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**BLACK ECONOMIC EMPOWERMENT:
SECTORAL ANALYSIS**

Final Report

U.S. Agency for International Development

Prepared for: USAID/South Africa and AFR/SD/PSGE
Prepared by: J.E. Austin Associates, Inc.
Sponsored by: Private Enterprise Development
Support Project III
Contract No. PCE-0026-Q-00-3031-00
Delivery Order No. 16
Prime Contractor: Coopers & Lybrand, LLP

June 1995

**Coopers
& Lybrand**

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ABBREVIATIONS

BMR	Bureau of Market Research
CSS	Central Statistical Service
DBSA	Development Bank of Southern Africa
DRA	Development Research Africa
GDP	Gross Domestic Product
NAFCOC	National African Federation of Chambers of Commerce
OHS	October Household Survey
PSLSD	Project for Statistics on Living Standards and Development
RDP	Reconstruction and Development Programme
SAARF	South African Advertising Research Foundation
SALDRU	Southern Africa Labour and Development Research Unit
SARB	South African Reserve Bank
TBVC	Former independent states Transkei, Bophuthatswana, Venda, and Ciskei
UNDP	United Nations Development Programme

1. INTRODUCTION

1.1 Background to the research

The United States Agency for International Development (USAID) is developing a strategy for a program to assist the development of the private sector of South Africa. The objective of the program is to increase the economic participation of previously disadvantaged groups in South Africa. BMI was asked to perform the necessary research in order to provide USAID a foundation for the strategy. The present study is one part of that research effort which also included a comprehensive annotated bibliography and a benchmark study.

1.2 Objectives of the Research

The objectives of this study are to:

- Identify sectors with high potential for expanding black economic participation;
- Identify constraints to growth that are general to the economy or target group as well as constraints that are specific to the sectors identified; and
- Identify useful interventions to mitigate these constraints.

The study attempts to identify those sectors or subsectors of the economy which hold the most potential for expansion and which have the highest propensity to increase participation in ownership, management and employment for the formerly disadvantaged. The research was based on available sources of economic and social data, as well as the opinion of a number of South Africans, who are considered knowledgeable in their respective fields.

1.3 Methodology

The research was conducted by gathering the available data on the different sectors in the economy. Subsequently the data was analysed by applying certain criteria to identify attractive sectors. These criteria were:

- The importance of the sector in the economy;
- The prospects for future growth of the sector;
- The extent to which blacks were represented in those sectors; and
- The ease of entry for both formal and informal activities.

A group of experts in small and medium business in South Africa contributed by reviewing the data and providing additional data. Subsequently constraints to growth in the target sectors and useful interventions to eliminate these constraints were identified with the help of previous studies. These constraints include those which are general to the economy or specific to the previously disadvantaged groups.

1.4 Limitations to the study

A major limitation to the study is the poor statistical base of quantitative data in South Africa. Institutions have very poor data sources, and the data that exists is often inaccurate or out of date.

Another limitation to the study is the fact that, due to the dramatic political transformation and the consequent re-entering of South Africa into the international community, past trends can hardly be extrapolated to the future.

It should further be acknowledged that a macroeconomic approach in identifying potential growth sectors will obscure the potential of certain subsectors within the broader sector. For instance, within a high-growth sector certain low performance subsectors will occur, and vice versa.

1.5 Organisation of the Report

Chapter 2 discusses the ways in which the previously disadvantaged population can be empowered economically. It further discusses the general constraints to black empowerment.

In *chapter 3* the structure of the economy is discussed whereafter a number of general constraints to growth of the economy are treated. Subsequently a number of interventions to counter these constraints are suggested.

Chapter 4 presents the actual sectoral analysis which identifies high potential subsectors for further analysis. These are:

- the manufacturing sector, discussed in *chapter 5*;
- the building and construction sector, discussed in *chapter 6*;
- finance and business services, discussed in *chapter 7*; and
- tourism-related sectors and trade, discussed in *chapter 8*.

2 BLACK ECONOMIC EMPOWERMENT

2.1 Fostering Economic Empowerment

The ideology of apartheid systematically excluded blacks not only from political power but also from wealth creating economic activities. As the legislative barriers to political and economic participation have fallen away, the issue of economic empowerment has begun receiving the attention it deserves. The decline of the South African economy in the past decades forms a serious constraint to the process of empowerment. The official unemployment rate is 41.1 per cent for the black population. These circumstances exacerbate the difficulties associated with bringing blacks into the mainstream economy, even though the legislative barriers have been removed.

Fostering black economic empowerment can take many forms and encompasses the following (Sidiropoulos, 1993):

- development of black business in the formal economy beyond the trade and service sector;
- stimulation of informal sector activities such as micro-enterprises;
- acquisition of equity resulting in an increased interest in preserving economic and political stability; and
- empowerment in the work place in the following areas:
 - advancement through affirmative action,
 - democratisation at the various levels in the organisation through participation, employee share ownership of profit-sharing schemes,
 - improvement of education and training opportunities, and
 - corporate social responsibility programmes; and
- growth of the spending power of black consumers.

2.2 Constraints to Black Economic Empowerment

The most obvious constraints to black economic empowerment are the effects of apartheid legislation. The principal measures under the apartheid regime that hindered black economic advancement were (Sidiropoulos, 1993):

- The Black Land Act of 1913 and the Development Trust and Land Act of 1936, prohibiting blacks from acquiring land outside designated areas;
- Blacks Urban Areas Consolidation Act of 1945 and the Blacks Act of 1952, impeding freedom of movement;
- Group Areas Act of 1966, controlling the ownership and occupation of land and premises;

- Labour Relations Act, reserving certain categories of work for certain racial groups (job reservation); and
- Various laws restricting black education.

The effect of these legislative measures was that commercial and industrial development of black business was restricted to the homelands, at least during the worst years of apartheid. Even in the townships blacks were not allowed to establish their own business premises and they could not have more than one business. Blacks could only provide services aimed at the provision of "daily essential domestic requirements" for other blacks. They could not form financial institutions, partnerships, trading companies or wholesale enterprises; trading licenses were granted only to blacks who had taken out homeland citizenship; and manufacturing by blacks was also not permitted.

These constraints have been removed over time, the most recent legislative repeals taking place during the 1991 parliamentary session. Their effects, however, still plague black business. In addition, the system of apartheid left behind other obstacles, which can only be overcome gradually. These include:

- Low education standards at primary and secondary levels;
- Education lacking emphasis on training in practical fields of business and management;
- Lack of managerial and technical training in the current generation of blacks, resulting in a shortage of white-collar workers and skilled manpower;
- Poor communication, co-operation and networking in the black business system, which hampers co-ordination of developments and mutual assistance;
- Reluctance of financial institutions to lend money to blacks, because very few have the required collateral and perceived lack of business acumen;
- A shortage of suitable business premises in black areas; and
- Inadequate infrastructure, such as electricity, water and roads in black areas.

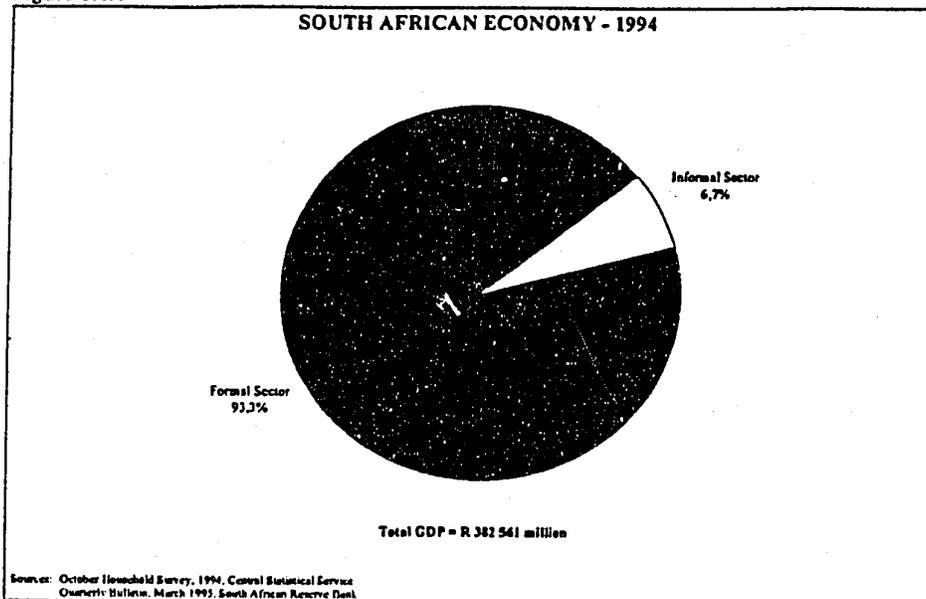
Sidiropoulos (1993) maintains that blacks suffer from personal and psychological disadvantages, mostly as a result of the sense of inferiority imposed on them by the apartheid system. A lack of self-confidence and individualistic assertiveness as well as a culture of entitlement are barriers to empowerment.

3 GENERAL CONSTRAINTS TO ECONOMIC GROWTH

3.1 Structure of the economy

The Gross Domestic Product at constant prices decreased from 1989 to 1993, and only increased by 1 percent during 1993 and by 2.5 percent in 1994 (SARB, 1995). There is no specific sector to which the recent modest growth can be ascribed. The South African Reserve Bank has determined that the Gross Domestic Product at factor cost amounts to R 383,561 million for 1994. The October Household Survey 1994 (CSS) reports contribution of the informal sector to the GDP of 6.7 percent or R 25,744 million for 1994 (figure 3.1.1).

Figure 3.1.1



Almost two million people find employment in the informal sector. This is more than 13.5 percent of the economically active population, and almost a quarter of the people who are active in the formal sector. Given the estimated value of informal sector production in 1994, equivalent to 6.7% of GDP, it can be concluded that marginal contributions to output are much higher in the formal sector. Employment creation in the formal sector can therefore be considered more desirable than in the informal sector. But, as table 3.2.1 shows, the formal private sector as a whole has not contributed to an increase of employment during recent years, with the financial and business services sector as the outstanding exception.

Table 3.2.1 Employment created in the Formal Sector
in terms of average annual employment growth rate and jobs created for selected periods

Sector	Average annual employment growth rate		Number of jobs created
	1970 -1992	1991 - 1992	1980 - 1993
Agriculture, forestry and fishing	-0.9	-1.0	- 141 500
Mining and quarrying	0.8	-7.8	- 144 100
Manufacturing	1.3	-2.5	6 700
Electricity, gas and water	3.2	-4.7	- 800
Construction	0.9	-4.5	2 900
Wholesale, retail, catering and accommodation	1.3	-0.7	21 200
Transport, storage and communication	0.6	-3.5	-129 700
Finance, insurance and business services	4.3	6.1	186 000
Total Private Sector	0.9	-2.9	- 199 300

Source: National Productivity Institute

3.2 Conditions for Economic Growth

The World Bank recently conducted a study, published as *The East Asian Miracle* (Page, 1994). The study focuses on the key determinants of rapid economic growth among the "High Performing Asian Economies" (HPAE). These countries grew at average rates from 1965-1990 of over 5% per year in per-capita terms, much higher than the developed OECD economies, or the Latin American, South Asian, Middle Eastern and African countries. More importantly, this growth was achieved in many, if not all, of these countries while simultaneously improving income equality. There were clearly identifiable sources of this growth:

High levels of savings and investment

Rates of investment for the HPAEs moved from about 20% in 1965 to well above 30% by 1987. Private investment levels reached 20% of GDP--a full 10 percentage points more than private investment in other regions. Macroeconomic stability played a key role in stimulating investment as indicated by very low relative volatility in interest rates and foreign exchange rates.

Investment in Education and Human Capital

Countries with successful economic strategies invested heavily in basic literacy, basic education and human capital and had a focus on primary education.

Productivity Growth From High Internal Competition

Successful countries got additional boosts in productivity by:

- Fostering internal competition;
- Openness to foreign technology, ideas and investment; and
- Building a bank-based financial sector.

Creating an Enabling Environment

An enabling environment can be created through:

- Clear rules;
- Business-Government Communications;
- Combination of Co-operation with Competition; and
- Central Role of Exports.

Sharing the Benefits of Growth

Successful governments did not just passively wait for benefits to trickle down but entered into an explicit or implicit social contract which demonstrated it could deliver tangible benefits to all social classes. These governments invested heavily in ways that assisted the masses to enter into economic life and make productive contributions: infrastructure, education, and health. The implicit social contract was that the government would deliver the goods and people would see visible results in their neighbourhoods: schools, electricity, health services, better roads, water, and educational opportunities for their children. In general, most of the HPAEs were able to achieve relatively good income distribution while also achieving high rates of economic growth.

The World Bank findings are similar to those constraints presented in other USAID/South Africa documentation. The USAID-commissioned DAI/Ebony "Private Sector Strategy" draft of March, 1995 mentions as requisites the following: competitive environment, outward-looking environment, appropriate economic policy, appropriate level of functioning infrastructure, political stability and economic stability.

3.3 Constraints in the South African Environment

If the requisites for rapid and sustained economic growth are clear, it is also clear that South Africa faces some important constraints in most of the areas mentioned in the World Bank review of successful economies.

Low Levels of Savings and Investment

South African rates of savings and investment have been extremely low. Gross savings fell to 16.5 percent in 1992 after having averaged 24.5 percent in the 1980s and gross investment had also fallen to about 16 percent in the same year. More importantly, as Harber (Harber, 1995) points out, net domestic saving fell to less than 5 percent of GDP since 1990. "After 1981 net domestic investment fell to less than ten percent of GDP, and fell to less than five percent of GDP after 1985. In 1992, net domestic investment was a mere 1.1 percent of GDP" rising to 1.9 percent in 1993 (Harber). These levels, even if they have increased since the election, are a far cry from the levels needed to generate 5 percent real growth in GDP, a growth target often cited.

Extremely Low Literacy and Education Levels

The Benchmark Indicators presented earlier as part of the MAPS study has thoroughly documented the very low literacy and education levels and will not be repeated here in detail. Literacy as measured by the completion of standard six reveals that only 45% of blacks and 64% of coloureds have attained this level. South Africa has historically done a woefully inadequate job of investing in the human capital of its majority population, a situation which should begin to change under the Mandela government.

Lack of Internal Rivalry, Competition, and Competitiveness

As the recent Monitor study pointed out, South Africa is not competitive in many key industries. The concentration which was partly the result of sanctions has resulted in an inefficient economy. While foreign investment is being cultivated and a number of highly visible new ventures have been announced, foreign investment will probably not account for more than about 20 percent of the total according to Alan Hirsch, Chief Director of Industry Technology Strategy for the Department of Trade and Industry of the Republic of South Africa. Having been cut off from much foreign investment, foreign trade and foreign competition during many years, South Africa faces special obstacles in making the economic transition agreed to in the GATT accords which allow 5 years and in some cases 6-8 years to move to the new tariff regime.

Constraints in the Enabling Environment

A number of uncertainties still exist for the business community regarding the long-term political and economic stability. Concerns continue about the level of personal security. An environment which would place a leading role on export-led growth has yet to emerge. Efforts have been made through the NEDLAC process to engage in an open, participative and transparent dialogue among business, labour and government and this has contributed to confidence building. The task of removing historical barriers of access for the majority population is a long one which only begins with the dismantling of formal legal impediments.

Shared Growth

The benchmark data reveal an exceptionally poor sharing of growth in all indicators including income distribution. Life expectancy, infant mortality, housing statistics, and other standard of living and infrastructure statistics in the Benchmark Study present a similar picture of an abnormally skewed concentration.

3.4 Criteria to Identify Sectors with High Potential

Several criteria were used to identify which sectors offer the greatest potential for expansion of employment, managerial employment and business ownership by the previously disadvantaged. The first was the relative importance of a sector in the economy, measured in terms of contribution to the Gross Domestic Product. A second criterion was the scope for increased black participation, measured by calculations of under-representation.

Another indicator was ease of entry measured by large numbers of black businesses already present in the formal or informal sector. Those sectors which are important to the economy, but where black ownership is relatively small may be targets for increased black participation.

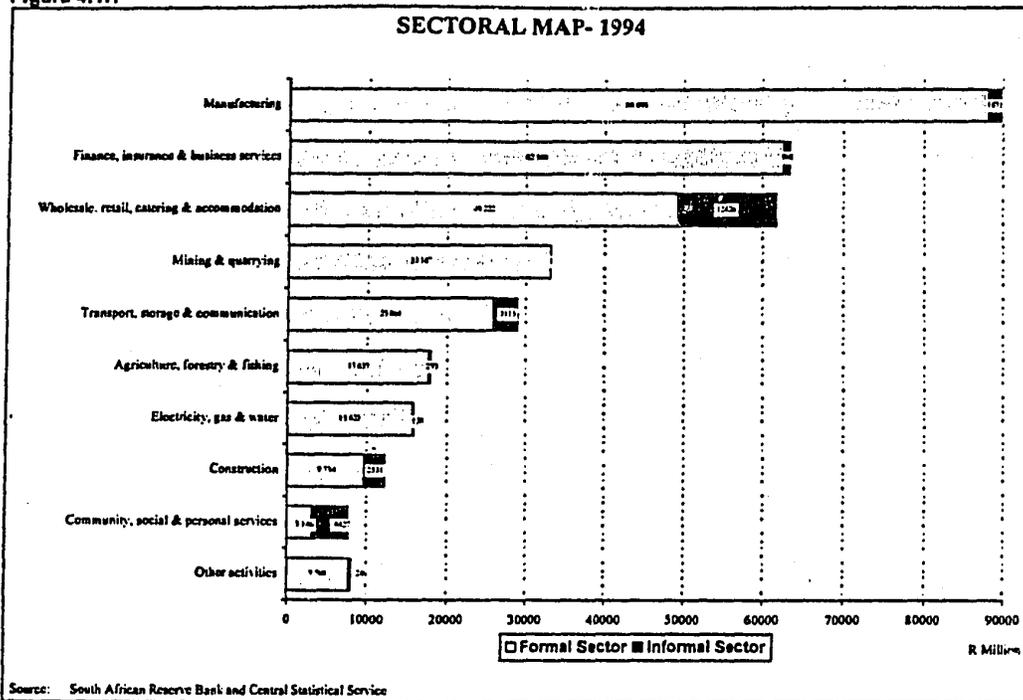
Finally, identification of those sectors with a high potential to grow in the future would also indicate areas for potential increased black participation. Because it is misleading to extrapolate past trends given recent changes, the study has relied on recent competitiveness studies and on input of industry experts.

4 SECTORAL ANALYSIS

4.1 Relative Importance of the Sector

Figure 4.1.1 shows the sectoral map of the South African economy in terms of contribution to the GDP of both the formal and informal sector. It shows that the manufacturing sector is the backbone of the economy, in spite of the decline of the sector over the past years. It also demonstrates that the contribution of the informal sector is considerable in the trade, transport and personal services sectors.

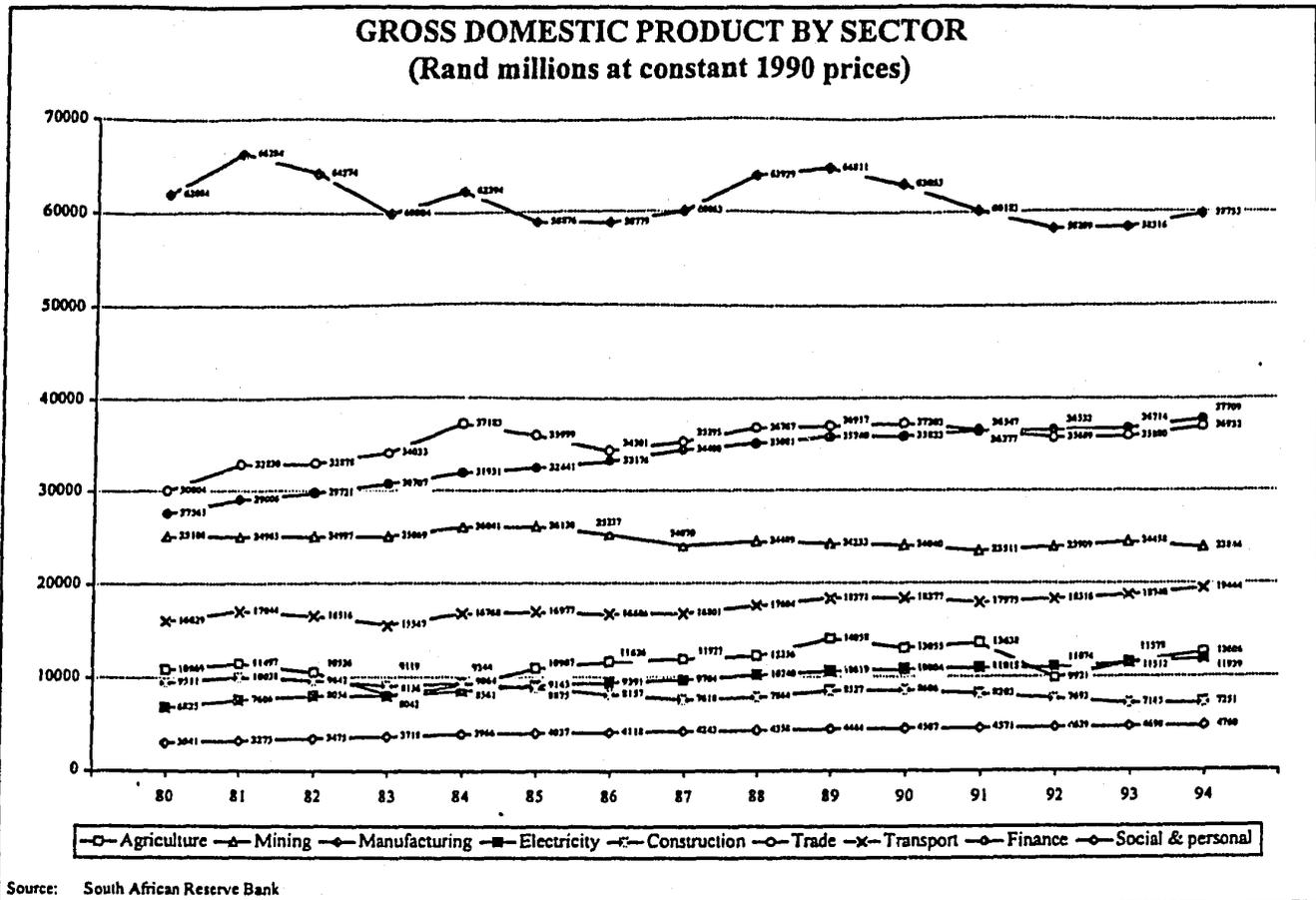
Figure 4.1.1



Extrapolating past trends in the South African economy to forecast future trends could lead to incorrect conclusions because of the changed political realities. However, there are still a number of conclusions to be drawn from the past (figure 4.1.2). The importance of the primary sector, agriculture and mining, has decreased during the past years. The secondary sector, manufacturing, electricity and construction has been stagnant in the recent past. On the other hand, the tertiary sector--trade, transport, finance and personal services--increased its importance considerably.

Figure 4.1.2 further demonstrates the highly cyclical nature of the largest sector of the economy, and shows that this sector, manufacturing, has been in decline during the past years. The strongest growth sectors are trade and finance.

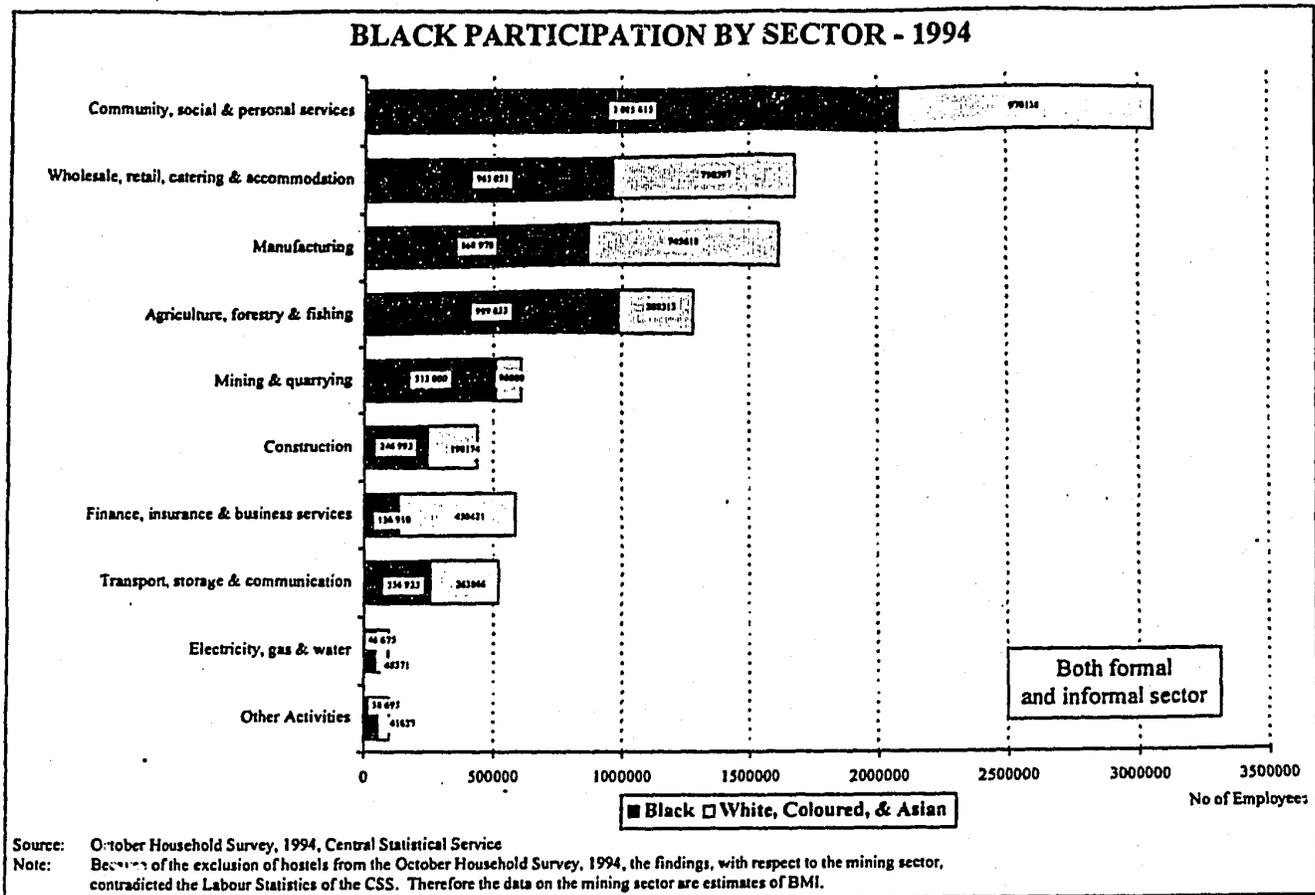
Figure 4.1.2



4.2 Black Participation

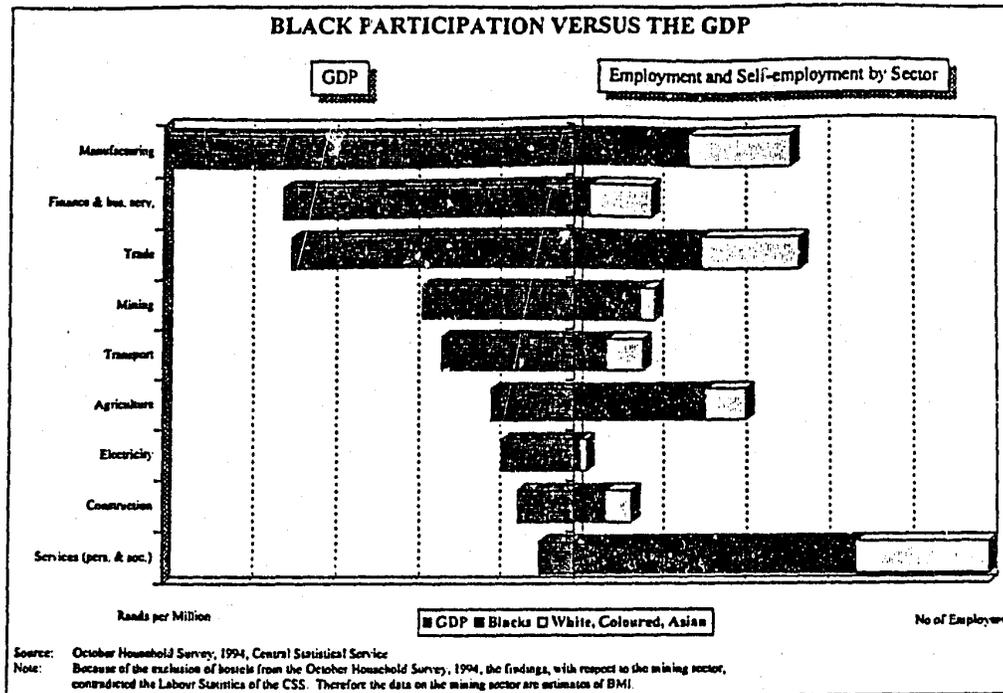
Figure 4.2.1 expresses the participation of blacks compared with the participation of the total population in both the formal and informal sector. Black participation is the largest in the community, social and personal services sector, followed by the trade and the agriculture sectors.

Figure 4.2.1



Comparison of black participation with the relative importance of the sectors to the economy (figure 4.2.2) shows that blacks are mainly active in the lower-value-added sectors. They are relatively under represented in the manufacturing and the finance and business services sectors, and they are very much active in the personal services and the agriculture sectors.

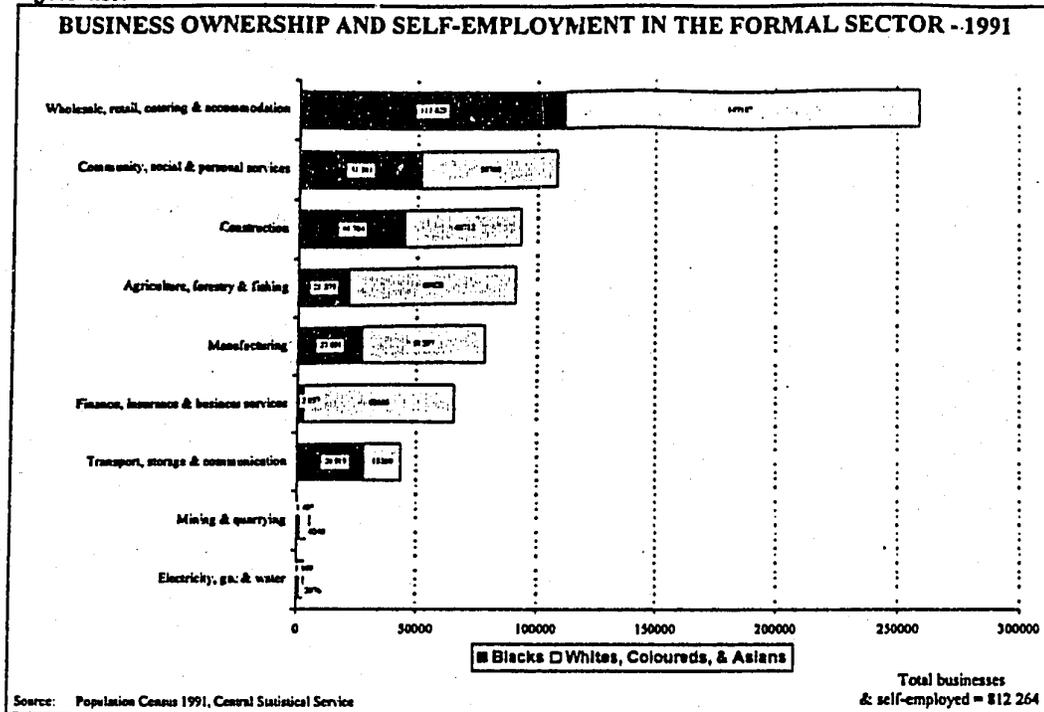
Figure 4.2.2



4.3 Ease of Entry: Existing Black Business Ownership

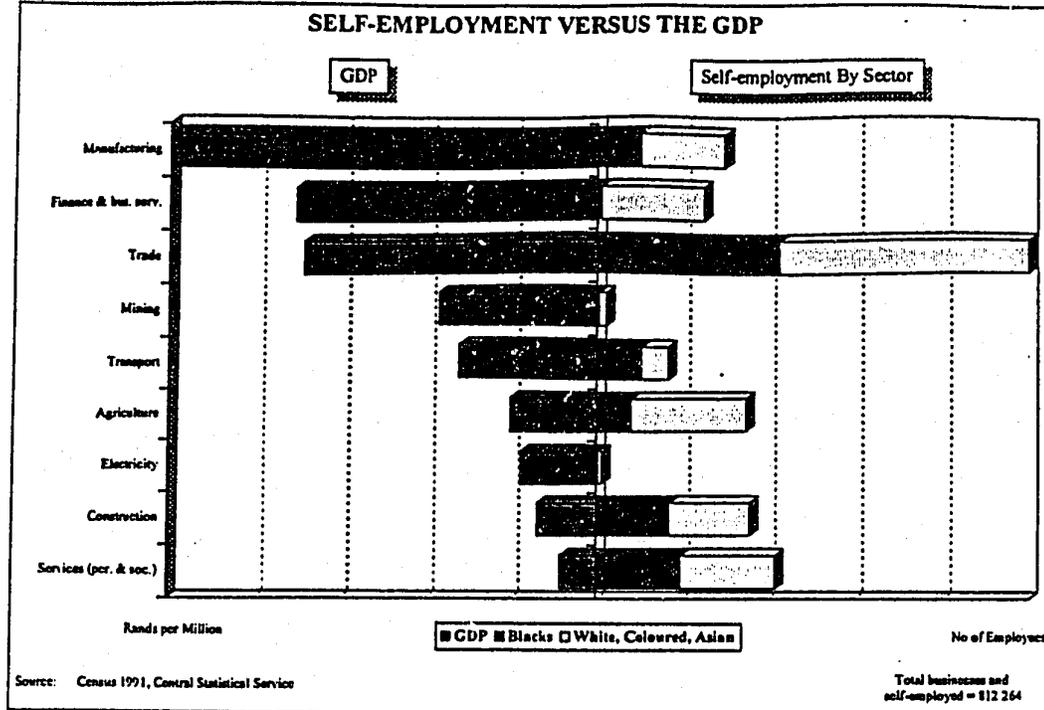
The data on business ownership in the formal sector used for figure 4.3.1 derives from the 1991 Census, where the respondents were asked if they were an employer or were self-employed. The data in this figure, however, does not take in account the size of the business of each respondent. Self employment therefore has the same weight as any other business. This undoubtedly overstates black business ownership. In spite of that, it should be considered as indicative for the distribution of business ownership over the different sectors.

Figure 4.3.1



Comparison of business ownership or self-employment with the relative importance of the sectors to the economy is shown in figure 4.3.2. The figure shows that blacks are under represented in the largest sector, manufacturing, especially when one takes in account that the most black-owned businesses in manufacturing are micro-enterprises. The other sector where blacks are under represented is the finance and business services sector. Blacks are strongly represented in trade, transport, construction and personal services.

Figure 4.3.2



Another source of data on black business ownership is the Gemini project on small scale enterprise in the two black townships Mamelodi and Kwazakhele (Liedholm, 1991). The surveys were censuses of all business activities in the two townships, and enumerated 5253 enterprises. The findings with respect to the sectoral distribution are given in table 4.3.1. The survey found trading activities to be dominant, which is not surprising given the restrictions on black business under apartheid. Another finding is the paucity of manufacturing activities. The bulk of the enterprises were extremely small, with an average of 2,1 employees per enterprise. Construction firms had the most workers (4,9) followed by manufacturing (2,4).

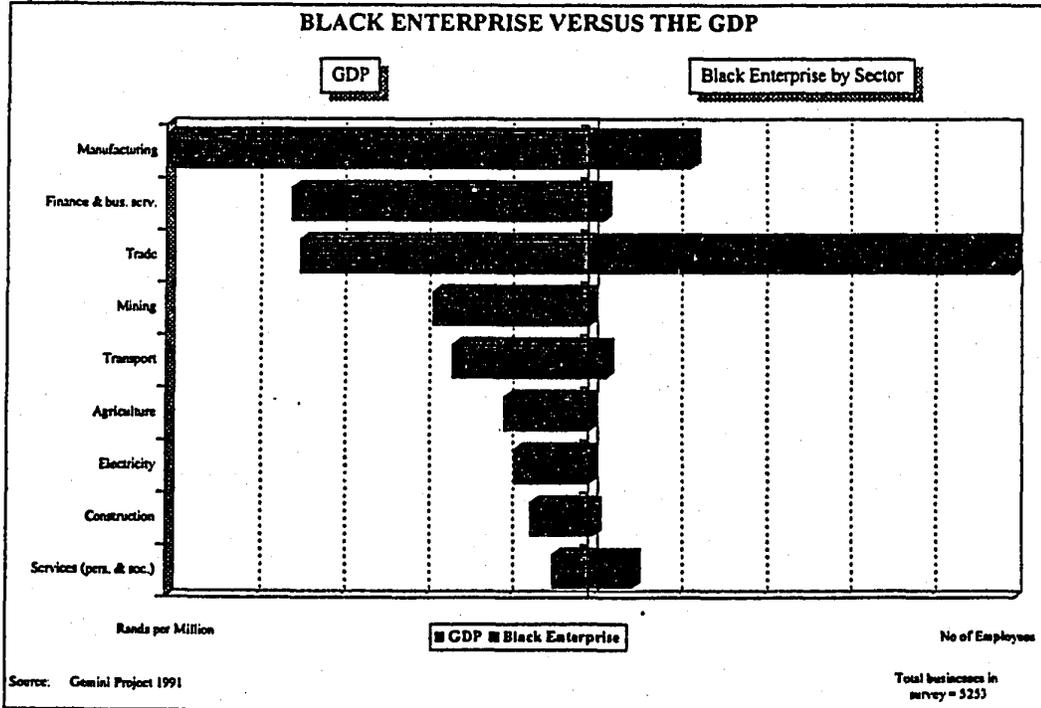
Table 4.3.1 Sectoral Distribution of Small Enterprises in Mamelodi and Kwazakhele

Sector	Number of enterprises	Percentage of total
Food and Beverages	187	3.6%
Textiles	360	6.9%
Wood and Wood Processing	67	1.3%
Paper, Printing and Publishing	1	0.1%
Chemicals and Plastics	6	0.1%
Non-metallic Metal Products	42	0.8%
Fabricated Metal Products	64	1.2%
Other Manufacturing	162	3.1%
Manufacturing	889	16.9%
Construction	31	0.6%
Wholesale trade	13	0.2%
Retail trade	3101	59.0%
Restaurants, Hotels, Bars and Shebeens	584	11.1%
Trade	3698	70.3%
Transport	141	2.7%
Finance and Business Services	120	2.3%
Personal and Social Services	374	7.1%
Total	5253	100.0%

Source: Gemini Project, Liedholm (1991)

The findings of the Gemini survey are consistent with the Census 1991 and the same picture emerges when black enterprise is compared with the sectoral contribution to the GDP (figure 4.3.3). There are, however, some differences with respect to the construction and agriculture sectors, but most of these activities take place outside the townships.

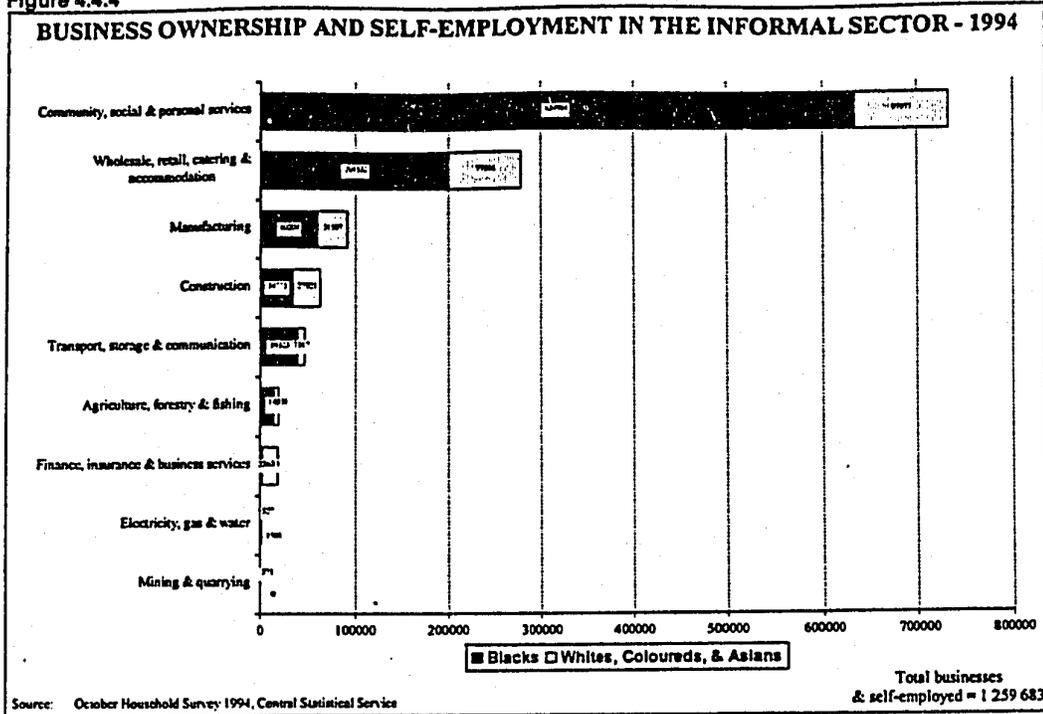
Figure 4.3.3



4.4 Ease of Entry in the Informal Sector

Business ownership and self-employment in the informal sector indicates those sectors where there are few barriers to entry and where entrepreneurs may easily gain experience. Figure 4.4.4 shows that most informal activities are to be found in the personal services sector, followed by trade and manufacturing.

Figure 4.4.4



4.5 Growth Potential of Sectors

Growth is another important criteria to assess the potential of sectors for expanding black business empowerment. A panel of South African experts was assembled to identify sectors with high growth potential. The sectors identified were: tourism, building and construction, certain manufacturing subsectors and finance and business services.

Tourism related sectors

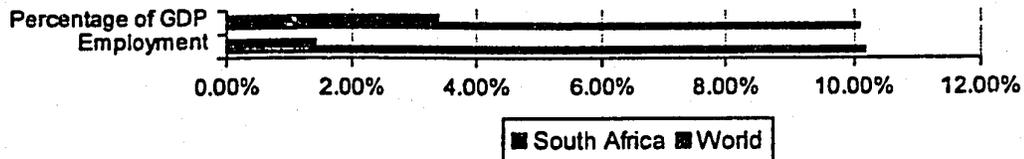
South Africa's national accounts do not track the aggregate contribution of tourism. Tourism can not be considered as a sector but should be considered as a market. Employment through tourism is generated in many sectors:

- Direct employment in businesses that sell goods and services directly to tourists, such as hotels, restaurants, transport operators and shops (1 to 1.4 employees per bed);
- Indirect employment stimulated by tourist expenditures in manufacturing and wholesale distribution (2 to 3 employees per bed); and

- Investment related employment in construction and other capital goods industries (2.7 employee years per new bed)

Tourism related sectors are likely to be growth sectors in South Africa. And there are good reasons for that as figure 4.5.1 demonstrates. The average contribution to the GDP of tourism in other countries of the world is 10,1% whereas it is 3,4 % in South Africa. The average number of employees involved in tourism is 10,2% of the global workforce, in South Africa it is 1,4%.

Figure 4.5.1



Foreign tourism has increased substantially over the past 8 years at a rate of more than 18% per year. The emergence from international isolation has already resulted in a massive growth of the sector. Domestic tourism, however, is worth more than foreign tourism, accounting for 60% of total tourist expenditure. The emergence of the 'black' market will result in an additional increase of domestic tourism.

Building and construction

According to a scenario planning exercise recently performed by the Building Industries Federation of South Africa (BIFSA) and other industry associations, the gradual stimulation of the building industry by building affordable housing could increase employment with a total of 530 000 sustainable new jobs (Khumalo, 1994). Small, black builders are generally regarded as the most appropriate and desirable vehicles for achieving these goals.

Finance and business services

The finance and business services sector has consistently increased its importance over the past years, as can be seen from figure 3.2.3. It is the only sector which increased employment substantially since 1980 with the creation of 186 000 jobs since then (table 3.2.1). The facts that new overseas investors are settling in the country and that local and international firms will increasingly transact with Africa as a whole lead to the expectation that the sector will grow.

Manufacturing

Manufacturing production grew by 2,5% in 1994 in real terms as opposed to 0,2% in 1993, and the decline in manufacturing employment was arrested. Though improved production occurred in almost all sectors of manufacturing, certain sectors did improve significantly better. This implies that certain subsectors have a larger growth potential. An example is the furniture sector where production increased by 17% during the last 6 months of 1994, and exports increased sharply. Another example is the fabricated metal products subsector where production increased by 2,6% and exports by 79,7%. The clothing subsector increased production by 3%, and the textiles subsector increased by 6% (IDC, 1995).

4.5 Conclusions

The most important sectors in terms of contribution to the GDP are:

- Manufacturing
- Finance and business services
- Wholesale, retail trade, catering and accommodation

Blacks are under represented in terms of economic participation in the following important sectors:

- Finance and business services
- Manufacturing

Blacks are under represented in terms of formal business ownership in the following important sectors:

- Finance and business services
- Manufacturing

There is ease of entry for blacks in the following formal sectors:

- Wholesale, retail trade, catering and accommodation
- Building and construction
- Certain manufacturing subsectors

There is ease of entry for blacks in the following informal sectors:

- Community, social and personal services
- Wholesale, retail trade, catering and accommodation
- Certain manufacturing subsectors

The following sectors can be considered as future growth sectors:

- Tourism related sectors: catering, accommodation, trade and other services
- Building and construction
- Finance and business services
- Certain manufacturing subsectors

Table 4.5.1 Findings of the Sectoral Analysis

Sector	Contribution to GDP	Under repres. of blacks	Ease of entry formal	Ease of entry informal	Future growth
Manufacturing	⊕	⊕	⊕	⊕	⊕
Finance	⊕	⊕			⊕

Trade	⊕		⊕	⊕	⊕
Mining					
Transport					
Agriculture					
Electricity					
Construction			⊕		⊕
Personal services				⊕	

Table 4.5.1 presents the findings in matrix form. It becomes clear that the following sectors should be analysed further:

- Manufacturing
- Building and construction
- Finance and business services
- Tourism related sectors and Trade

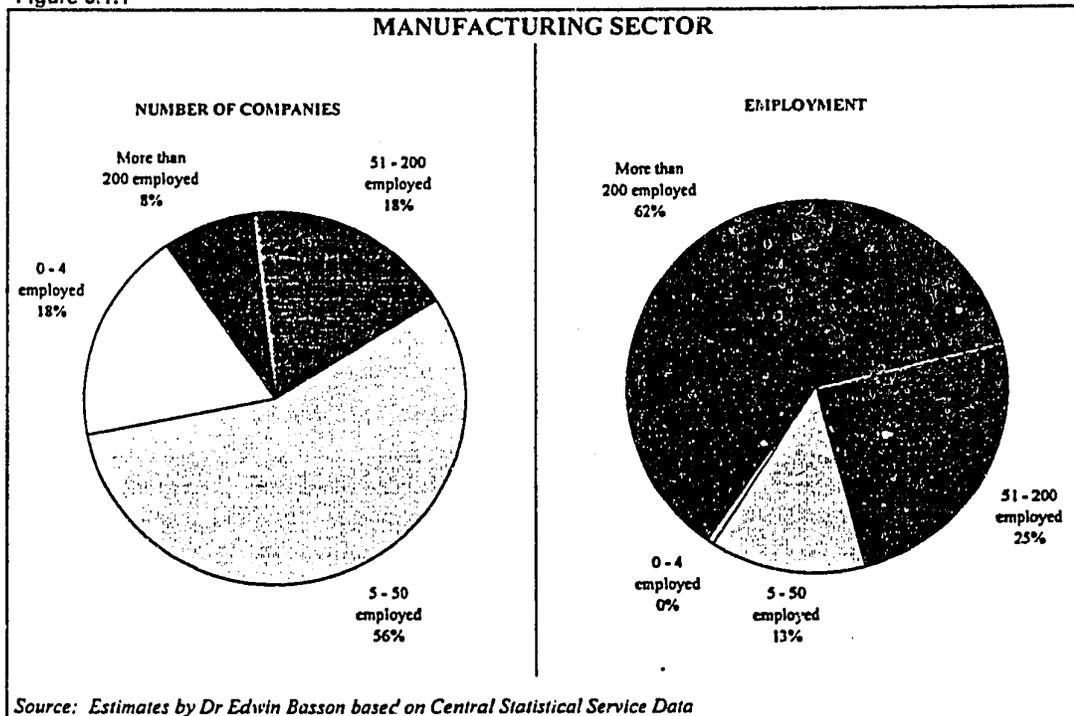
5 MANUFACTURING

5.1 Introduction

The critical importance of the manufacturing sector as the backbone of successful economics has been amply demonstrated (McCarty, 1993). The "sectoral map" of the South African economy demonstrates that manufacturing also plays the leading role in the South African economy. It provides productive jobs and can provide for a potentially large expansion in black economic participation, provided it can become more competitive than it is at present and achieve significant rates of growth.

Increased black economic participation is strongly related to macroeconomic policies, international competitiveness, and industrial development strategies. Various studies have argued that manufacturing development in South Africa has been sub-optimal and that this a severe constraint to growth. Excessive import substitution, deteriorating labour relations, factor price distortions in favour of capital, trade sanctions, and worst of all, a lack of investment in human capital through education and training, have resulted in an industrial sector noted for its poor productivity and lack of growth.

Figure 5.1.1



Another characteristic, which coincides with the previous named characteristics, is the under-representation of small-scale industry in South Africa. World wide SMMEs play a large role in manufacturing. In South Africa, however, though only 8% of all companies employ more than 200 employees, those large companies employed 62% of the manufacturing workforce (figure 5.1.1). Given the world-wide tendency to smaller and medium sized scale production (most new jobs created world-wide are small business) there seems to be a strong case that South African manufacturing is overly concentrated.

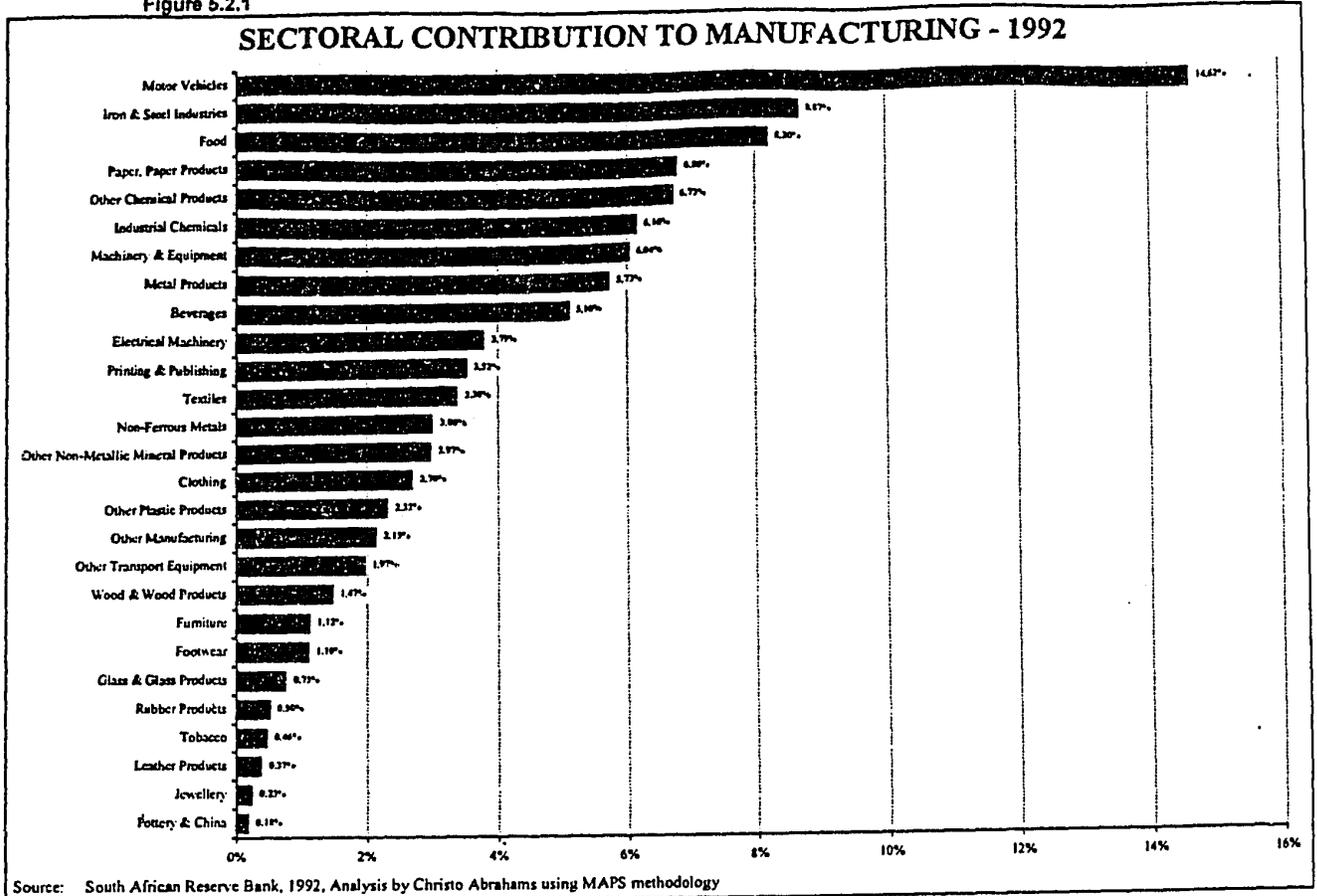
In the next section the selection of manufacturing subsectors with the potential for expanding black economic participation will be discussed. Thereafter two subsectors with potential are analysed: fabricated metal products; and furniture and fixtures. This is done to indicate constraints to expansion and useful interventions to mitigate those constraints.

5.2 Selecting Manufacturing Sectors

In selecting manufacturing sectors with a potential for expanding black participation, several criteria were used: a) current size of the sector; b) low barriers to entry; and c) low initial technology requirements.

Current size indicates the extent to which resources are available, and the extent to which there is a market for the products of that sector. Figure 5.2.1 presents the contribution to manufacturing in terms of value added for the different manufacturing subsectors. This criteria should be treated with caution, because it ignores a number of influencing variables such as protectionist measures and the potential of subsectors that have been ignored until now but should be competitive under a less protectionist policy environment.

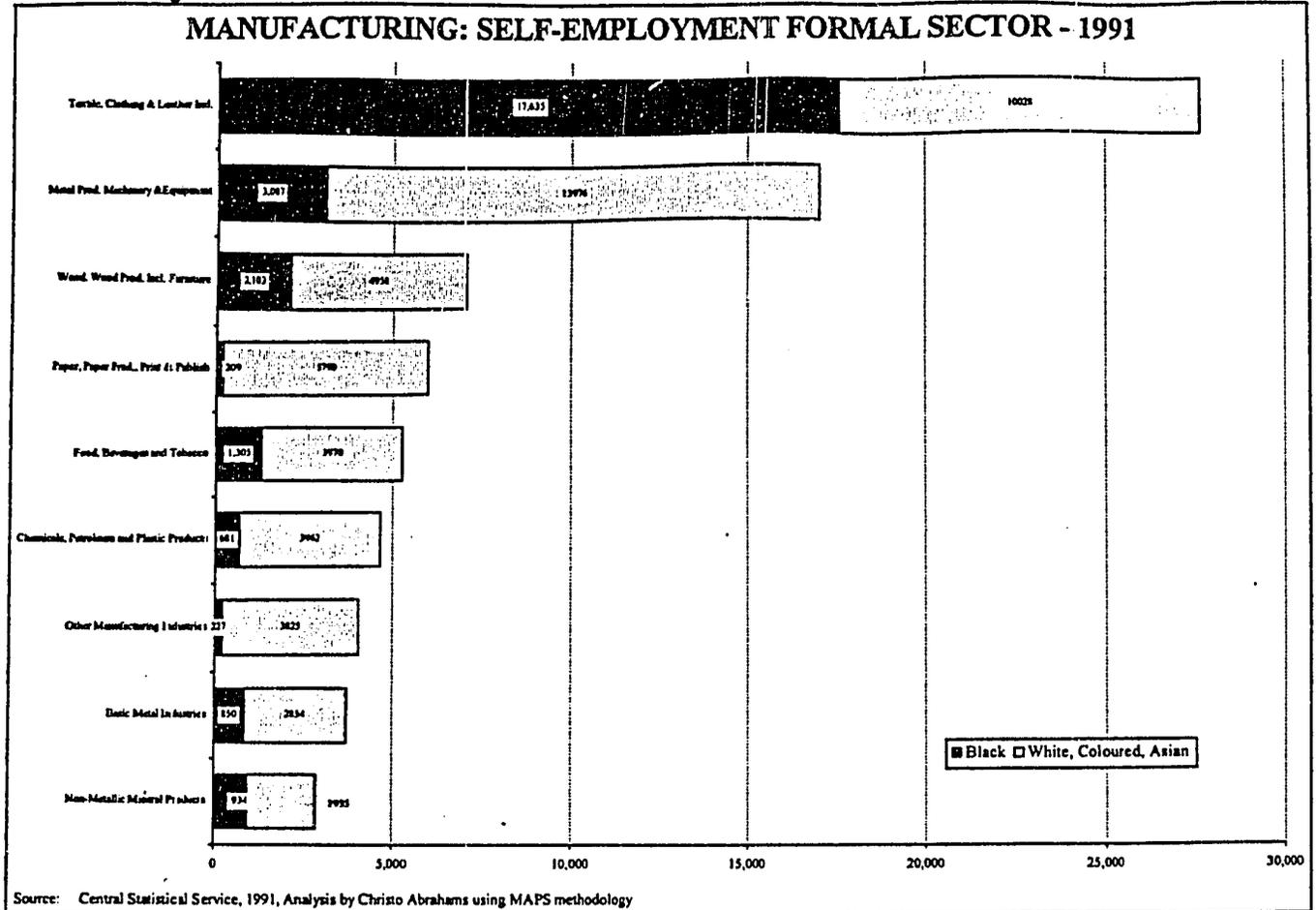
Figure 5.2.1



Low barriers to entry in a specific subsector can be measured by measuring the existing base of black entrepreneurs in that subsector. As figure 5.2.2 shows, as well as the data on informal sector activities, these sectors are:

- Clothing and textiles
- Fabricated metal products
- Furniture and fixtures
- Food and beverages
- Plastics and chemicals
- Wood and wooden products
- Printing and publishing

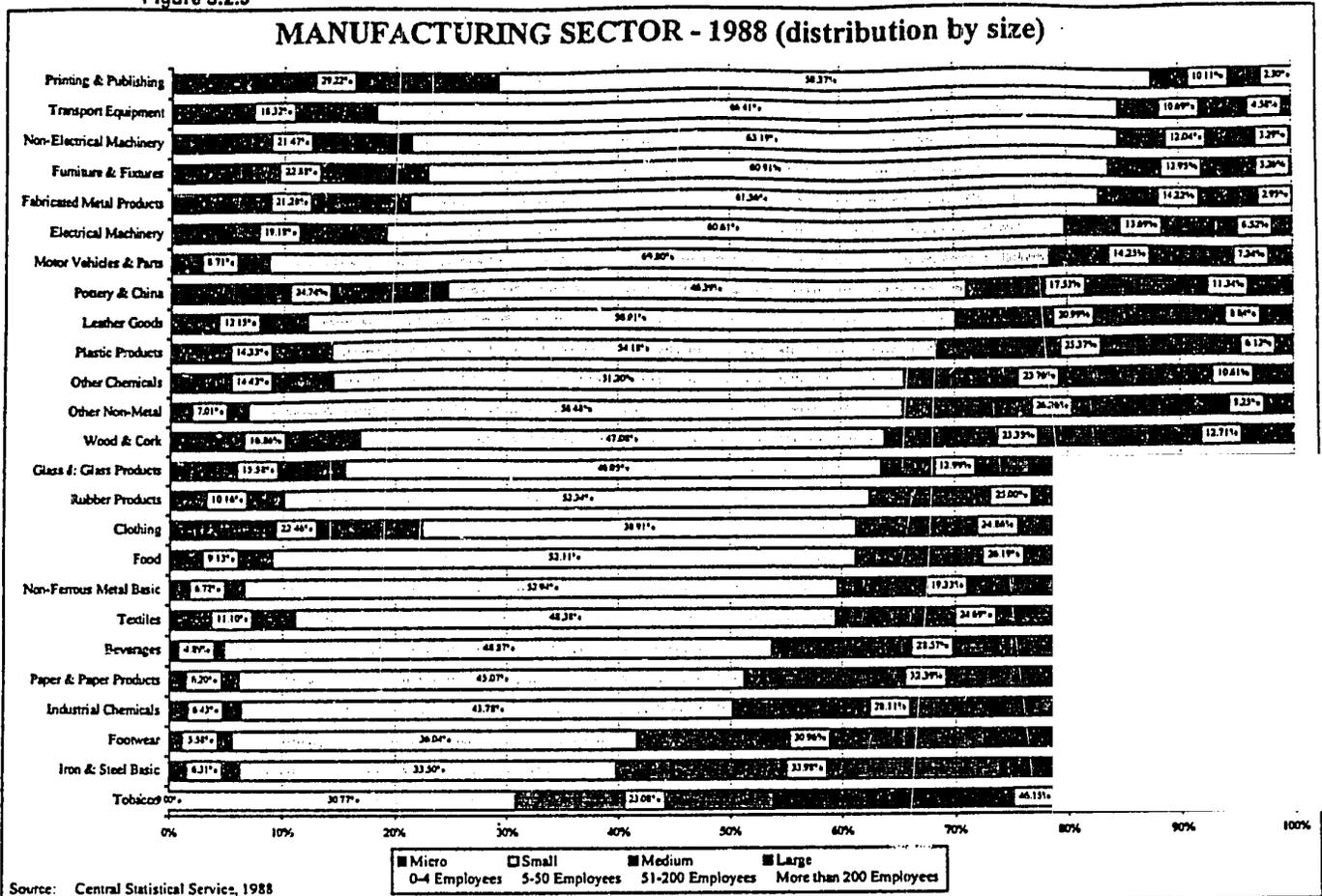
Figure 5.2.2



Ease of entry is also indicated where there is a higher proportion of new and small enterprise relative to medium and large firms. Industry concentration, as Michael Porter has pointed out, is a sign of higher barriers to entry. Figure 5.2.3 gives the size distribution of the manufacturing subsectors. The sectors at the top of the chart, with a higher tendency to have a large percentage of small firms are:

- Printing and publishing
- Transport equipment
- Non electrical machinery
- Furniture and fixtures
- Fabricated metal products

Figure 5.2.3



Ease of entry is also associated with lower capital costs, i.e. higher labour intensity. Certain manufacturing subsectors tend to employ more people in small business than others. The subsectors that employ the highest percentages in small business are:

MANUFACTURING SUB-SECTORS RANKED BY LABOUR INTENSITY

– Furniture and fixtures	74,5% of employment in that subsector
– Plastic products	61,5% of employment in that subsector
– Printing and publishing	60,9% of employment in that subsector
– Fabricated metal products	58,0% of employment in that subsector
– Leather and leather products	53,9% of employment in that subsector

Attractiveness (or lack thereof) in a sector is also analysed by the intensity of existing rivalry. Most black manufacturers operate in over-traded sectors, with basic skills and a low technology level. The challenge is to increase these skills by training and technology transfer. It then will be possible to let these entrepreneurs diversify into higher-value-added markets. A final, but not less important criterion is the potential for growth of the sector, both on the short and the long term. This criterion includes the vulnerability for import penetration of that sector in the future.

After analysis of the different subsectors, with the help of these criteria, it becomes clear that two subsectors qualify for further analysis:

- Fabricated Metal Products
- Furniture and Fixtures

It should be noted that, though these subsectors stand out as having a high potential to expand black participation, it does not imply that other subsectors should not be considered for further consideration. Rather these will serve as illustrative cases.

5.3 Fabricated Metal Products

One of the first subsectors of the manufacturing sector into which black-owned microenterprises entered is that of metal bending and processing. The reasons for this are that the entry barriers are low (both the capital as well as the skill requirements are minimal) and the market--black township resident--was close.

At present there are many entrepreneurs active in this subsector. The market that most enterprises serve has reached a saturation point. Few entrepreneurs have expanded into the more lucrative white household markets or into higher-value-added products. Competition amongst entrepreneurs is fierce, and margins are extremely low in the sector. While large numbers of entrepreneurs continue to enter the sector, there is hardly any growth taking place within existing enterprises.

Another problem is the cost of inputs which are untenably high, since microenterprises tend to source in very small volumes. The supply market is further highly concentrated with ISCOR producing the bulk of all steel in this country, and two other producers providing the rest.

One means of addressing the first problem would be to encourage diversification into more lucrative segments of the market. For example, the production of metal furniture requires a similar base of knowledge of metal processing, yet there are few manufacturers in this sector. Given that metal furniture production is one of the fastest growing segments of the furniture market internationally, and that it is just beginning to become popular in South Africa, this sector is a potential growth sector. The reasons that black SMMEs have not identified this market and penetrated it are: a lack of information; fear of risk-taking implied by moving out of a secure market; and the most important one, skill shortages.

Interventions addressing these constraints would be the simulation of innovation through, for instance, the supply of information about new markets, and skills training and technology transfer to enable the production of higher value added products. The constraint of high input costs can be addressed by establishing alternative patterns of sourcing. This can be done by encouraging entrepreneurs to source collectively or to establish some type of buying co-op, which mediates between the large suppliers and small manufacturers.

In summary, the sector seems suitable for expansion of black economic participation because:

- A large number of black entrepreneurs are already in the metal processing sector;
- Technology and skill requirements are not prohibitive;
- Any support for entrepreneurs can be directed at skill or asset deepening rather than start-up, because of a large existing entrepreneur base;
- There is potential for greater value-added through diversification; and
- The market for the final products is likely to grow in the near future.

5.4 Furniture and Fixtures

Another example of a subsector in which black manufacturing is likely to expand is the manufacturing of furniture. There are about 1300 registered furniture manufacturers and another 300 unregistered furniture manufacturers. The majority of the enterprises in the furniture industry are SMMEs. Though the majority of the small firms are white-owned, there are a substantial number of black-owned enterprises. Micro-enterprises tend to be clustered in the upholstery sector, because the skills, technology and capital requirements are the lowest in this segment of furniture making.

There is a high concentration of input suppliers with 4 mills producing over 70% of all sawn timber. The sector is further dominated by one manufacturer producing 40% of all manufactured furniture in SA. The small manufacturers each have marginal market shares. Distribution channels are highly concentrated with seven retail groups selling more than 90% of all furniture. Less than 10% of all furniture is sold through independent retailers, the upper end of the market. Only a marginal proportion of all furniture is exported from South Africa.

In this sector, a leading constraint to growth is a lack of working capital. Manufacturers are only paid 90 days after delivery, therefore they are in fact financing the credit sales of the retailers in a certain extent. Cash flow problems are often debilitating small manufacturers, for whom access to overdraft facilities is limited. Another problem is the concentration of buyers. The structure of the industry makes it difficult for small manufacturers to penetrate the market. Because the large retail chains have a national presence, consistency of supply is essential. They are therefore more likely to source from larger manufacturers, who can supply the volumes that they require. The third problem is lack of managerial training. Entrepreneurs do not know what the requirements are to establish growth.

Despite these significant problems, several reasons make this a sector in which black economic participation can be expanded:

- The implementation of the RDP, specifically the housing programme, will provide a boost to the furniture industry. This increase in demand at the lower end of the market can partially be met by micro enterprise.

- The implementation of a procurement policy aimed at promoting small (black) enterprise. Government is a major purchaser of furniture, yet past procurement policy has been heavily biased against smaller producers. An explicit shift in this policy will take place, with a positive spin-off for small producers.
- The technological barriers to entry are low, but there is large scope for technology transfer and innovation, with potential for adding value.
- Low risk of import penetration. Furniture is a bulky and heavy item, resulting in high transport costs. Most imported furniture arrives in knocked down form, and there is a high resistance to having to assemble the furniture.

However, several interventions can be recommended:

Government

- A procurement policy should provide preference for SMMEs
- The competition board should investigate allegations to a timber cartel
- Import duties and surcharges on imported boards need to be revised, since local prices are reputed to be at least 30% higher than international prices.

Private Sector

- The Furniture Industry Training Board should be restructured to enable more effective representation of SMME's
- Large retailers can be encouraged to work with small business, especially if filling orders for the government
- Small business themselves need to explore options to overcome volume constraints. Co-operatives, networks or joint marketing mechanisms are possible vehicles to address these constraints.

Donors and NGOs

- Information and advice regarding management systems for micro and small enterprises. A successful example is a USAID programme used to help upgrade the management systems of a black furniture manufacturer. The matching of own finance with grant finance for training and a management information system was extremely successful, with the entrepreneur noting immediate results.
- Financial assistance, via credit unions, SMMEs, NGOs, etc., to alleviate cash flow problems.

5.5 Useful Interventions

In summary, based on the constraints and recommended interventions of the two examples of potential subsectors the following interventions, aimed at the manufacturing sector can be recommended:

- Technology transfer to SMME's
 - Manufacturing Technology Centres
 - Innovation assistance
 - Vertical linkages between big and small
 - Joint ventures
 - Exchange programs with foreign companies
- Access to markets
 - Sub-contracting
 - State procurement
 - Export assistance
 - Trade fairs
- Stimulating horizontal linkages
 - Building alliances and networks
- Competition policy
- Industrial Hives

6 BUILDING AND CONSTRUCTION

6.1 The Building and Construction Industry

The total expenditure in the industry accounted for 8% of the GDP in 1991, and amounted about 24 million Rand. Expenditure in the industry can be divided into residential building (28%), non-residential building (35%) and construction works (37%). The principal clients are public authorities (29%), public corporations (16%) and private enterprises (56%). Housing-related expenditure accounts for the largest portion of public sector funding in this industry (CSIR, 1993).

There are a large number of firms operating within the industry and they are well organised in a number of representative bodies. The established businesses have sufficient capacity and are able to handle a moderate increase in demand. The situation of small (informal sector) builders, however, is quite different. They experience more problems with obtaining finance and are unable to negotiate favourable prices on materials.

The proposed Government program to increase housing construction, coupled with a hoped-for general economic upturn, may result in a rapid growth of the building industry. The provision of low-cost housing is a priority within the Reconstruction and Development Programme, and it is thought that small majority-owned building enterprises are the appropriate means to achieve the goals. They should be involved either as principal contractors or subcontractors to large property developers. The expansion of the black building industry, however, is confronted with a number of constraints.

6.2 Constraints to the Development of Black Builders

Shortage of skilled labour

The shortage of skilled and reliable labour constrain the growth of black builders. Though the shortage of skilled labour is a general constraint to the whole industry, it is a more serious problem for black business. The training facilities of the representative bodies are only accessible for those contributing fees and dues. Small and informal builders often can not afford to pay these fees.

Lack of managerial skills

The major constraint to growth of black building enterprises is the lack of managerial skills of their owners. Many entrepreneurs fail to keep even the most rudimentary records, and planning is hardly practised. Another related problem is the weak cost accounting practices, which often leads to builders working on unrealistic prices (Krafchik, 1991; and Cattell, 1992). Black builders should be better trained, particularly in management skills such as tendering, project management, resource control and marketing techniques (Khumalo, 1994).

Access to finance

Another constraint to growth is finance, because financial institutions are reluctant to support the sector with loans. Black building firms are stereotyped as high-risk enterprises run by unreliable entrepreneurs who lack good track records. Several support schemes have been suspended in the past because of repayment problems, but Khumalo (1994) maintains that the problems were caused by reasons outside the builder's control. At any rate, black builders are often unable to obtain finance.

Access to markets

Access to markets is another constraint. Black builders do control the market for renovations and additions in black townships, but the most lucrative market is that of new housing, which is dominated by white-owned business. Black builders do not have easy access to this market because of the lack of working capital, and they are often confronted with a bias in favour of white contractors. Furthermore, black builders have never seriously attempted to penetrate the home building and renovation market in white residential areas because of a lack of confidence.

6.3 Interventions

Vocational training

Vocational training should be made more accessible to all stakeholders in the industry, which means that access should be broadened to small and informal builders. Industry associations should consider differential fees and structures to permit entry by smaller businesses. A reduced labour rate on contracts can be used as an inducement for on-the-job training.

Managerial training

Access to managerial training should be made easier and sources of funding need to be explored. Those firms who are most in need of the training are those least able to afford it. Specialised courses for small, emergent contractors should be initiated, together with a mentorship program to support training in tendering, project management, resource control and marketing techniques.

Finance

New mechanisms for financing what are perceived to be high risk firms must be sought. Financial institutions should be encouraged to work with their clients and potential clients to develop relationships and partnerships. Loan guarantee or alternative forms of collateral or risk management should be explored by financial intermediaries. The availability of end-user finance will further contribute to the growth of black builders.

Preference to black builders

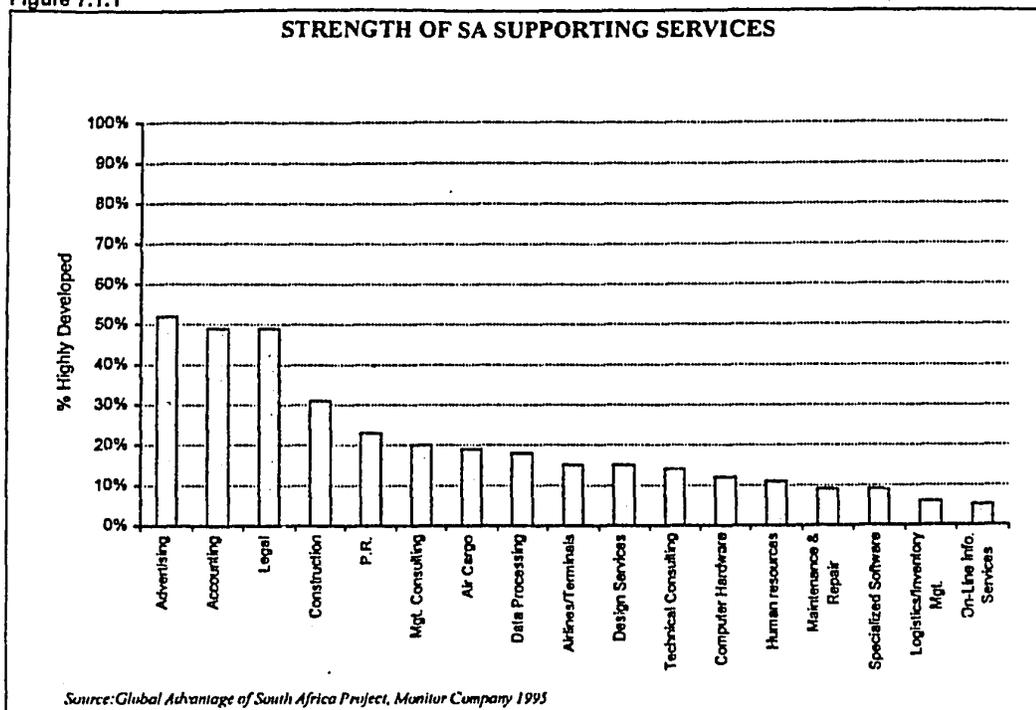
The Government should help create markets for black builders by giving them preferences as part of the affirmative procurement policy. Under the RDP program, this could amount to a major boost in work for this group.

7 FINANCE AND BUSINESS SERVICES

7.1 Introduction

The finance sector of South Africa is well developed and is considered to be highly sophisticated. The business services sector, however, seems to be critically weak. The opinions of 400 leaders in business, government and labour organisations were asked on the performance of business services. Figure 7.1.1. presents the findings of the Monitor project. It is apparent that there is a gap to be filled, especially when the fact is considered that the business services sector should be a driver to regaining competitiveness and creating a culture of innovativeness.

Figure 7.1.1



7.2 Constraints and Interventions

Majority-owned firms are significantly under-represented in the finance and business services sector, as employees, managers and self-employed or entrepreneurs. The main constraint to increase black participation in the sector is education and training. The universities have a large role to play to eradicate these constraints. Large financial institutions have to contribute by increasing the skills levels of their staff through in-house training programs. Interventions that will contribute to an increase of the number of black professionals in this sector include:

- Scholarships to black students, both local as well as international;

- Exchange programs for black professionals to both local and international firms; and
- Technical assistance to majority-owned finance and business services firms.