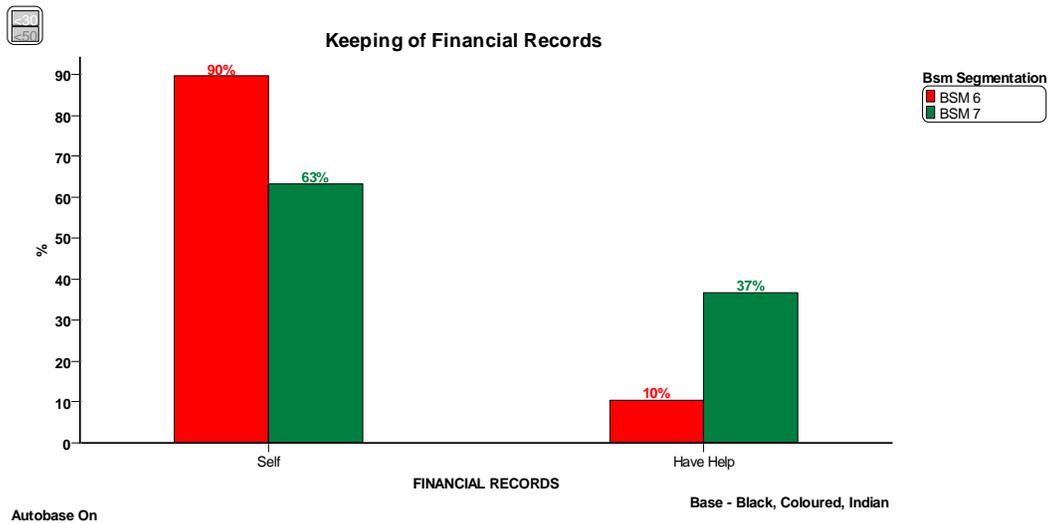


## 6.20 Financial record keeping

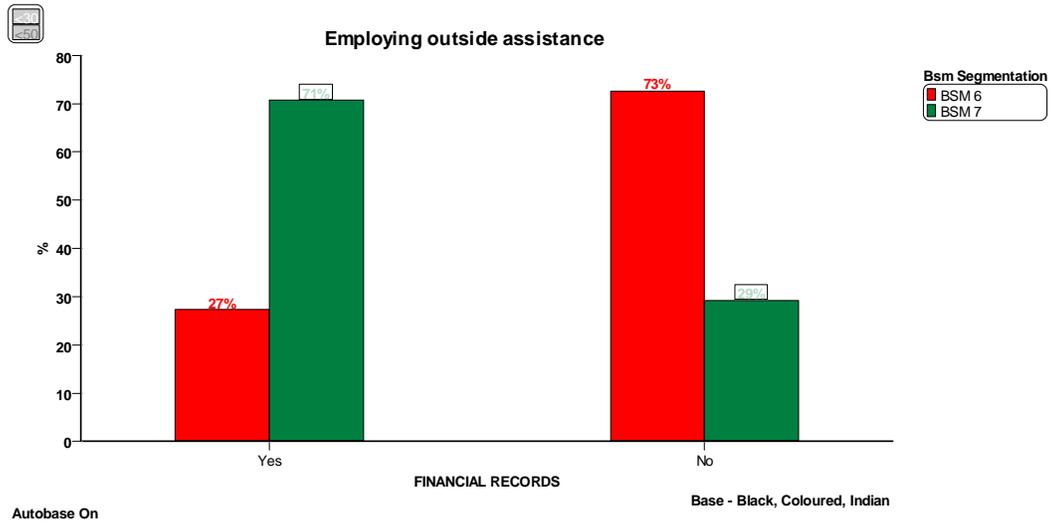
Business owners in BSM 7 tend to be better at keeping financial records than those in BSM 6 by quite a significant margin.



The majority of business owners in the target groups keep the records themselves with a skew towards BSM 6.

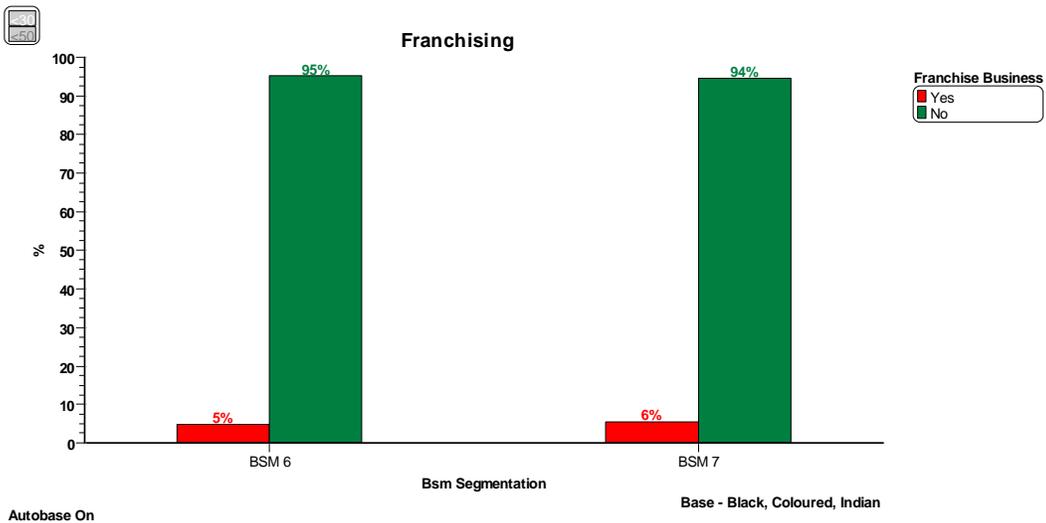


Those claiming to use outside help skews towards BSM 7 however the base sizes are small and therefore the percentage figures are somewhat unreliable.



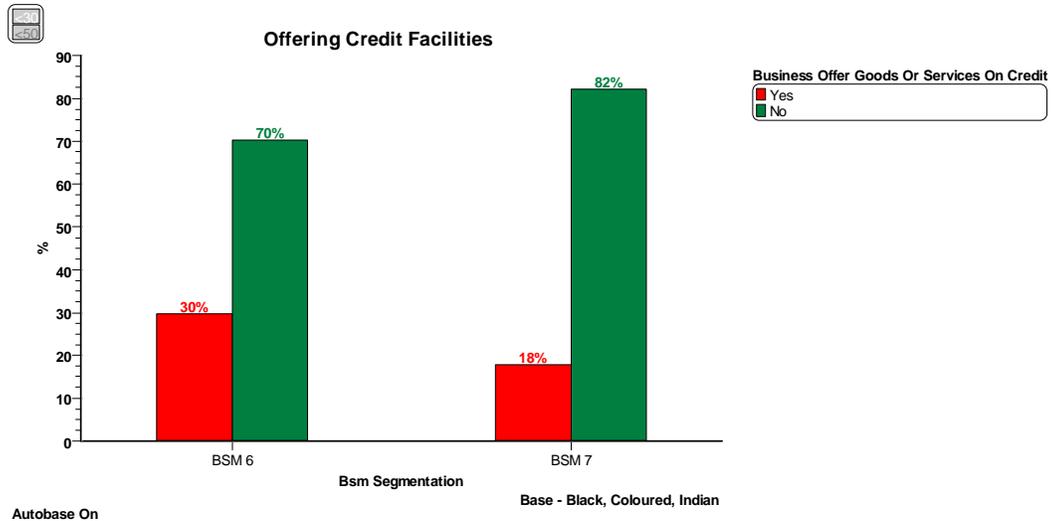
### 6.21 Franchising

The majority of businesses in the target BSM 6 and 7 groups are not franchised operations.



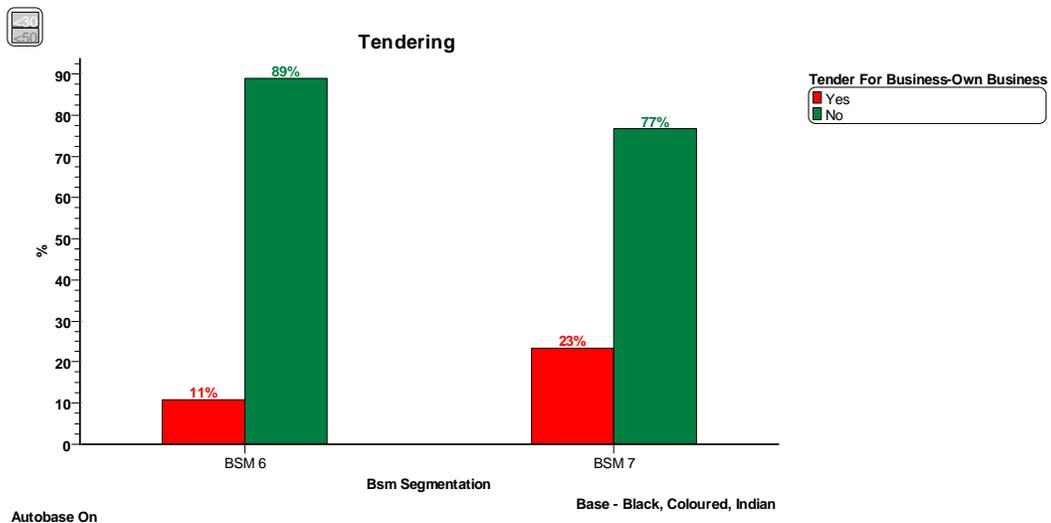
### 6.22 Offering credit facilities

The majority of businesses in the BSM 6 and 7 target group do not offer credit facilities to their customers due largely to the fragile nature of the overall funding structure of the businesses.

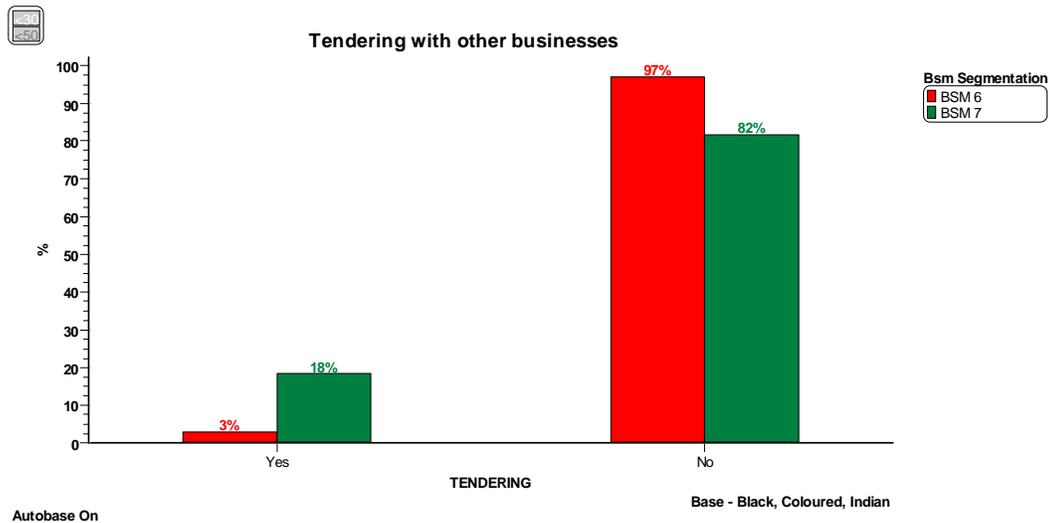


### 6.23 Tendering

The majority of businesses in the target group do not tender for business on their own although tendering is more prevalent in BSM 7 than in 6.



Neither do they tender in conjunction with other businesses.



#### 6.24 Attitudes towards Business

In 2006 the attitudes toward business by the target group were buoyant. The economic climate in the country has changed considerably from then, however it is worth exploring the psychographic mindset of the target group:

From the battery of attitudinal variables offered to respondents regarding their perceptions of their business and what they had done during the past year, the follow were the most significant differences between BSM 7 and BSM 6:

CURRENT ATTITUDES TO BUSINESS	BSM 7	BSM 6
Upgraded computer	21%	0%
Did business over the internet	20%	0%
Real growth in turnover	46%	16%
Did staff training	19%	2%
Showed increased profits	37%	13%
Launched/developed new products	25%	6%
Increased number of staff	28%	9%
Too many government regulations	24%	8%
Too many levies and taxes	14%	4%
Best description of business - currently: growing	79%	62%

Clearly, the level of sophistication and the activities under taken in BSM 6 contribute to the overall significant differentiator of the business currently growing. Activities such as staff training and launching new products contribute to the overall success and wellbeing of the businesses.

Again, identifying the significant differences between BSM 7 and 6 in terms of the management of their businesses, it is clear that BSM 7 is more inclined to address important control and management tools within their businesses than BSM 6.

<b>PROFESSIONAL SERVICES AND ASSISTANCE</b>	<b>BSM 7</b>	<b>BSM 6</b>
Handled By An Existing Staff Member: Accounting / Book-Keeper	50%	7%
Handled By An Existing Staff Member: Customer Management	48%	11%
Handled By An Existing Staff Member: Secretarial	30%	2%
Handled By An Existing Staff Member :IT / Computer	48%	11%
Handled By An Existing Staff Member: Legal Services	34%	4%
Handled By An Existing Staff Member: Public Relations	34%	5%
Handled By An Existing Staff Member: Marketing And Sales	42%	9%
Handled By An Existing Staff Member: Human Resources / Personnel	22%	1%
Gov Assistance Programmes from Professional Service: Yes	57%	28%
Handled By An Existing Staff Member: Debt Management	15%	2%
Mentor Or Advisor In Business: Yes	38%	18%
Brought In-Part-time/Contract Basis: Accounting / Book-Keeper	26%	0%
Used Government Assistance Programmes: Yes	35%	10%
Bring In On A Part-time/Contract Basis: Legal Services	16%	5%
Bring In On A Part-time/Contract Basis: Customer Management	12%	3%
Bring In On A Part-time/Contract Basis: Marketing And Sales	15%	5%

It is significant that the reason for not contracting the above services is that BSM 6 believes that they have the skills to perform these tasks themselves.

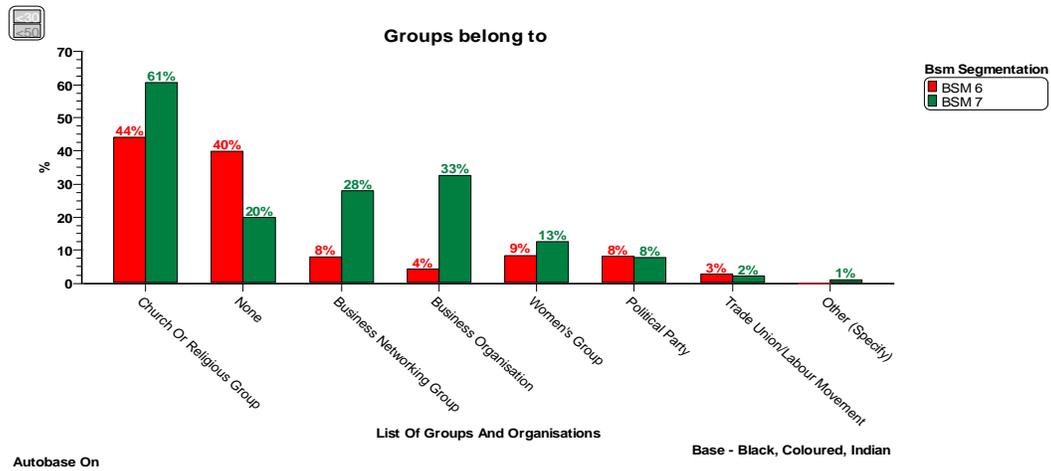
Reasons Not Contracting In Any Of These Service: Have The Skills In-house		15%
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#### 6.25 Other Business Attitudes

<b>ATTITUDES &amp; BELIEFS &amp; THINKING AHEAD</b>	<b>BSM 7</b>	<b>BSM 6</b>
Take advantage of opportunities offered by networking / use my contacts	57%	11%
Future objectives: improve computer skills	36%	10%
Not necessary to repay a government loan: agree a little	31%	9%
Future objectives: advertise	67%	44%
Have less time for personal life: disagree	52%	33%
Need to take greater risks: disagree	33%	17%
Need to have further training and development: agree a little	42%	24%
Future objectives: outsource labour	17%	6%
Don't have same opportunities as others: disagree	51%	34%
Factors contributing to success of business: reserve funds for emergencies	21%	9%
Government programmes for small business not working: disagree	31%	16%
Have plans for business to take advantage of 2010 world cup: yes	59%	42%
Things need to do to take advantage of opportunities offered by 2010: develop new products & services	45%	22%
Factors contributing to success of business: good staff	39%	25%
If offered a formal job would take it: disagree	51%	35%
Crime is serious threat to business: don't know	6%	0%
Things need to do to take advantage of opportunities offered by 2010: revise my business strategy	38%	17%

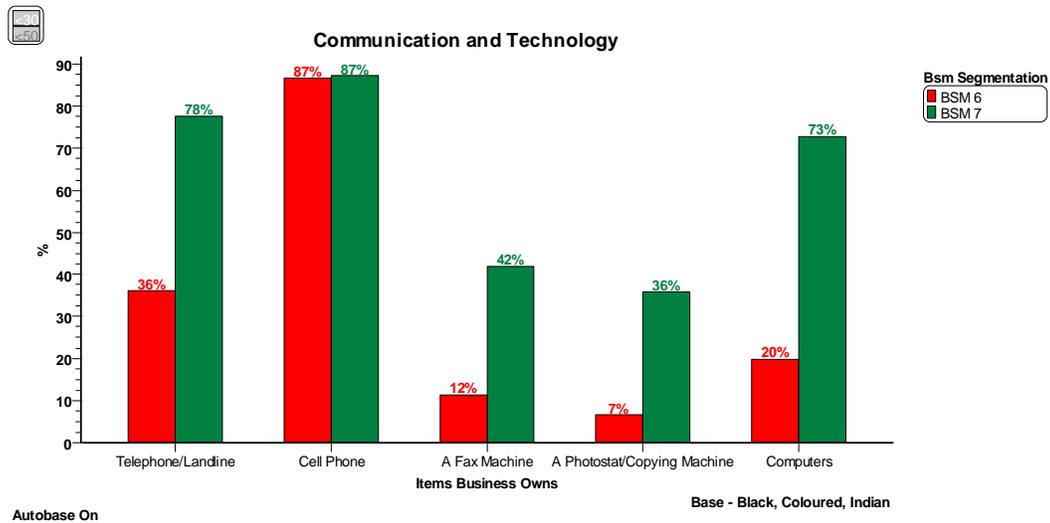
## 6.26 Networking

BSM 7 has a better developed network which could be a contributing factor to the success of these businesses.



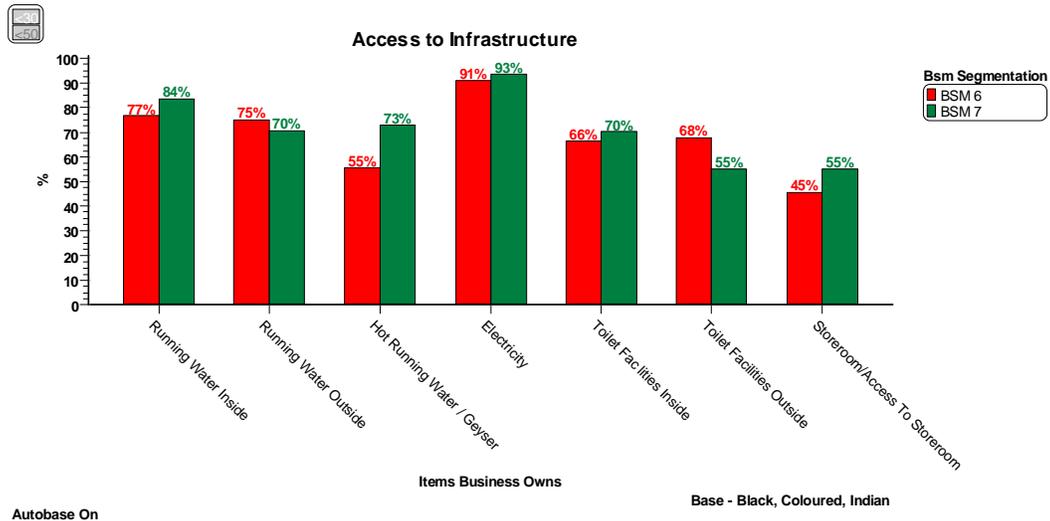
## 6.27 Communication

BSM 7 target group has better access to landline telephones however the penetration of mobile phones is very much on a par. BSM 6 lags behind BSM 7 in terms of access to other communication technology.



## 6.28 Access to infrastructure

Access to basic needs is not a major issue in either BSM 6 or 7.



## 6.29 Business items

BSM 7 is significantly different from BSM 6 in terms of the development of some of the more sophisticated and necessary business tools and processes. Importantly, BSM 7 has written plans, keeps records of financial activity and uses internet technology.

Items Business Have	BSM 7	BSM 6
Internet Access	49%	5%
An Email Address	49%	5%
A Vision Or Mission Statement	34%	2%
Credit Card Machine	29%	0%
A Written Business Strategy	48%	9%
Security System	37%	4%
Up To Date Financial Records	42%	8%
A Website	21%	0%
A Written Business Plan	55%	18%
A Written Marketing Plan	34%	5%
Own Network (LAN) & Server Room	18%	0%
Staff Access Control	19%	1%
An Executive Dining Room	14%	0%
A Canteen Or Dining Room	17%	2%
A Business Budget	55%	31%
Switch Board	12%	2%
A Formal Training Program	23%	8%

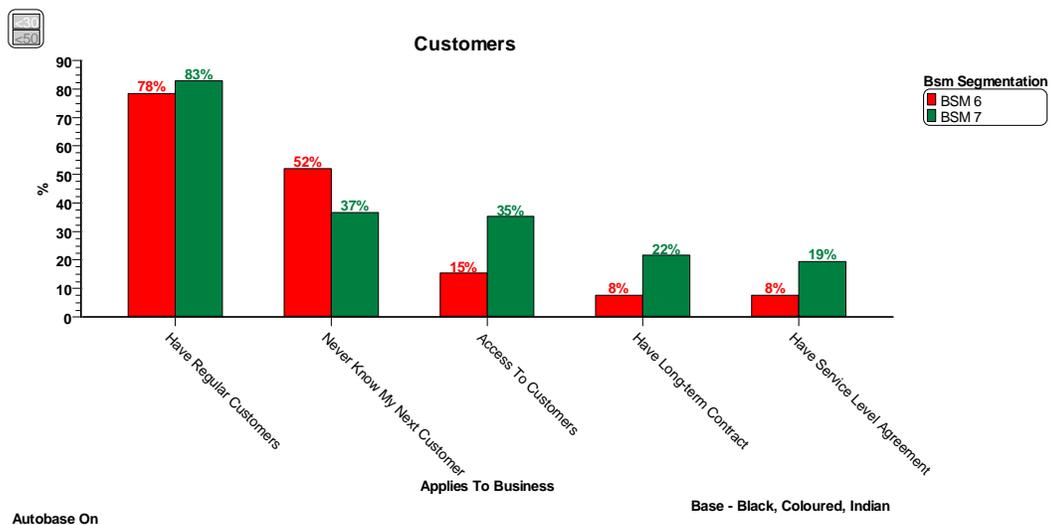
### 6.30 Attitudes to re-investing

In addition to the above levels of sophistication of the businesses, the significant differences between BSM 7 and 6 in terms of profit re-investment are that BSM 7 is more likely to consider re-investing profits in the business than BSM 6 ó albeit that some do withdraw all the profit in both groups.

	BSM 7	BSM 6
Measure/Monitor Growth Of Business: Yes	95%	73%
Re-invest Some Of Profits: Yes	92%	75%
Withdraw All The Profits: Yes	37%	19%

### 6.31 Customers

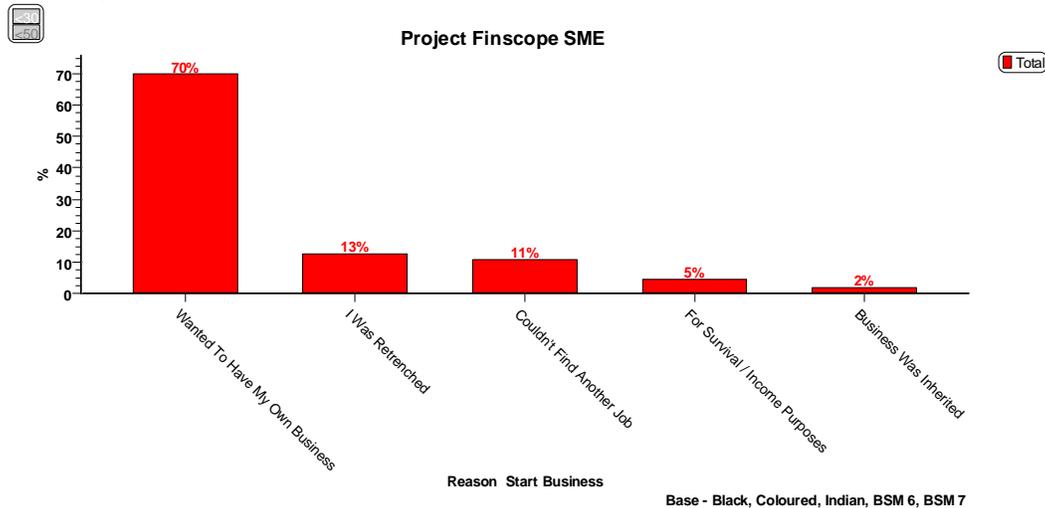
Perhaps because of the access to and use of more sophisticated planning and business tools, BSM 7 tends to have a more solid relationship with clients, providing a more stable business base:



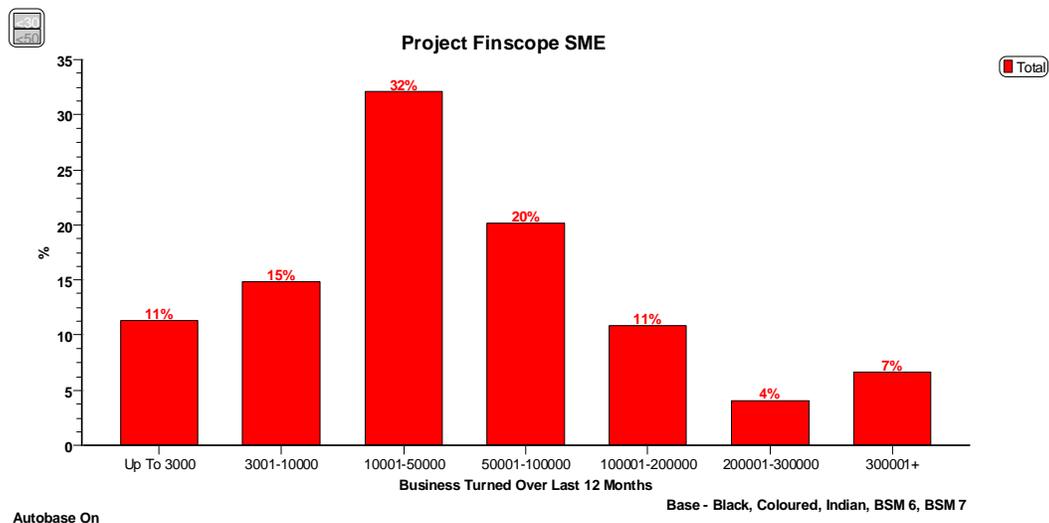
## 7. Summary and Conclusion

The FinScope survey showed that there are an estimated 109 000 previously disadvantaged individuals in BSM 6 and 7 in the province of Gauteng who own and run their own businesses.

Unlike the 'lower' BSM groups, the target segment started their own businesses because they have always wanted to run their own business rather than through necessity:



One of the major drawbacks to interest in and the overall development of the small business sector as a whole has been the size of the businesses. The declared turnover of the HDI businesses in BSM 6 and 7 in the last 12 months is not particularly high with only 7% declaring income of over R300 000 while 78% declared income under R100 000:

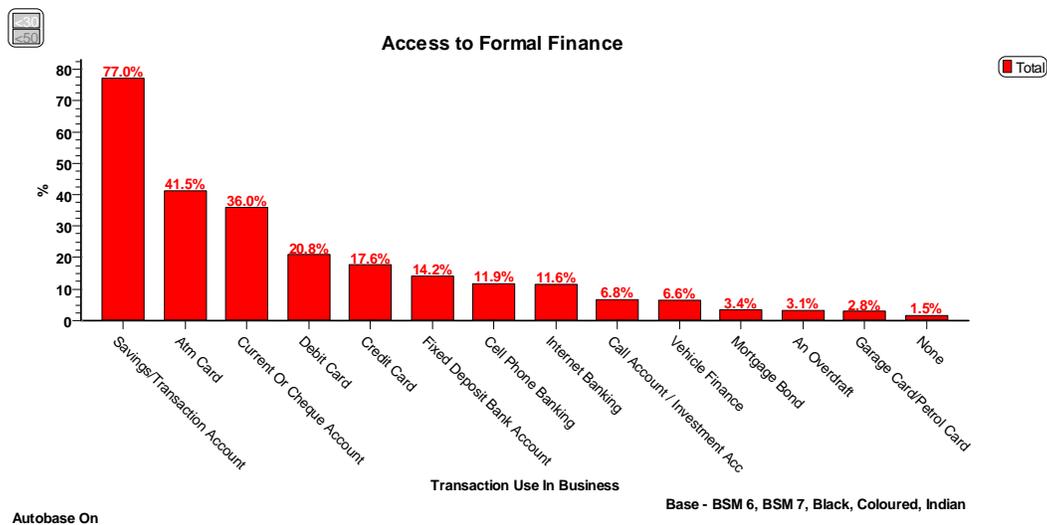


The majority of HDI individuals in BSM 6 and 7 have either a personal bank account or a business bank account or even both of these however only 2% of this group claimed to have a loan.

The fact that only 2% claim to have a loan means that the base sizes in this survey are very small and the analysis of the reasons for not having a loan should rather be handled in the qualitative focus group work. Having said this, the lack of financial record keeping on the part of the business owners does complicate matters from a formal financial institution's perspective in the ability to access the viability of the business and the soundness of the loan repayment.

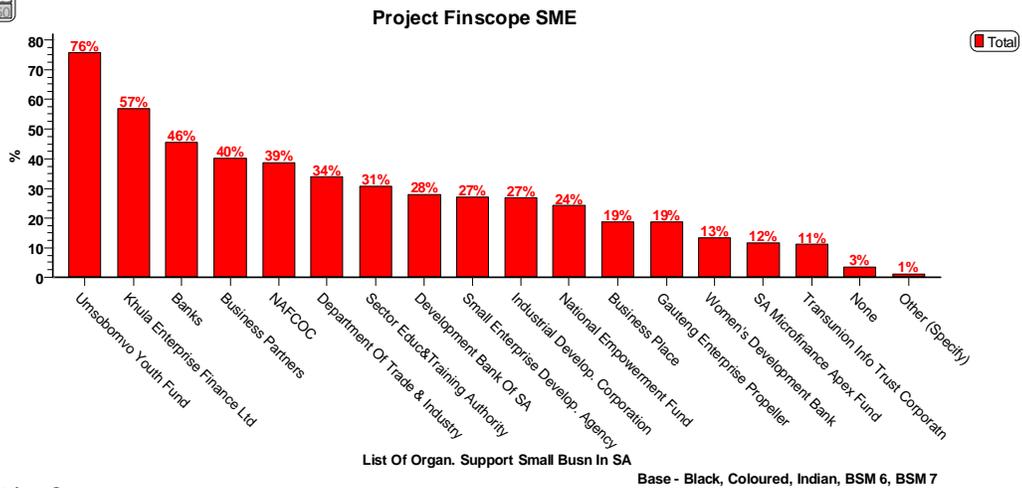
The approach to the market by financial institutions needs to change and a better understanding of the needs and challenges faced by small business obtained. Innovation in terms of product offering and revised credit scoring approaches needs to be developed ó this will not be helped by the stringent controls placed on banks by the new Credit Act.

The savings account has the highest level of penetration of all financial product options available, with only around a third having a cheque account.



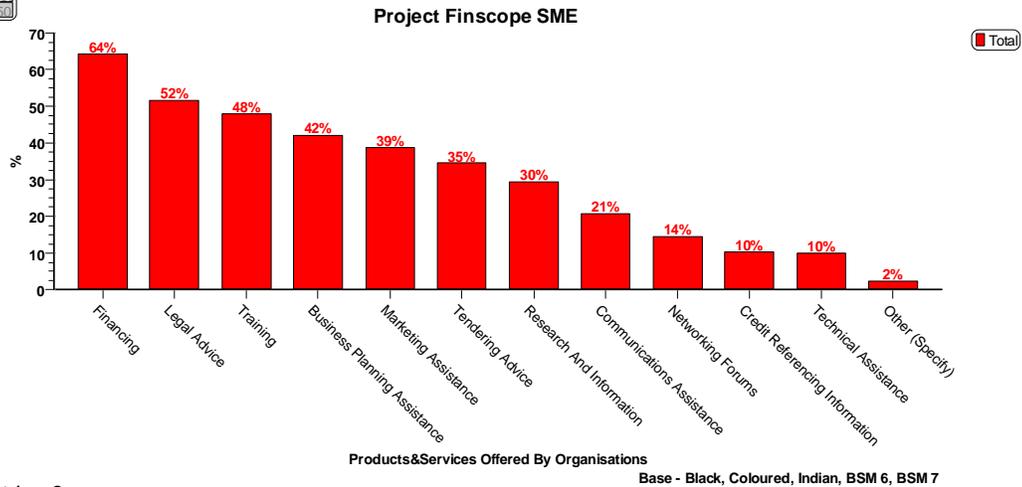
The survey showed that the business owners experience numerous problems when starting out and access to finance is a significant obstacle.

In terms of support for small business, there is significant awareness of institutions established to support small businesses.



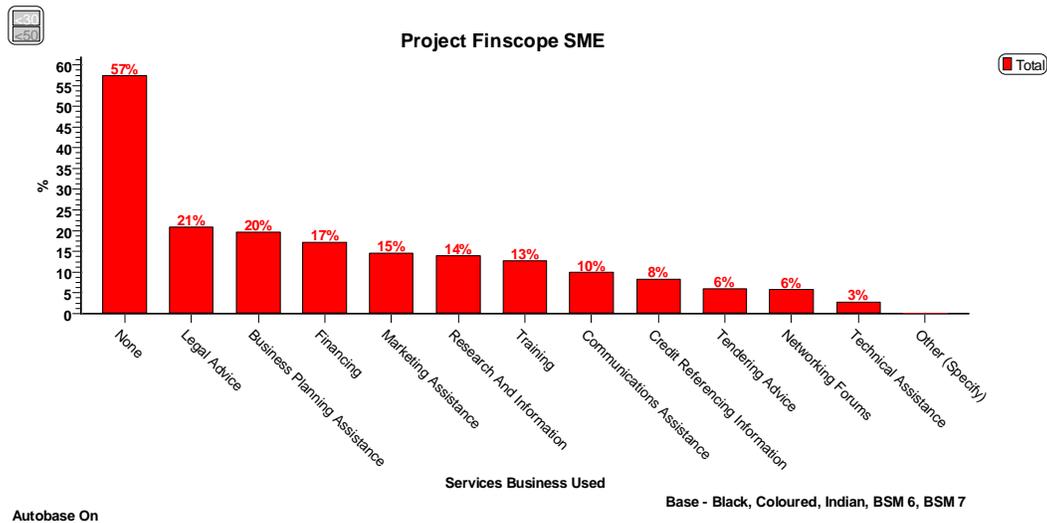
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The awareness of products offered by these institutions is also significant with finance being top-of-mind.



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The usage of these services does not match the awareness with 57% claiming never to have used the services.

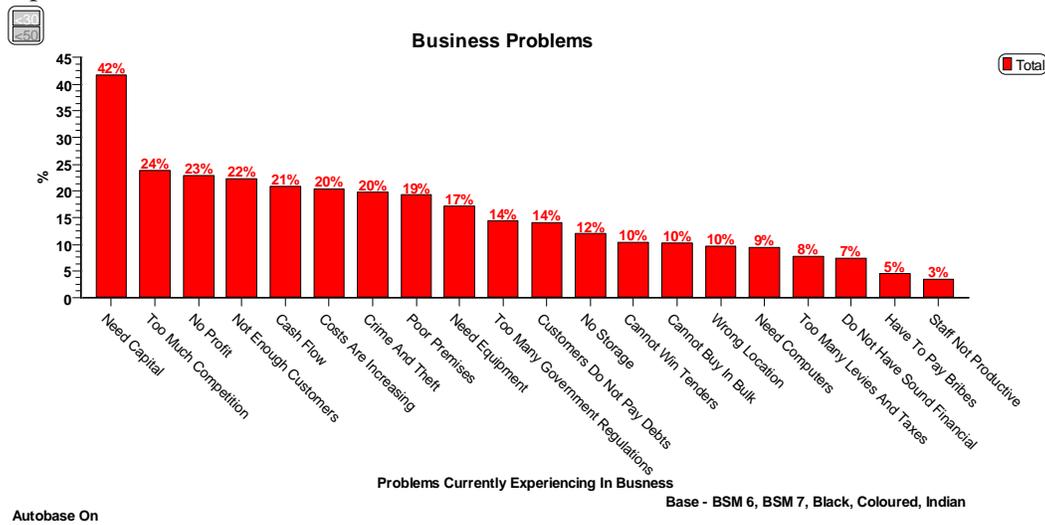


Clearly there is a need for the business support institutions to segment the small business market and to individually structure their approach to the market to become more relevant and effective within their defined segment, rather than all having a catch all approach.

The importance of the small business sector to the growth of the economy overall will be significant if this sector can be further developed as a sustainable and vibrant market. Much has been done up to now but there is clearly need for improvement. The policy framework within which the businesses operate needs up-dating, financial institutions need to become more innovative in this segment and the level of skill within the segment needs to be improved.

In many instances the personal bank account is used in preference to opening a business account and the reasons why HDI businesses use their personal accounts are largely for reasons like: their business is too small, or they don't need a special business account, it's too complicated to open a business account, the costs are too high, their business and personal affairs are one and the same or that they simply haven't registered the business. In many cases the financial institutions could overcome these attitudes via more selective marketing and targeting of businesses that show greatest potential.

The overwhelming problem faced by businesses in the target category is the need for capital.



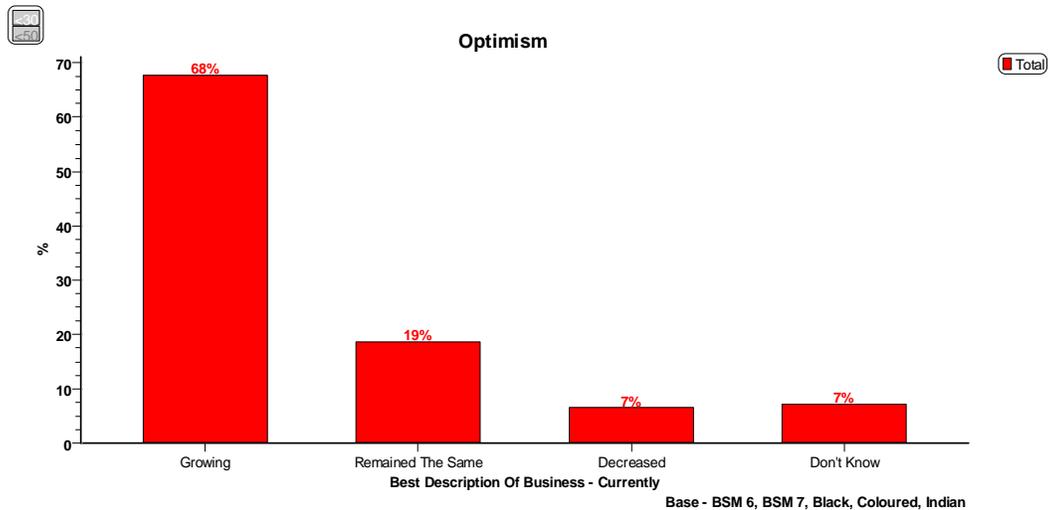
The chief challenge going forward is to devise plans that will assist the growth businesses to capitalize their businesses. There needs to be innovative thinking around:

- the creation of partnerships with investors
- capital provision linked to mentorship in company
- government subsidies
- tax relief on money ploughed back to capital projects
- low cost/low hassle loans

This is not an easy solution when the levels of financial literacy, education in general and levels of business sophistication and governance remain at low levels.

The institutions that have been established by Government departments are not functioning properly because they are not focussed enough or single minded in their approaches. GEP for example states that their mandate is to "help everybody in business". These are noble ideas but totally impractical to implement. Each support institution needs to define what it does best, who its chief targets should be and go for these, ignoring the rest and leaving them to other, better focussed institutions.

Despite the obstacles out there it is remarkable to observe the optimism of small business in Gauteng. Nearly 70% said that their businesses were growing.



The lack of sophistication of the target market in general points to the need for business education and financial literacy to be placed high on the development agenda.

The relatively small numbers of businesses that are of significance and their wide distribution across the province linked with their general lack of visibility in the market place means that they will be difficult to find and work with. What will be important going forward is a strategy that brings the businesses to the institution set up to provide assistance rather than that institution going out after the market.

It is important for AfricaScope to interface with USAID in order understand the organizational framework which is to be followed going forward in order to optimise the effectiveness and impact against the target audience.