The Impact of SMEs on Socio-Economic Development in South Africa: A theoretical Survey

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Abstract
This theoretical survey seeks to critically investigate the impact that Small and Medium Enterprises (SMEs) have had on socio-economic development in the South African (SA) context. A global perspective of the impact of SMEs is incorporated in order to have a feel of how other economies have benefited from this venture. The survey followed a desktop literature review research design in order to gather data regarding other economies in Europe, Asia, America, Latin America and select countries in Africa. Regarding challenges currently experienced by SMEs, the survey established constrained government support and lack of universally accepted standard unit measurement of SMEs. The survey discovered several varying socioeconomic roles played by SMEs in SA and other regions alike namely, job creation, reduction in rural and urban poverty, narrowing income inequality disparity and contributing towards the nation’s Gross Domestic Product (GDP). Given the undisputable significant roles played by SMEs particularly in SA, the following recommendations have been advanced in order to strengthen SME’s roles; firstly, streamlining stringent rules and regulations which inhibit SMEs in venturing into more rewarding business opportunities. Secondly, reviewing the prohibitive terms and conditions of accessing financial aid from the government and financial institutions. Thirdly, continuously empowering prospective entrepreneurs through tailor made capacity building initiatives.

Keywords: Entrepreneurship, SMEs, socioeconomic development, South Africa.

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1. Introduction and research background

Primarily, it is of paramount importance to note that a standard international definition of small and medium-sized enterprise (SME) does not exist since they are defined differently in the legislation across various nations and this is simply because the dimension “small” and “medium” of a firm varies depending on the size of the domestic economy. However, for statistical purposes, the OECD (2016a) defines SMEs as those firms employing up to 249 persons, with the following breakdown: micro (1 to 9), small (10 to 49) and medium (50-249).

This research survey provides a synthesis of the contemporary state of affairs about small and medium sized enterprises (SMEs) and their contributions towards economic and social well-being. However, these contributions vary widely across firms and across countries and sectors. The survey also touches on the various characteristics of SMEs, the opportunities and challenges they face. Areas where knowledge or data gaps exist and where more analysis is needed shall also be explored.

Since the dawn of the democratic era in 1994, the South African government has been putting concerted efforts in supporting SMEs in local government spheres in order to promote empowerment, job creation, economic growth and community development. Alert (2015), points out that like many other third world or developing nations, South Africa’s socio-economic development strategy hinges on harnessing the entrepreneurial potential and supporting small to medium enterprises (SMEs). Chinweuba & Sunday (2015), asserts that entrepreneurship and SMEs contribute to the growth of the economy as well as the creation of jobs. He further argues that their growth and development could be a viable strategy that would ensure sustainable development that comes through a reduction in unemployment rate, poverty and inequality in developing countries.

Therefore, given the benefits that accrue with the development of SMEs, since the promulgation of the 1995 White Paper on SME development, prioritization of this sector by the South African government has been on the increase such that a separate Ministry of SMEs. Other support functionaries such as the Small Enterprises Development Agency (SEDA) were created in order support and revamp this sector into a robust and significant contributor to the economic growth of the country (Bureau for Economic Research, 2016).

As alluded to, the campaign to empower SMEs comes with its challenges and the proceeding sections shall explore such both at global and national level.

2. Literature Review

2.1 SMEs are essential for delivering more inclusive socio-economic growth

In The Organization for Economic Cooperation and Development (OECD) countries, SMEs are the dominant form of enterprise, constituting approximately 99% of all firms. It thus apparent that they provide the main source of employment, accounting for about 70% of jobs on average, and are the main contributors to value creation, generating between 50% and 60% of value added on average (OECD, 2016b). In emerging economies, SMEs
contributing up to 45% of total employment and 33% of GDP. Taking into consideration the contribution of informal businesses, SMEs boast up to more than half of employment and GDP in the majority of countries irrespective of income levels (IFC, 2010).

In many countries, and in particular OECD countries, governments have had to deal with a number of hurdles regarding low growth rate, weak trade and investment, and rising, or persistently high inequality (OECD, 2016a). This has often resulted in a growing dissatisfaction among citizens with the current state of affairs, and this has been a draw-back or a backlash against globalization. As such, governments have realized and initiated the growth and development of SMEs, providing an environment where they can easily adapt and thrive through actively participating and thus boosting economic growth and delivering a more inclusive globalization. Across countries at all levels of development, SMEs have proved beyond doubt that they have the potential to play a big role in the achievement of the Sustainable Development Goals (SDGs), through the promotion of an inclusive and sustainable economic growth that is characterized by employment creation, sustainable industrialization and reinforcing innovation while at the same time reducing income inequalities.

2.2 SMEs are central to the efforts to achieve environmental sustainability
The reduction of the environmental effects of SMEs by emphasizing and going beyond environmental compliance with the current rules and regulations in both manufacturing and services is fundamental for success in the green transformation. This is particularly urgent for SMEs in the manufacturing sector, which accounts for a large part of the world’s consumption of resources, air and water pollution and generation of waste (OECD, 2017a). The green transition also gives business opportunities to SMEs as suppliers of green goods and services. In the OECD countries, innovative SMEs play a very important role in the eco-industry and clean-tech markets. For example, in the United Kingdom and Finland, SMEs represent over 90% and 70% respectively of clean technology businesses (ETLA, 2015).

2.3 Creation of more inclusive growth
One major advantage of SMEs is the creation of job opportunities right across geographic areas and sectors, employing broad segments of the labor force which comprises low-skilled workers, and providing opportunities for skills development. In some cases, they also help support their employees’ access to health care and social services. Therefore, SMEs that generate jobs and value added are an important channel for inclusion and poverty reduction, especially but not exclusively to emerging and low-income economies. According to OECD (2009, 2017b), the upgrading of productivity in a large population of small businesses, including in traditional segments and the informal economy, can facilitate the achievement by governments of both economic growth and social inclusion objectives, including escaping from low productivity traps and bettering quality of jobs for low-skilled workers. This is the case of social enterprises, which bring innovative solutions to the problems of poverty, social exclusion and unemployment, and fill gaps in general-interest service delivery (EU/OECD, 2016). In most of the countries, the economic weight of the social and solidarity economy, in which social enterprises operate, has steadily increased steadily of late, including during the post global crisis. According to EU (2016), in Belgium, over 2008-14; employment in social enterprises increased by 12% and accounted, in 2015, for 17% of total private employment. In the United Kingdom, in 2015, 41% of social enterprises had created jobs compared to 22% of SMEs (SEUK, 2015).

2.4 Variation of contributions by SMEs across countries.
The level of contribution by SMEs to the socio-economic development of any given economy depends on a number of factors such as the country or sector they find themselves in. In all countries, micro-enterprises (up to 9 employees) dominate the business landscape, accounting for 70% to 95% of all firms. However, notable cross-country differences are witnessed regarding the contribution of micro-enterprises to employment and value added. For example, in the services sector, the SMEs share in employment ranges from more than 60% in Greece to 20% in Denmark and Germany, while their share in value added ranges from about 45% in Luxembourg to 15% in Switzerland (OECD, 2016b).

According to OECD (2017c), sectors also determine the performance of SMEs. In nearly all countries, SMEs account for 60% or more in services of total employment and value added. The opposite is true in manufacturing although relatively few in number, large firms outnumber SMEs in terms contribution to employment and value added. In other countries like Germany and Mexico, large manufacturing groups capture a significant share of total employment and value added. Some exceptions are experienced in smaller economies such as Latvia and Estonia, as well as larger economies where SMEs have traditionally dominated manufacturing activity, such as Italy.

2.4.1 Brazil
Brazil is another BRICS nation that has encouraged the development of small business through a favorable government policy. The legislation passed in 1999, in an effort to stimulate SME growth, made it easier for businesses to pay taxes, access investment loans, and export their goods. A recent announcement of a reduction in
the interest rate on public loans for small businesses from 8% to 5% is a commitment by the government to empower and liberate SMEs. The expansion of the presence of business which assist early-stage small businesses with strategy, legal navigation, educational resources, and other guidance, through its National Incubation Support Programme is also a signal of how much the government wants to empower and boost SMEs. In fact, The World Bank ranks Brazil 134th out of 189 countries for ease of doing business. It ranks 109th for ease of credit and 159th for ease of paying taxes, OECD, (2017c).

2.4.2 India

India has put in place measures to help promote SMEs. Research has it that SMEs in India employ 69 million people and their contribution to India’s GDP has been increasing at 11.5% annually, faster than the country’s overall GDP growth of 8%.11. India’s Ministry of Micro, Small, and Medium Enterprises was created in its present form in 2007, but the government’s efforts to assist SMEs dates back to 1999 when the Ministry of Small Scale Industries was put in place. The Indian government has done a lot to help SMEs through giving them sufficient access to credit, supporting in technology modernization, and through the provision of educational opportunities for business owners and managers, OECD, (2017c).

2.4.3 The United States

Although some studies have questioned the true impact of small businesses on job creation, their role remains pivotal in the United States. Between 1993 and 2011 alone, small firms, defined in the United States as having fewer than 500 employees, created 64% (or 11.8 million of 18.5 million) of the net new jobs. The support and involvement of the American government with small businesses dates back to 1953 when it formed the Small Business Administration (SBA). The sole objective of SBA’s support was to foster small business growth through training and development and access to finance. Since then, the SBA has taken several steps some of which included the removal of bureaucratic red tape, facilitating access to capital, streamlining application procedures, and the improvement of educational opportunities for small business owners.

In its 2014 Congressional Budget Justification and FY 2012 Annual Performance Report, the SBA laid out its strategic goals with the principle one being to grow businesses and create jobs by expanding access to capital through its lending network, ensuring that federal contracts are being given to a defined number of small businesses, fostering its entrepreneurial education and counseling services, and enhancing its focus on high-growth entrepreneurs, OECD, (2017c).

2.4.4 Sweden

Lee, Herold, and Yu (2016) assert that 90% of global firms are SMEs and they employ more than 50% of all labor in the private sector, with Swedish SMEs contributing 56% of economic wealth production. SMEs constitute 99.9% of enterprises in Sweden. They account for about 60% of total added value and 60% of total employment. This makes SMEs a crucial part of the Swedish economy. The research also pointed out some factors that determine readiness to grow by Swedish SMEs and these were:

- belonging to the service sector (companies in the accommodation and food service, and wholesale and retail sectors were most willing to grow);
- level of cooperation with other companies;
- franchise and group affiliation;
- internationalisation;
- innovativeness – companies that considered themselves innovative had a more positive view on their future growth;
- sustainability – companies that sell environmentally friendly products were more willing to grow.

2.4.5 Nigeria

Jibir and Ahmed (2018), report that SMEs enhance economic growth and act as catalysts for the development of the Nigerian economy which is arguably the biggest in Africa after South Africa. Nevertheless, this development is limited by a number of constraints such as inadequate access to finance capital. This has adversely affected SMEs scale of operations and as a result the Nigerian government has adopted policies aimed at ameliorating their financial conditions such as liberalization of the financial markets, the establishment of lending institutions as well as the formulation of policy measures that compel financial institutions to allocate a certain percentage of their lending portfolio to SMEs. Other constraints that have negatively affected the growth and contribution of SMEs in Nigeria include inadequate infrastructural facilities such as epileptic power supply, lack of adequate water supply, poor state of road network and unreliable telecommunication facilities among others.

3. Performance overview and outlook of SMEs in South Africa

Notwithstanding the claims that SMEs are a major ingredient for economic development, their contributions to the economy remain underappreciated, debated, and contested in addition to being undermined and misinterpreted (SEDA, 2018).

Thus, there have been conflicting sentiments regarding the real mark that SMEs have left on the South African soil to date. The Small Business Institute (SBI) (2019), reports that the contribution of SMEs toward the creation
of employment has fallen short. They have actually credited large businesses for creating more jobs at a much faster rate than SMEs. In contrast, the Real Economy Bulletin, (2017) asserts that SMEs are the major force behind employment creation and poverty alleviation. It further argues that in the previous two years, formal small business employment figures were 5.8 million people in comparison to 3.6 million people employed by large businesses. Business Unity South Africa (BUSA) (2019), also echoed the same and stated that SMEs create 65% employment opportunities making them the largest contributor to private employment in South Africa.

However, these positive accounts of the impact of SMEs remain challenged primarily because there is no existence of distinct evidence of the degree to which SMEs deliver towards poverty alleviation, employment creation and economic growth. Godfrey Jacobs, the Cape Chamber of Commerce and Industry as cited in an article by Mohedeen (2019) adds that in South Africa, “the corporate sector has been shedding jobs over the past decade and the bloated public service has probably reached its limit and will be under pressure to bring staffing numbers to more realistic levels”.

In South Africa and as elsewhere in Africa, historical surveys attest to the fact that the prevalence of big businesses such as multinational corporations (MNCs), without the active participation of small business is the reason why poverty, unemployment, and low economic growth is characteristic of the continent.

4. Challenges that have stalled the success of SMEs in South Africa

4.1 The historical economic development in the country

It is crucial to note that under apartheid, SMEs existed on the peripheries of economic recognition, more or less regarded as an informal economy, a status quo that unfortunately continues to the present day. Buthelezi, Mtani, and Mncube (2018) assessed the extent of market concentrations in South Africa and discovered that large businesses dominate markets primarily because of past privileges, such as state support, which SMEs did not also enjoy.

The literature further reveals that, prior to 1994; black entrepreneurs were barred from owning businesses. This implies that a democratic South Africa dawned with only small number of established small business (Real Economy Bulletin, 2017). The bulletin still maintains that even following the onset of democracy, not much changed in the local economic structure as SMEs continue to experience economic exclusion from mainstream economy as a result of distrust held by carryover apartheid institutions and the racially exclusive culture of business networks in the country that have set up industry standards that are unattainable, (Real Economy Bulletin, 2017). In his view Urban (2018) states that the growth of SMEs is inhibited by tight oligopolies in many markets where several large firms dominate the competitive landscape and erect high entry barriers. This has resulted in SMEs being marginalized to less protected sectors such as trade, business services, and retail.

4.2 Constraints in measuring SMEs contributions

Chikweche and Mujeyi (2015), in a survey carried out in Zimbabwe, assert that the usage of established national economic indicators such as GDP, formal employment figures, or export values especially in developing countries have often fallen short of capturing and presenting an authentic and true account of the SME sector’s contributions to the economy. According to Bureau for Economic Research (2016), the problem is that different researchers and institutions apply different methodologies to produce SMEs statistics, and this has resulted in different accounts of size and potential impact of SMEs to the economy.

A good example is the claim by the Small Business Institute (2019) that there are only a quarter of a million SMMEs, other literature (SEDA, 2018:2; SBP Alert, 2014) assert an estimate of between 1.2 million and 6 million SMEs. In addition, the Small Business Institute claims large businesses and government create 56% of jobs and so are the largest employers. This therefore shows so much divergence of data on the actual size and state of the South African SME sector to an extent that all estimations can be regarded as mere guesswork. This implies that the contest on the value of SME to socioeconomic development is expected to continue because the actual size of the SME sector remains unknown.

5. SME contributions to socioeconomic development in South Africa

In-spite of the arguments by researchers and institutions regarding the contributions of SMEs in South Africa, evidence on the ground has proven that these small to medium scale firms have impacted on the socio-economic dimension to a great extent. Below is a detailed explanation of the immense contribution by SMEs toward socioeconomic development in South Africa which include job creation, sustenance of the rural economy, distribution of income and poverty alleviation, nurturing entrepreneurship, maintaining a healthy economy, enhancing social cohesion and reducing social conflict as well as addressing economic, social and racial inequalities.

5.1 Job creation

Following a massive loss of jobs due to the unprecedented restructuring, downsizing and retrenchments instate entities such as ESKOM and South African Broadcasting Corporation (SABC), many retrenched employees, in
order to mitigate the impending abject poverty, turned to entrepreneurial ventures most of which are of a survivalist nature (SEDA, 2018). Jili, Masuku, and Selepe (2016:6) affirmed that small businesses reduce the unemployment rate and alleviate poverty through offering an immediate escape route for people confronted with little life opportunities for employment, access to capital and social support.

5.2 Sustaining the rural economy
Because of their size, SMEs are ideal for rural communities where the markets are too small to attract large businesses that would otherwise outdo them in terms of competition. Thus SMEs link the rural economy and the urban economy through trade relationships as they serve as the fulcrum of rural and peri-urban South African economy. They assume greater responsibility in providing a source of livelihood and sustenance to many families in both the rural and urban areas and thereby help curb or reduce the challenge of rural-urban migration. Lastly they also help in spreading industrial enterprises more evenly across the country to support sustainable economic development.

5.3 Distribution of income and poverty alleviation
In-spite of the fact that income earned by employers and employees in the informal economy is less than in the formal economy (Real Economy Bulletin, 2017), entrepreneurial self-employment tends to cushion retrenched employees against abject poverty. Harris (2018) states that the burden for poverty alleviation falls on the SMEs as most large businesses are downsizing and automating leading to loss of jobs.

5.4 Nurturing entrepreneurship
According to Waterhouse (2019), contemporary entrepreneurs are keen on learning new and advanced modern ways of doing business contrary to a neoclassical idea of entrepreneurs as simply risk takers. SMMEs have the ability to groom entrepreneurship and innovation and could possibly attract foreign investment. Nevertheless, in South Africa SMMEs ability to attract foreign investment has been dampened by the ever-present corruption scandals in large business (for example, Steinhoff fraud) and government scandals (for example, State capture) which have adversely affected the image of the country. In-spite of such draw backs the SMME sector has often acted as a “nursery” for higher-level entrepreneurship and innovation where entrepreneurs learn by failure until they gain the skill to grow their business.

5.5 Maintaining a healthy economy
Although SMEs are by nature confined to operating in their local communities and markets, evidence shows, they are also involved in export business and this has facilitated the generation of the much needed foreign currency for a healthy economy. Furthermore, exports link SMMEs with business from other countries, thereby exposing local firms to international standards in such a way that will improve their industry knowledge and skills.

5.6 Enhancing social cohesion and reducing social conflict
Dlova (2017) points out that the high influx of foreign nationals into South Africa is met with entrepreneurial opportunities which allow them to start their own small businesses thus avoiding conflict through scrambling for a few jobs on the market. He also asserts that since SMEs are locally owned, they strengthen extended family relationships, social systems, and cultural traditions. Furthermore he asserts that through job creation SMMEs significantly assist in achieving social and political stability.

5.7 Addressing economic, social and racial inequalities
The South African Human Rights Commission (2018), argues that given the high disparities in terms of socio-economic, racial and gender inequality in South Africa, smaller companies like SMEs have tried to a certain extent to bridge the gap through the empowerment of the previously disadvantaged. Both poverty and economic inequality continue to manifest along racial, gender and disability lines and because of that the South African government has launched a campaign to promote SMMEs as a vehicle to achieve a radical socio-economic transformation agenda. Through the enactment of the BEE programs, preferential vulnerable groups such as women, disabled persons and youths who were often overlooked in the formal economy find sanctuary in the SMME sector.

6. Conclusions and Recommendation
Based on the information gathered, tabulated and analyzed, the following conclusions can be drawn:
- SMEs do act as a catalyst in driving the growth of any given economy both in the developed and developing countries.
- Consistent with global trends reviewed, SMEs have the capacity to stimulate the most basic form of commerce in society, considering their dynamic nature which ranges from street vendors to medium-
According to Rungani & Potgieter (2018), SMEs facilitate a much easier entry to business and self-sustenance and do provide the incubation and breeding platform for entrepreneurship and innovation. The following recommendations could possibly be taken into consideration if the government of South Africa is to get the best from the role that SMEs are already playing in developing the country’s socio-economic status:

- Recognizing SMEs as an integral sector of the national economy thereby giving it the support it duly requires.
- Streamlining stringent rules and regulations whose inhibitive tendencies have created challenges in venturing into more lucrative businesses which as of now, are deemed to be of the “elite”.
- Reviewing the terms and conditions of accessing financial aid from the government and financial institutions.
- Empowering prospective entrepreneurs through organizing training and development interventions in various sectors.

References


