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BLACK INDUSTRIALISTS, BARRIERS TO ENTRY, AND APPROPRIATE INTERVENTIONS

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Abstract

This paper provides a high level review of the design and objectives of the BIS based on publically available information and insights gathered through interviews with DTI and other organisations providing business support initiatives. The assessment considers the complementarity between BIS and other initiatives and agencies, the selection criteria of potential beneficiaries, the core economic and ownership criteria applied for selection of beneficiaries, the funding model and links to other DFIs and issues in non-financial support since the inception of the programme. Drawing from the detailed interviews with the DTI, Industrial Development Corporation and other stakeholders involved in providing support for SMEs, as well as publically available information, the paper identifies key challenges for businesses relating to access to working capital, the complexity and duration of application, approval and disbursement processes, and coordination issues within the co-funding model. This paper forms the basis for a second paper assessing survey data on the outcomes and performance of the BIS.

JEL classification: L60, O25

Keywords: black industrialists, funding, working capital, access to markets

Contents

1. Introduction

The Black Industrialists Policy (BIP) was created by the Department of Trade and Industry (DTI) with the primary aim of transforming the manufacturing industry in South Africa through prioritisation and inclusion of black businesspeople (NCOP Committee, 2016). The underlying premise is that development of the manufacturing sector generally, and broadening participation within it including through the production of higher value products and associated jobs, is critical for establishing a new economic growth trajectory for South Africa. The emphasis on empowering black owned businesses in particular, relates to the continued concentration of economic power in the economy in the hands of the few, and the apartheid legacy of limited participation in the economy by black individuals as owners of factors of production and resources. There is therefore a compelling political and economic imperative to foster the inclusion of black business owners in the mainstream economy, going beyond those that have obtained ownership of established businesses through the Black Economic Empowerment strategy.

Early discussions around the BIP, and specifically the Black Industrialist Scheme (BIS) which is the specific funding programme under the policy, began in the mid-2000s. The BIS was approved by Cabinet in November 2015 and launched publicly in February 2016. The scheme is intended to assist black industrialists by providing concessional (grant) funding through a central office which sources funding from the other development finance institutions (DFIs) such as the Industrial Development Corporation and various provincial DFIs. The BIP was also created to provide other market interventions to assist these businesses in terms of access to markets including through procurement and supplier development agreements with state-owned enterprises (SOEs) and the private sector.

At inception funding was provided through a concessional loans framework, which was funded by the national DFIs as well as by provincial DFIs. The DTI also had a pool of funds dedicated to the programme. The BIP is distinguished from other existing programmes of government in that it focuses on development and improvement of existing black owned and operated manufacturing businesses in the economy, rather than necessarily creating new businesses. The programme therefore runs alongside other programmes such as B-BBEE, special economic zones, and other support and incentive schemes of DTI and government (NCOP Committee, 2016).

The BIS exists alongside several programmes of government under different institutions that focus on business support and funding in different ways; financial or non-financial. Non-financial needs of the entrepreneur are just as important as financial ones. For example, managerial, organisational and technical requirements can be limiting factors for new entrants. Therefore, the BIS needs to be understood in the context of the programmes that on paper offer complementary services (i.e. incubation, proposal development, feasibility assessment, technical and managerial training, access to start-up capital, etc.) such as those under the Industrial Development Corporation (IDC), the Small Enterprise Development Agency (SEDA) and the National Empowerment Fund (NEF), amongst others. As several of the initiatives and policy programmes have been in place for some time now, and even as the BIP is in the early stages of growth, it is an opportune time to reflect and critically analyse the design and implementation of the BIS to understand how existing programmes can be adapted, replicated or improved to provide appropriate complementary support for emerging enterprises.

This paper provides a high level review of the design and objectives of the BIS based on publically available information and insights gathered through interviews with DTI and other organisations providing business support initiatives. The assessment considers the complementarity between BIS and other initiatives and agencies, the selection criteria of potential beneficiaries, the core economic and ownership criteria under BIS, the funding model and links to other DFIs and issues in non-financial support since the inception of the programme. The initial intention of the paper was also to evaluate the actual outcomes against the design and objectives of the programme, however given data limitations and the fact that the programme is still in its early stages, the paper rather focuses on the above aspects relating to the design and objectives of the programme. The paper is intended as a background paper for the second study which will analyse survey and interview data on the experiences of firms that have received support under the BIS and other government and private or NGO-led business support programmes. The following key research question is explored in this paper:

(a) *Is South Africa's Black Industrialist Scheme appropriately designed and implemented to increase the quantitative and qualitative participation of black industrialists in the economy?*

Key questions explored in the second paper are as follows (although some of the issues are introduced in this paper):

(b) *What have been the outcomes of the Black Industrialists Programme and firm support initiatives?*
(c) *What are the key barriers for firm growth under the various programmes and what interventions are necessary to improve outcomes?*

The paper is structured as follows: Section 2 reviews studies of barriers to entry and SME participation to set out the core concerns facing businesses, before Section 3 sets out the approach followed in the research. Section 4 provides an overview of the BIS, and Section 5 and Section 6 analyse the design, objectives and outcomes under the BIS. Section 7 draws together other cross-cutting issues for businesses identified through interviews and Section 8 concludes with key issues for consideration in the second phase of the research.

2. Studies of barriers to SME participation

There are a range of mutually reinforcing obstacles which hinder meaningful entry and participation in the economy by black owned businesses and SMEs The BIP was launched, in part, to address some of these challenges (DTI, 2015 and 2016). However, in order to effectively address the needs of black industrialists, it is imperative to develop a clear understanding of the nature and significance of the barriers, and the extent to which existing policies address these challenges. Several studies have identified the following key barriers to entry and challenges facing business development in South Africa (Banda et al, 2015; Hawthorne et al, 2016; Ncube et al, 2016; Paelo & Vilakazi, 2016; Roberts, 2017; SA SME Fund, 2018). Some of the key issues from these studies are set out in this section.

Access to finance

One of the challenges identified in the different studies on barriers to entry is access to finance. While other barriers are equally important, the issue of access to finance is critical because new and black entrants face considerable challenges in obtaining start-up capital[1]; whether from commercial banks or development finance institutions (Ncube et al, 2016). For example, while scale economies are crucial, the major barrier for new entrants is the substantial investments required in order to be efficient producers. Furthermore, applications for financing are typically cumbersome and lengthy, with entrants often assessed against historical performance rather than projections (Herrington & Kew, 2015; Ncube et al, 2016; SA SME Fund, 2018; Seed Academy, 2018). This discriminates against new entrants.

Routes to market

One of the critical stages in the entire value chain of any product/service is the ability to reach customers, which is a significant challenge in several sectors of the South African economy, including for manufacturing and processing firms. For instance, in the Fast Moving Consumer Goods (FMCG) value chains, supermarkets are a key route to market for suppliers of food and household consumables. However, concerns have been raised that large supermarkets place stringent demands that small and medium-sized local suppliers often find difficult to fulfil given lack of capabilities (das Nair and Chisoro-Dube, 2017). These concerns are exacerbated by the fact that the formal retail industry remains concentrated in South Africa (das Nair and Chisoro-Dube, 2017). This has had the effect of excluding small and medium-sized suppliers from important supply chains.

Furthermore, the use of exclusive agreements in the distribution of beverages, and in the allocation of retail space in the shopping malls or retail centres, creates significant barriers to entry (Banda et al, 2015; Bosiu et al, 2017).

Scale economies

This typically happens when there are substantial fixed (and likely to be sunk) costs which do not increase with output. However, small entrants may be unable to raise the capital required for large scale entry. These effects are large in mobile telecommunications and retail banking due to significant initial infrastructure investment requirements (Hawthorne et al, 2016; Makhaya and Nhundu, 2016; Roberts, 2017). In milling, silos and SAFEX operate in such a way that substantial deposits are required to be able to trade (reportedly of R1mn for accessing silos) (Roberts, 2017).

Vertical integration

This is typically a barrier in as far as the entrant relies on their rivals for key inputs and/or key markets. Furthermore, new entrants in milling are reliant on the supply of grain from silos owned by large firms that are either integrated into milling or grain trading themselves, or have established relationships with larger incumbent millers, making it difficult for smaller and new millers to do business with silo owners (Roberts, 2017). Thus, rivals have to enter simultaneously at different levels of the value chain as vertically integrated operators, which significantly increases the entry costs. The entry of Grain Field Chickens (GFC) in poultry is a typical example (Ncube et al, 2016). For small and medium-sized firms with limited financial resources, the cost of entry can be so high as to render them uncompetitive.

The above set of barriers is not exhaustive, and there are other general challenges facing small and medium-sized businesses in particular, such as poor infrastructure, low levels of

[1] This is generally as a result of lack of collateral.

research and development (R&D), onerous labour laws, organisational capabilities, skills shortage, inefficiencies in government bureaucracy and high levels of crime (BER, 2016).

This research is not the first of its kind in terms of assessing the experiences of SMEs in their interactions with government and private sector-led business support programmes. The SBP SME Growth Index has been an annual index reported on from the year 2011 by SBP Business Environment Specialists.[2] The intent of the index has been to track the dynamics driving South Africa's SME community with a focus on the extent of employment absorption by SME's as well as turnover growth.

SME Survey is an entity providing an annual representative survey of small, medium and micro enterprises in South Africa.[3] This survey focuses on the impact of business environment factors on the competitiveness and success of SMEs. Year-on-year findings are based on 1,400 telephonic interviews with a randomly selected sample of decision-makers at South African SMEs, consisting of companies across all vertical sectors. The Seed Academy also conducts a survey in South Africa (in its fourth iteration in 2017/18) of over 1000 SMEs to assess key challenges for growth, cutting across sectors and sizes of enterprises (Seed Academy, 2018).

The common thread among these surveys is that the main barriers faced by SMEs are regulation barriers, lack of skills and finance, and challenges with labour legislation. However, an important issue to note is that these surveys highlight barriers insofar as they are linked to SMEs in general and not necessarily to SMEs owned by individuals/groups that were previously disadvantaged. The issues identified are generic cutting across business activities with no emphasis on identifying the ownership of businesses or distinguishing whether the challenges of access to finance, for example, are more acute for black-owned business or otherwise.

3. Assessment framework

It is important to recognise that the BIS is a relatively new programme within the range of business support and funding programmes in South Africa. Having been launched publicly in 2016, the programme is only in its fourth year of implementation. This context is important given the outcomes observed, and the performance of the programme against the stated objectives need to be considered as part of this early-stage development of the programme, noting also that some of the key objectives may not be achieved as yet. This assessment is therefore a contribution to the evaluation of the programme within an adaptive regulatory framework as has been set up, with a view to aiding the strengthening and development of the programme to fully address the needs of businesses over time.

The approach followed is to evaluate the following key aspects of the BIS:

- Assessment of the design, functioning and performance of the programme against the issues identified in the interviews and the programme objectives
- Analysis of the programme in the terms of alignment with other complementary programmes of government and private sector programmes for black business and SME support

[2] SBP website: http://www.sbp.org.za/
[3] SME Survey website: http://www.smesurvey.co.za/

The study has been conducted primarily through a combination of interviews with the DTI and government agencies providing the support initiatives. Furthermore, data has been requested at the organisation and/or programme level, as well as selected interviews with beneficiaries under the programmes as follows:

- Data on beneficiaries under the black industrialists programme and initiatives of the DTI, IDC, SEDA, and NEF where possible. This includes assessing the extent and nature of support, trends in sectors and nature of businesses supported, and potential challenges and opportunities both within programmes and across them.
- Detailed interviews of organisations and recipients of support under the black industrialists programme and initiatives of the BIS, IDC, SEDA, and NEF.

In the second phase of the research, a broader baseline survey of beneficiaries across programmes will be conducted as well as in depth firm level interviews of a selection of beneficiaries.

In terms of the data and information received to date, this report relies extensively on interviews conducted with the DTI, NEF, IDC, SEDA, ProfitShare Partners, Black Umbrellas and BrownSense. Submissions of data have been requested and are expected to be received shortly.

The assessment therefore relied on the high level information received in the interviews and triangulation with publicly available information. In terms of the key insights set out below, a number of the questions raised about the BIP will be tested against the data received from the different organisations, as well as the broad baseline survey and interviews of beneficiaries to be conducted in the next phase of the research.

4. Background on the DTI Black Industrialists Scheme

The BIP was refined through a series of discussions dating as far back as 2005, and largely informed by the outcomes of the BEE Commission which had raised concerns that the DTI appeared to be supporting mainly existing businesses.[4] Moreover, even in the case of entrants, support still favoured white owned businesses. Thus the purpose of the policy is to leverage the state's capacity to unlock the industrial potential that exists within black owned and managed businesses that operate within the South African economy through deliberate, targeted and well-defined financial and non-financial interventions, as described in the IPAP and other government policies. The policy subsequently led to the establishment of the Black Industrialists Scheme (BIS) in December 2015, launched publicly in February 2016.[5] Disbursements, approvals and job creation under the BIS are discussed in more detail further below.

The policy/scheme has two key objectives: 1), to accelerate the quantitative and qualitative increase and participation of Black Industrialists (BIs) in the national economy, selected industrial sectors and value chains, as reflected by their contribution to growth, investment, exports and employment; and 2), to create multiple and diverse pathways and instruments for BIs to enter strategic and targeted industrial sectors and value chains. Overall, it is envisaged

[4] Interview with DTI, 16 October 2018
[5] Black Industrialists Policy: Department of Trade and Industry briefing, 24 February 2016. Parliamentary Monitoring Group webpage.

that the industrialists will contribute to South Africa's developmental objectives, such as job creation, exports, skills and supplier development, industrial decentralization and localization.

4.1. Defining Black Industrialists

A Black Industrialist is a juristic person that includes co-operatives, incorporated in terms of the Companies Act (2008) that are owned by black South Africans, as defined by the B-BBEE Act, who create and own value-adding industrial capacity and provide long-term strategic and operational leadership to a business. A Black Industrialist can also be a natural person. BIs are African, Coloured and Indian persons who are natural persons and are citizens of the Republic of South Africa by birth or descent, or by naturalization before the commencement date of the Constitution of the Republic of South Africa Act of 1993. The term also refers to individuals who became citizens of the Republic of South Africa after the commencement date of the Constitution of the Republic of South Africa Act of 1993, but who, had it not been for the Apartheid policy, would have qualified for naturalization before then. The definition includes South African Chinese people as per the Pretoria High Court ruling on the 18th June 2008.

Particular focus is also given to entities owned by individuals with disabilities, and those based in historically disadvantaged regions.

In addition to the definition above, a Black Industrialist has the following characteristics[6]:

- Has a high level of ownership (more than 50%);
- Exercises control over the business;
- Takes personal risk in the business;
- Identifies opportunities and develops the business to take advantage of these opportunities (entrepreneurial);
- Conducts business in the manufacturing sector, with particular reference to IPAP focus areas;
- Is a medium- to long-term investor with a long-term commitment to the business.

In addition to these characteristics, which also form part of the mandatory conditions for applicants, the following are required in terms of the mandatory conditions:

- The applicant must have a valid B-BBEE compliance certification;
- The applicant must be a taxpayer in good standing, with a valid tax clearance certification at assessment and before the grant is disbursed;
- The applicant must be involved in the day-to-day running of the operations with requisite expertise in the area;
- The applicant must have a project with a minimum investment of R30 million;
- The project should result in the securing or increasing direct employment.

While the emphasis is on companies with significant and dominant black ownership and control, it is acknowledged that there may be a need to include other shareholders to attract the relevant skills, finance and opportunities, and so some discretion is exercised in this regard. This means that in some cases companies can have less than 50% black ownership, although this is considered on a case-by-case basis.

[6] Department of Trade and Industry, Republic of South Africa. Black Industrialists Scheme policy document.

Furthermore, the policy targets entities that have experience, operations and a track-record in their respective or envisaged industrial sectors.

In terms of the economic sector criteria, and in line with sectors identified in various iterations of IPAP, only entities operating in the following productive sectors are eligible:

- Blue/Ocean economy, including vessel building and repair
- Oil and Gas
- Clean Technology and Energy
- Mineral Beneficiation
- Aerospace, rail and Automotive Components
- Industrial Infrastructure
- Information Communication Technologies
- Agro-Processing
- Clothing, Textiles/Leather and Footwear
- Pulp, Paper and Furniture
- Chemicals, Pharmaceuticals and Plastics
- Nuclear
- Manufacturing related logistics
- Designated Sectors for localization

Other manufacturing activities may be considered based on economic impact in terms of job creation, geographic spread and strengthening supply chains. Further, these sectors will be reviewed from time to time, in line with government priorities. Notable omissions from this list are the machinery and equipment sectors, and food processing, despite their potential for employment generation and upgrading of industrial capabilities.

4.2. Specific support measures targeted

The BIS proposes three measures of intervention: 1) access to capital; 2) access to markets; and 3) non-financial support.

4.2.1. Access to capital

The DTI works with DFIs to assist BIs with financial support, through concessional loans, investment grants and export market exploration support. Some DFIs have already come on board. Commercial banks have also shown interest to partner with government on this initiative. Moreover, the Black Industrialist Financing Forum has been established to facilitate syndicated funding for Black Industrialists. The DTI partners with other DFIs and commercial banks on a co-funding basis, with the DTI contributing in the form of a grant against which the BI can submit a claim. The other institutions typically contribute in the form of concessional loans repayable over an agreed upon period.

The DTI essentially offers a cost-sharing grant, specifically ranging from 30% to 50% of the approved funds up to a maximum of R50m. For example, if a company is approved for an amount less than (or equal) to R100m, say R90m, the DTI will contribute between R27m (30%) and R45m (50%) in the form of a grant, with the rest contributed by a co-funder. If the amount approved is greater than R100m, say R150m, the DTI will contribute between R45m (30%) and R50m, as the maximum contribution is capped at R50m, and not the 50% threshold amounting to R75m.

The exact quantum of the grant within these thresholds depends on the level of black ownership and management control (Table 1), the economic benefit of the project (Table 2), and the project value. There are no stated additional performance conditionalities or dynamic incentives associated with the programme.

Table 1: Ownership and Control Criteria

Points on Economic Benefit Criteria	Percentage Black Ownership		
	50% - 75%	>75% - 90%	>90% - 100%
4 to 6 points	30%	35%	40%
7 points	40%	45%	50%

Other factors that contribute to the points are economic benefits expected to be derived from the funding provided, as listed in Table 2 below. Each economic benefit criterion is allocated one point, with the Black Industrialist expected to achieve at least four points out of eight for an award.

Table 2: Economic Benefit Criteria

Benefit	**Description**	**Points**
Employment	Securing/retaining/increasing direct employment	1
Market share	Securing new business operations, and/or increasing existing business operations	1
Quality improvement	Reduction of relative prices and/or increasing the quality of products to consumers	1
Green Technology and Resource Efficiency Improvements	Savings or better utilization of energy or materials and/or cleaner production improvement and/or waste management improvement and/or water usage improvement and/or use of renewable energy	1
Localization	Increasing the localization of production activities (diversification and exports)	1
Regional spread	Projects should be located in rural areas or areas with unemployment higher than 25%	1
Personal risk	Demonstrate own financial and/or non-financial contribution to the business	1
Empowerment	Achieve at least a level 4 B-BBEE contributor status as per revised B-BBEE codes of good practice published in October 2013	1

The BIS offers cost-sharing grant support towards four key items: capital investment costs; feasibility studies towards a bankable business plan (to a maximum of 3% of projected investment project cost); post-investment support (to the maximum of R500 000); and business development services (to the maximum of R2m). The maximum grant of R50m may be fully utilized on capital investments or can be split between capital investment and other support measures (i.e. investment support, business development services and working capital). In this regard, the following costs are eligible:

Capital investment costs

- Machinery and equipment (owned or capitalized financial lease), tools, jigs and dyes and forklifts, at cost and will also include green technology, energy and resource efficiency equipment.
- Owned and leased (capitalized leased) factory buildings, at cost. The investment in qualifying buildings must either constitute newly acquired buildings or the acquisition of an existing building at cost. Building costs must be directly associated with the purchase or construction of a new production facility for the investment project under consideration, and must be located on land that has been zoned for either industrial, agricultural or commercial activity, with respect to buildings, will be based on the amount of the factory and administrative space utilized.
- Commercial vehicles (owned or capitalised financial lease) are only eligible if such vehicles are to be used for commercial purposes linked to the production process. This includes vehicles such as for collection, delivery and distribution of goods. Commercial vehicles must be registered in the name of the approved entity and must be in the asset register for a period of 3 years.
- Assets purchased from a connected party and business development services including feasibility studies and post-investment support sourced from a connected party are excluded from qualifying costs.

Investment support costs

Feasibility studies. The objective of this component is to offer support for project feasibility studies and related assessments that have a positive impact on the development aspects including job creation, skills development, as well as black business empowerment. The feasibility studies will include licenses, quality assurance, conformity assessments and standards. Furthermore, the appointed service provider for the feasibility studies must be sourced from the DFI's list of accredited service providers.

Table 3: Qualifying Investment Costs

Focus areas	**Categories**	**Consulting fees and expenses**
• Product development	Product design	Pattern-making, prototyping, grading, sizing and counter-sampling
	Product development	Introducing product ranges and product adaptations for new markets
	Conformity assessment of products e.g. testing, inspection, certification	Costs for conformity assessment of products
	Consumer acceptability studies	Marketing new products to focus groups before product launch to market
	Packaging design	Consultancy and design
• Conformity assessment certification	Quality management improvement, environmental management improvement,	Cost of installing or improving quality management systems; and costs for preparations for

	process capability improvement and product quality improvement	certification and pre/initial assessment costs
• Information technology systems	Acquisition and deployment of systems	Acquisition software for integrated production management information
• Procurement process improvement	Introducing improved and efficient procurement process	Cost of introducing new procurement process
• Patents costs	Registration of patents	Registration costs

In summary, access to capital forms the core target of the BIS, as evidenced by the broad variety of items prioritized, which is a critical milestone given the wide acknowledgment that access to funding is one of the barriers to entrepreneurship in South Africa. Importantly, and not notwithstanding the list of qualifying items above, the BIS lists several other items that do not qualify for funding. These include: salaries and wages; passenger vehicles (i.e. non-commercial vehicles) such as sedans, luxury 4x4s, SUVs and People Carrier Minibuses, even if registered in the applicant (entity's) name; VAT and finance charges on assets; rates and taxes; training that is not related to the manufacturing operations of the entity; staff wages and salaries, and staff related costs incurred in implementing any of the above projects; and costs incurred before approval.

4.3. Access to markets

The DTI works with various institutions to facilitate access to market opportunities for Black Industrialists, including with SOEs, government departments, chief procurement offices and private sector companies. This follows from cabinet approval of the BIP, which indicated that the DTI will work with the State-Owned Enterprise Procurement Forum (SOEPF) to explore market opportunities in government departments, SOEs and private sector. The DTI is leading this area of work and the process of amending the current SOEPF Memorandum of Understanding has been initiated. The objective is to establish a dedicated Black Industrialist State-Owned Enterprise Procurement Forum (BISOEPF) that will focus on facilitating access to procurement opportunities, both in the private and public sector.

Senior members from all SOEs are expected to participate in the forum to facilitate access to opportunities for BIs after careful consideration of capacity, skills requirements and due diligence of the proposals. SOEs are further expected to publish long-term procurement opportunities as per their demand management strategies. The forum aims to target procurement for local production, as well as facilitate access to domestic supermarket shelves when working with the retail industry and supermarket chains. Furthermore, the DTI seeks to champion engagements with the private sector to negotiate off-take agreements and enterprise and supplier development to strengthen and empower BIs.

4.4. Non-financial support

The DTI also aims to provide post-investment support. This includes specialized technical training and mentorship support. Technical training is provided in selected areas identified by the BI with the assistance of the DFIs. Mentorship guidance includes financial management, operations and production planning, human resource development, administration, marketing and business continuity. Additionally, the DTI aims to develop a suite of other non-financial support measures to increase the visibility of Black Industrialists. These include: a portal for networking and matchmaking; mentoring and incubation of Black Industrialists – the incubation programme of the DTI will be tailor-made for this purpose; and access to Black Industrialist support measures.

5. Assessing the design and implementation of the BIS

Outcomes and the design of the programme are assessed along several dimensions based on the publicly available data and interviews with government agencies, as follows: participation and take up; the funding forum; funding model; application criteria; access to markets; the range of other support measures; managerial and technical support.

5.1. Plausibility of the pre-conditions necessary to meet goals

The measures of success in the DTI and public discourse around the BIS have largely related to the number of industrialists that have been identified and supported, the jobs created by these firms, and the value of disbursements to the firms in the short period that the programme has been in place. These are of course critical measures of success given the challenges of opening up the South African economy to greater participation. However, it is just as important to assess the substance of support provided and the extent to which firms have been assisted sufficiently to establish and expand their businesses.

In terms of the early days of the programme, one of the key questions raised regarding the BIP was whether the DTI would be able to find and attract black industrialists given a history of marginalisation and concentration in the South African economy (NCOP, 2016). It is therefore unsurprising that there is some emphasis by the DTI on the fact that these companies have in fact been identified and supported through the programme.[7] While only 131 firms have been supported through the BIS by October 2018, it is significant that the programme has in fact identified a strong pool of established black owned companies (although some at relatively early stages of establishment), across different economic sectors, which have built capabilities over time and positioned themselves for further expansion through funding support from DTI. It is also notable that these firms are all involved directly in manufacturing activities which is critical to broadening the productive base in the South African economy.

Given this early progress, also recognised in terms of the numbers of jobs that have been created by some companies[8], it is an apt time to reflect on the design and implementation of the programme. This is important given that the BIS exists in the context of other funding and non-financial support initiatives for SMEs and BIs, including programmes to support smaller enterprises to grow their businesses – essentially creating a feeder pool for the BI going forward, other things equal. These issues are discussed in this section.

The target businesses under the programme are set out above. The specific criteria applied to select firms for award of the cost-sharing grants are also critically evaluated, in the context of the range of other programmes which exist to develop SMEs. Disaggregated data has not

[7] Inaugural Ministerial Black Industrialist Dialogue, 3 October 2018
[8] Inaugural Ministerial Black Industrialist Dialogue, 3 October 2018

been available to assess the nature of firms that have received awards, the sectors in which they operate, their ownership composition, and levels of disbursements.

A key question is whether there is a strong feed of manufacturing firms that can grow to apply for the BIS over time, or whether the BIS total beneficiaries will be limited by unavailability of the desired category of applicants. For example, the BIS generally considers relatively established businesses. It is unlikely that there are sufficient such businesses in the identified sectors given the overall barriers to entry discussed in the previous sections. Moreover, if the SEDA, SEFA and NEF programmes for incubating and funding smaller enterprises have a strong focus on firms in services and other non-manufacturing activities, then it less likely that appropriate applicants for the BIS will be sustainably produced or identified. This is not to say these potential applicants cannot emerge outside of government support programmes, however it is clear that the challenges of doing so are significant as discussed in the studies of barriers to entry.

Furthermore, while SEDA and other initiatives may support large numbers of SMEs including with training and business planning, there is a significant step up in terms of capabilities for a firm to be considered export ready, and capable of making large scale investments at the level that has been evidenced by the existing BIs under the BIS. As discussed below, the firms that have been supported under the BIS have been well established and 'ready' to expand their operations through the funding support.

A question which arises from the above is whether there is a structured, proactive framework in place for identifying potential BIs – the assumption being that having more (successful) applicants is desirable from the perspective of the overall economy despite the funding constraints that may be created. At this stage, there is no such framework in place. While some of the current cohort of BIs were sourced utilising existing relationships with other support initiatives, many of them were not proactively sourced. Furthermore, of those companies that have not received funding or support under the BIS, or other programmes of government for that matter, are there mechanisms in place to identify the primary and common reasons for why firms have been rejected and assisting them to reapply under the BIS and other programmes in future? This is important as some of the 'marginally' rejected firms may in fact be the next in line in terms of capabilities to apply under the programme in future.

There is a question about whether the programme may create dependency on government support on the part of BIs. In reality, all businesses regardless of ownership apply for funding from different sources to grow their businesses, especially where capital cannot be sourced from equity markets. Furthermore, it has been established through studies of barriers to entry that firms have struggled to obtain funds from commercial banks and in some cases DFIs, which means this failure in financial markets may leave businesses stranded in the absence of alternative support.[9] Lastly, to the extent that the BIs also receive co-funding at 'concessional' rates, this is not fundamentally different from the larger companies loaning funds from private equity or banks in that the loans are then paid back. The question is the level of risk perceived by different potential funders, where commercial banks and DFIs may make judgements against the perceived risk profile of the entrepreneur alone, including their personal credit history, notwithstanding the potential of the business project overall necessarily. These funding issues are discussed further below.

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[9] https://www.competition.org.za/competition-and-barriers-to-entry/

5.2. Funding Forum

An aspect of the establishment and design of the programme is the nature of the relationships held by the DTI with partner DFIs. This is primarily expressed through the funding commitments to the BIP which were initially made by different DFIs in the establishment of the programme (NCOP, 2016), as well as the fact that the DFIs also form part of the Black Industrialists Funding Forum (BIFF) which adjudicates applications. The BIFF consists of representatives of the major DFIs, which began as eight institutions with a view to assisting the DTI in the coordination and facilitation of the programme.[10] The role of the different funders is critical to the design of the BIS, as discussed below. It is worth noting here that in the adjudication process, funders make upfront commitments to support particular applications prior to approval – this is critical as it ensures that applicants, if awarded the (limited) DTI grant, are also able to access matching funding from DFIs to make the investments required.

The BIFF also plays a key role in building the rules for funding under the BIS and ensuring effective mechanisms are in place for due diligence and meeting of financing requirements by applicants, given the expertise of DFIs in this area. It is important to note, however, that the fact that the BIFF comprises funding institutions in adjudication may mean that applicants under the BIS are exposed to some of the same stringent criteria typically applied by private sector funders in processing applications by black owned firms and SMEs. There are also strong indications that firms have had to face the same challenges when applying to some DFIs directly (Bell et al, 2018a)), not least because of high financing costs and commercial risk standards as discussed below.

Data on the rejection rates under the BIS is not available to assess the number and reasons for rejection of applications under the BIS.

Despite the above concern, the BIFF has over time improved the rate at which applications are processed and the systems in place for doing so. In addition, the strong coordination and relationships between the DTI and BIFF partners are a positive aspect of the programme design, to the extent that the interactions help to address the challenges of coordination between government departments which have limited the success of several initiatives of government in the past.[11] As the BIFF involves the core funders, it also provides a platform for managing and sharing risk across institutions, which impacts on finance costs for firms and sustainability of the programme given the funding constraints that many DFIs also face in terms of being self-sustaining. However, the collaboration of funders potentially also removes any potential rivalry that may exist between different DFIs to 'win' attractive projects of applicant BIs that may be potential lucrative or successful, such as through lower finance costs offered.

5.3. The BIS funding model

As highlighted above, the scheme brings together funders to provide finance on a cost-sharing basis, with the DTI component provided in the form of a grant. The other funders typically offer loans to supplement what the Black Industrialists require. The DTI component is effectively used to de-risk the project/enterprise as a way of attracting other funders to come on board. Thus, Black Industrialists are likely approach the DTI first, before going to the DFIs for the remainder of the funding requirement. The other reason why qualifying industrialists are likely

[10] Interview with DTI, 16 October 2018
[11] See Minister Rob Davies' remarks, Inaugural Ministerial Black Industrialist Dialogue, 3 October 2018

to approach the DTI first is the simple incentive to avoid financing costs associated with other funders, whereas the DTI component is a grant that does not need to be repaid. Moreover, IDC's lending rates (IDC is the major co-funder[12]) are relatively high, even higher than those of commercial banks (Bell et al, 2018a), although this would need to be risk adjusted. This is as a result of three primary reasons: the IDC's finance is not subsidised; unlike with commercial banks, the IDC does not take deposits; and, the IDC largely borrows from the same commercial banks in order to on-lend.

However, the DTI's approved component is not disbursed upfront, but only after the investment is made. That is, the DTI uses a claims-based method of disbursement, where a Black Industrialist is required to incur the expenditure/investment first and claim for that amount afterwards. This assumes that Black Industrialists are able to source funds elsewhere to undertake investments before they are able to access the DTI funds, which may not always be the case especially as commercial lenders may consider these investors as being more risky (Bell et al, 2018a).

But even if one assumes that accessibility to funding elsewhere was possible, it still means extra and unnecessary financing costs for the Black Industrialist. Further, this creates a dilemma in the sense that the DTI support incentive ends up benefiting firms that could have managed to source funding elsewhere anyway, even in the absence of the scheme. In that way the DTI funding competes with other funding sources instead of supplementing them. Development finance by its nature seeks to crowd-in private financial sector funding, as opposed to crowding it out. The implication is that, by design, funding may end up escaping Black Industrialists who need it the most, in favour of those who could easily get it elsewhere. This is especially concerning given that DTI's resources are limited, as is clear from the R50 million cap imposed.

Furthermore, if it is not relatively easy to obtain funding elsewhere in a timely manner, opportunities may be lost in instances where investments are required to be made within a relatively short period of time.[13] For instance, where working capital requirements are high to meet expansionary projects or unexpected increases in orders, the process of having to source funds elsewhere before an enterprise can access DTI's funds may cause such opportunities to be lost. Moreover, the application process for funding from commercial banks and DFIs is cumbersome, with lengthy due diligence processes.[14] That is precisely the reason why private funding initiatives such as ProfitShare Partners are able to fill such gaps even in the presence of multiple government initiatives, as described further below.

ProfitShare Partners is a financial private company that provides disruptive funding solutions to businesses, particularly SMEs, with credible transactions, but who are unable to access capital or funding because they lack the financial history and security that is normally required by lending institutions.[15] This is because when it comes to accessing funds for immediate transacting to deliver on purchase orders and contracts, business owners often face serious risk due to cash flow constraints. More discussion on the lessons from the ProfitShare Partners model is provided below.

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[12] Standard Bank is the leading private sector co-funder so far (DTI, 2018).
[13] Inaugural Ministerial Black Industrialist Dialogue, 3 October 2018
[14] Presentation by Kevali Chemicals, 3 October 2018 - Inaugural Ministerial Black Industrialist Dialogue
[15] See ProfitShare Partners website

Initiatives like the ProfitShare Partners are able to make funding decisions and disburse funds within a relatively short period time (i.e. in less than a week).[16] This enables entrepreneurs to grab opportunities timeously and make the necessary investments. Lengthy application processes often cause companies to lose out on opportunities especially in situations where a company may need a breakthrough in a short period of time.[17] This is not to downplay the importance of a proper due diligence process, but to put more emphasis on the need for innovative risk-assessment tools, as already demonstrated by ProfitShare Partners' financing model.

Cap on grant financing available to BIs

The DTI has capped the amount that can be disbursed through a single application to a maximum of R50 million. Beneficiaries can apply to have the R50 million serve different purpose including machinery purchases, feasibility studies, business development services etc. However, given that these costs may in fact exceed the R50 million which is the maximum available from DTI, the BI effectively faces a choice in terms of what costs or projects to apply for (to fit within the R50 million) and which ones to omit, even though they may in fact be very important costs linked to the main investment required. Furthermore, given that firms in some industries may need funding for multilevel entry and investments to be an effective competitor, it is unlikely that the R50 million would be sufficient.

Moreover, the total budget for this programme is of course also limited, and may have only been sufficient to date because there is simply not many established Black Industrialists in the economy as yet. The question is whether there has been adequate rationing of finance. That is, it is expected that agencies such as SEFA and SEDA would be able to continue to broaden the base of potential Black Industrialists that could apply under the BIS. If this was the case, then it is highly likely that the current budget for BIS would fall short of requirements, and that the BIS would not be as impactful as it appears to be currently. Furthermore, there may be constraints in terms of the ability of the DFI partners to continue to match a growing pool of funding required under the BIS given several DFIs also face funding-model constraints of their own (including the requirement to be self-sustaining in terms of the funds disbursed and returns).

Nevertheless, it is also important to highlight that DTI grant is tied to a co-funder that is meant to top-up the shortfall occurs. Thus even though the R50 million may not be sufficient, the overall funding (including funding from other partners such as DFIs) extended to an industrialist may be able to cover the firm's requirements. Moreover, it is important to acknowledge that the BIS is still in the early stages of implementation, and therefore the programme may be expanded and refined with time and experience.

5.4. BIS criteria on firm expertise and existing operations

Other than the mandatory minimum requirements in the form of economic benefits and others listed above, the design of the BIS in terms of minimum qualifying value and sectors can appear to be exclusionary. For example, concerning the minimum value funded, the BIS only accepts applications to the value of R30 million or more, meaning all relatively smaller projects/enterprises are automatically excluded. Thus, the scheme appears to target relatively

[16] Interview with ProfitShare Partners, 01 October 2018
[17] Presentation by Kevali Chemicals, 3 October 2018 - Inaugural Ministerial Black Industrialist Dialogue

established medium sized firms as opposed to small and large firms. In the broader South African context where participation in the mainstream economy is a critical issue, the exclusion of small businesses in particular raises serious concerns, also raised in the initial stages of the BIP (NCOP Committee, 2016).

Further the emphasis on firms with existing operations means new entrants are excluded (although seemingly with some exceptions), which is problematic given historically low levels of black participation in the mainstream economy. This also goes against the BIS's own objective of accelerating the *quantitative* and qualitative increase and participation of BIs in the national economy.

However, the relatively established medium enterprises are likely to be more innovative and capable of making meaningful investments with high employment potential, as opposed to extremely small enterprises. Furthermore, given that the BIS is located within a range of other funding initiatives, new entrants and relatively small enterprises are expected to be catered for by other institutions (i.e. NEF, SEFA, SEDA, Department of Small Business Development, etc.). Thus, the BIS ideally targets enterprises that have already gone through other initiatives such as SEDA and SEFA, or those that through their own efforts have managed to grow their businesses over time.

This critical balance between initiatives depends on the different agencies and initiatives as a whole exercising their functions effectively and efficiently. It is doubtful whether this is the case, given that the there is still this overarching concern about the lack of growing, small and medium sized, black owned businesses in South Africa overall. These critical links between the BIS and other initiatives is assessed further in the second working paper titled "*What lessons and innovative solutions can be drawn from the experiences of new platforms and private initiatives in supporting SMEs and the growth of black business in South Africa?*"

With regards to the exclusion of much bigger enterprises, a similar argument applies. Larger firms with established market positions may face limited incentives to invest extensively, or innovate (Bosiu et al., 2017). As such they may require less support from government, which has expressed a focus on building small and medium sized enterprises in particular. Moreover there is still a significant gap in South Africa in terms of the number of large black owned enterprises in the economy (Bosiu et al., 2017), and in any event those companies could easily source funding from the private sector.

Sector specifications

The BIS targets industrial sectors in line with the IPAP. This is a critical issue given that South Africa has deindustrialised, as a result of low investments in productive capacity reinforced by a number of other factors including financialisation. That is, the tendency of financial and non-financial companies to invest in short term financial instruments as opposed to investments in increasing productive capacities in the real economy.

There is no real exclusion of firms based on sectors (although it could be argued that sectors such as machinery and equipment, and food products and processing should be included overall in the focus sectors) given the provision that other sectors will be considered based on other grounds including employment, for instance. Further, the acknowledgement that the South African economy is still reliant on the upstream industries that are still tightly linked to the minerals and energy complex (MEC) and finance, has increased the need to diversify towards downstream labour absorptive industries, as expressed in the IPAP framework.

5.5. Access to markets

One of the primary challenges for the BIS relates to opening up routes to market for beneficiaries. The challenges faced by firms in this regard have been canvassed in various studies as set out above. In terms of the design of the programme, the intention is that the BIS will assist beneficiaries to access markets primarily through state procurement levers, DTI export incentives and facilitation, as well as by assisting businesses to connect with one another and with private sector value chains.

The DTI has to this point found it difficult to facilitate these links. While there has been some success with assisting beneficiary firms to negotiate contracts with retailers, and through the export initiatives, this objective has not been achieved in a systemic way. Specifically while some firms have had success with this, there is no coherent strategy or framework for bringing on board retail and other private sector clients to contract with BIs. There has generally been no incentive to retailers and other large private sector clients to incorporate small and medium enterprises in their supply chains, or BIs specifically. One example given is that of Mthembu Tissues, a beneficiary of the BIS, which has had significant challenges with getting its various paper and tissue products onto the shelves of major retail groups. Where the company has gained access, it has largely been through supermarket house brands (which points to the adequate quality of the products), or in producing products for major household brands.[18]

Furthermore, the State Owned Enterprise Procurement Forum (SOEPF), which is meant to coordinate state procurement in this regard, has not yet performed at the desired levels.[19] The platform, which brings together procurement officers from different SOEs, has not been able to offer a coherent framework for engaging BIs. This partly relates to the financial and governance challenges that have faced many large SOEs in South Africa, and the likely effects of state capture and regulatory uncertainty in different organisations. Furthermore, the experiences of firms with SOEs indicate that there also irregularities and inconsistencies in payments, and at times particular procurement contracts may in fact be cancelled.

The DTI's post-investment office has started to track these concerns and has worked to assist firms with these challenges. However, at the core of the problem seems to be the lack of key partnerships with existing private sector businesses that have access to mass market and large contracts. In the absence of a proactive framework, large firms may leverage buyer power or control of value chains to undermine smaller entities. Intervention in this context may require a proactive, structured incentive framework and negotiations with large enterprises, rather than more ad hoc approaches. An important aspect to test through the further interviews and survey is the extent to which this concern is widespread amongst BIs and other SMEs, but also the extent to which it may be specific to particular economic sectors such as consumer goods retail.

These challenges are exacerbated by the significant expenditure required to build a brand and invest in marketing and advertising, particularly where companies have scarce resources of their own and need to trade off investments and financing for machinery and capital equipment, against the costs of building brands and marketing. Preliminary assessment of this issue from the interviews suggests that this is an issue across the different platforms and

[18] Interview with DTI, 16 October 2018 and Inaugural Ministerial Black Industrialist Dialogue, 3 October 2018
[19] Interview with DTI, 16 October 2018

funding initiatives that are available, and that the scale of the problem as identified through previous research has not been matched by the reach and capabilities of the interventions provided for under the BIS and other programmes.

5.6. Range of support initiatives

The BIS explicitly targets entities that have experience, operations and demonstrable track-record of operation, with the justification from the DTI being that experienced entrepreneurs would not be reliant on grants and that it was not viable for the DTI to "continually provide funds to agents that were likely to fail" (NCOP, 2016). This requirement appears to be exclusionary, on the face of it, to black owned businesses of a relatively smaller size with little to no experience in the sectors in which they operate. It is also a stringent requirement given a legacy of under-development of black businesses and entrepreneurs in South Africa. It is important though, to understand that the BIS exists alongside other support initiatives, all ostensibly with the aim of supporting SME and black business growth as stipulated in the NDP (National Development Plan, 2012).

Businesses go through several stages in their growth process, all of which require different forms of intervention. Interventions necessary at the ideation stage (where a business is simply just a concept) will not be the same as those required at the acceleration stage for scaling up of the business (ANDE, 2017). Several initiatives are in place to meet the different needs of SMEs at different stages, and as stipulated by the DTI, the BIS's existence within the range of other initiatives is to encourage black business participation at a larger scale than the small and micro enterprise. This appears to be tied with the potential for diverse, medium sized firms to make investment, contest markets, employ large numbers of people, and innovate to increase productivity. However, a more complete analysis of this aspect will be possible through using the survey data in the second phase, which will ascertain the size of firms that have been supported, amongst other factors.

Furthermore, there are certainly significant government initiatives and agencies that are in place to support different sized SMEs with different levels of capabilities and experience in business. This SME support includes financial support (some sector specific), incubation, mentorship and technical support as reflected below (Table 4), through agencies such as SEDA and NEF, and at provincial levels, amongst others. The NEF, for instance, provides both financial and non-financial support under its Pre-Investment Unit (PIU) and Post-Investment Unit (POIU).[20] Due to few businesses qualifying for financial support, the NEF identified the need to address a lack of 'bankability' of business ideas through incubation.[21]

SEDA, on the other hand, does not provide direct finance.[22] One of the objectives of SEDA is to de-risk entrepreneurs as a way to enable them to attain access to finance from other institutions such as SEFA, the IDC and the DTI. This is achieved through a range of support services such as incubators, business accelerator initiatives and mentorship.[23] Again the BIS can serve as a scheme that entrepreneurs link up with after having successfully gone through incubation in order to significantly contribute to the industrial base.

Table 4: Government support initiatives

[20] Interview with the National Empowerment Fund (NEF), 12 October 2018.
[21] Interview with the National Empowerment Fund (NEF), 12 October 2018.
[22] Interview with the Small Enterprise Development Agency (SEDA), 8 October 2018.
[23] Interview with the Small Enterprise Development Agency (SEDA), 8 October 2018.

Initiative	Focus area(s)	Type of fund	Lower fund threshold	Upper fund threshold
DTI Black Industrialists Scheme	Black-owned manufacturing businesses	Cost sharing grant	30% of approved funds	50% of approved funds, maximum of R50m
NEF Strategic Projects Fund	Black-owned businesses (early-stage projects)	Venture capital	-	R75m
NEF Non-financial Support	Black-owned businesses	Business incubation, technical support and mentorship	-	-
SEFA Direct Lending Product	SMEs and Co-ops in all sectors	Loans	R50 000	R5m
SEDA Technology Transfer Programme	Business ideas and struggling SMEs in the technology industry	Business incubation	-	-
IDC Black Industrialists Programme[24]	Black-owned businesses in all sectors	Debt and equity	R1m	R1bn

It is important then for support initiatives to work in complementary ways in order for the BIS to effectively fill its intended place. There appears to be graduation of small businesses between government initiatives, as well as from private initiatives such as the Black Umbrellas.[25]

The BIS is meant to serve as a scheme that can carry forward entrepreneurs that have graduated from pre-investment support (and attained considerable training and growth) to the next phase of their business life cycle in order to scale up and achieve productive efficiencies. However, there is need to assess the extent of referrals between initiatives and into the BIS. The key question is whether this network of support mechanisms is in fact working to deliver these outcomes across agencies, and whether the connections and feed between agencies is structured and proactive in terms of approach. It is also important to understand what the experiences of actual beneficiaries have been with different agencies and programmes, as considered in the broader survey and firm level interviews.

5.7. Access to managerial and technical support

Another specific support measure from the BIS is the provision of non-financial support. The aim of the non-financial support is to increase the visibility of the industrialist. Measures under

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[24] Black industrialists are drawn from the IDC's wider application base, fund thresholds therefore apply to all IDC funding applicants

[25] Interview with Black Umbrellas, 5 October 2018.

this form of support include a portal for networking and matchmaking, and tailor-made mentoring and incubation. Technical training is provided in selected areas identified by the BI with assistance of the DFIs, with funding commitments having been set aside to support this aspect of the scheme.

Identifying the relevant support (financial or non-financial) needed by a business requires a due diligence assessment, even when the entrepreneur highlights where they believe support is needed. Due diligence assessment is a costly exercise, requiring time, money and individuals with the relevant expertise depending on the sector.[26] However, the process also adds value as a kind of management consulting; where entrepreneurs get the opportunity to realise where exactly they lack capacity or expertise and necessary measures to address this can be taken with assistance from the scheme. DFIs such as the IDC stress the importance of the process, highlighting that the benefits of the process outweigh the lengthy time taken and costs to complete it.[27]

Non-financial needs of the entrepreneur are just as important as financial ones, and the same applies for the support that they receive to address these needs. Not only should there be coordination between government initiatives, but within initiatives as well. Clear matching of capacity and funding support is needed in order for financial assistance to be effectively realised. At this stage, it is not clear the extent to which the connections between the different government agencies are working effectively, although there are some indications that the DTI has leveraged these links to some extent for the BIS.

Engagements with national and provincial DFIs, SOEs and even the private sector have been a way to bring in other market participants to assist BIs with access to markets and access to support measures that may not be within the BIS.[28] Particularly with access to markets, an important measure taken by the DTI is establishing a relationship with SOEPF for BIs to explore market opportunities in government departments, SOEs and the private sector through a dedicated Black Industrialists State-Owned Procurement Forum (BISOEPF). However, this has currently not been taken forward as far as would be expected due to issues such as procurement legislation as discussed above.[29]

Lessons can also be drawn from private sector initiatives, some of which have managed to come up with structured approaches to non-financial support. Black Umbrellas, for instance, has implemented a five pillar programme encompassing training, pre-incubation, business ignition, further training, and networking and mentorship (including in-house enterprise development and systems tracking).[30] The mentorship and further training aspects have thrived from leveraging key relationships with other agencies and companies, including law firms and firms operating within the financial space.

However, it may be unsustainable to expect the BIS to drive each aspect of non-financial support as it may differ depending on the market a BI operates in. DFIs are perhaps well placed to do this because they have the necessary technical capabilities, although even then resources are already being committed to due diligence and post-investment support initiatives in the main. The requirements of businesses in this regard, although they are not

[26] Interview with the Industrial Development Corporation (IDC), 11 October 2018
[27] Interview with the Industrial Development Corporation (IDC), 11 October 2018
[28] Interview with the DTI, 16 October 2018
[29] Interview with the DTI, 16 October 2018
[30] Interview with Black Umbrellas, 5 October 2018

always best placed to determine what they actually need, will be considered in the second phase survey and interviews.

6. Outcomes and performance of the BIS

The intention of the BIS is to contribute to shifting the demographic composition of South Africa's industrial sector and to drive growth in areas such as employment, revenue and innovation. The scheme has shown some significant results in achieving some of its objectives, although it is still in its early stages of implementation. The performance of the BIS over the past three years is discussed below in relation to grant approvals, investment and employment.

6.1 Grants, approvals and investment

2017/2018 approvals highlight the potential of black industrialists and show substantially higher grants, projected new jobs and disbursements. The DTI received 69 applications in the year 2017/2018 of which 50 were approved (IDAD, 2018). The value of these grants was R1.4bn, up from R1bn the previous year (Table 5). However, important to note is that only R505.1m of these approved grants have been disbursed which may reflect the inability of firms to obtain matching funding from other sources, or deals not going through, or delays n project implementation as companies under the claims process are required to fund the required investments and claim the expenditure back from the DTI. This leaves just under R900m yet to be disbursed, which in turn affects the extent of projected outcomes in employment and investment.

Table 5: Aggregate BIS performance

	2016/2017	**2017/2018**
Projects approved	36	50
Value of grants	R1bn	R1.4bn
Projected new jobs	3 979	5 159
Baseline jobs	3 837	2 536
Disbursements	R122.5m	R505.1m

Source: IDAD (2018)

Agro-processing as well as chemicals, pharmaceuticals and plastics are sectors with the most approvals since the inception of the BIS (Table 6). The agro-processing sector has had a total of 15 approvals over the past three years. It also accounts for R413.9m in approved grants. The chemicals sector has seen an increase in approvals, from 6 in 2016/2017 to 11 in 2017/2018. Grant amounts for the sector as a proportion of total also increased from 18% to 21%.

Industrial infrastructure and manufacturing related logistics have also seen a significant rise in approvals along with mineral beneficiation, clean technology, and oil and gas. The BIS is beginning to show that strategic sectors targeted under IPAP are seeing increasing investment by black industrialists although the nature of projects and specific activities of companies would need to still be assessed.

The clothing and textiles sector is also noteworthy. With grant increases from 1% in 2016/2017 to 5% in 2017/2018, these may be strides displaying capabilities being built in a sector that has struggled to compete in previous years.

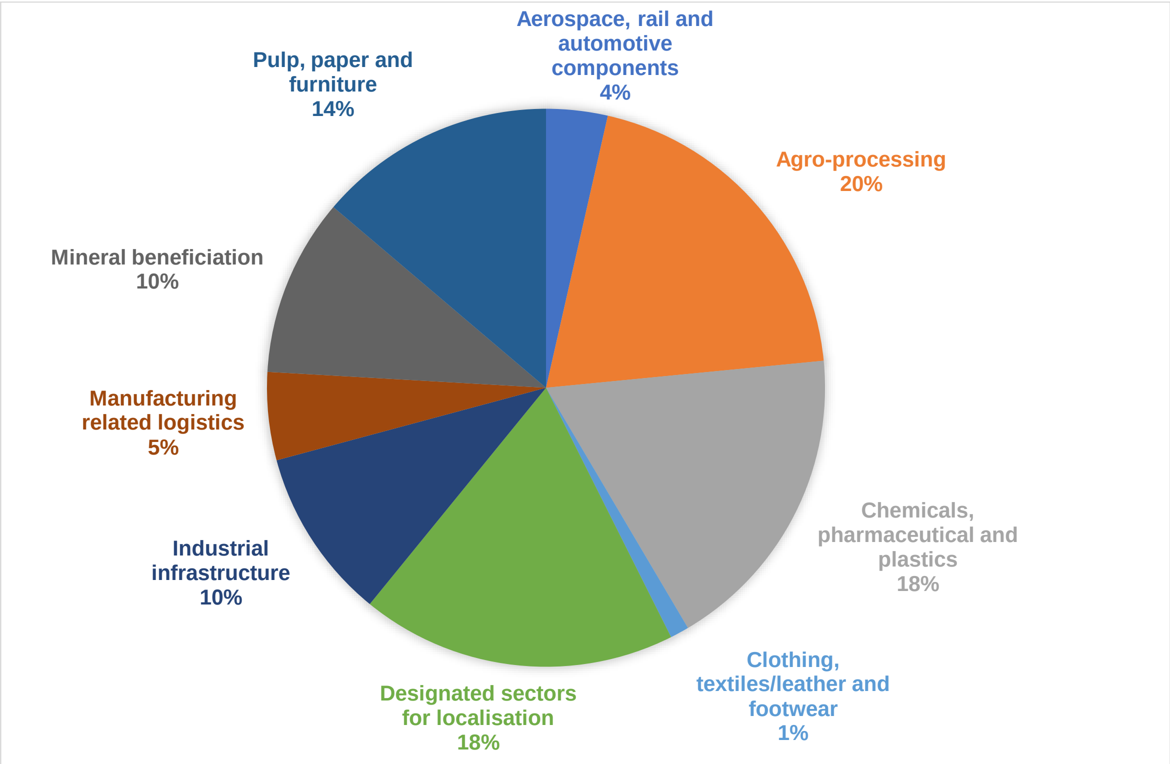
The IDC's Black Industrialist Programme (BIP) has approved R7.9bn worth of black industrialist support, noting that this programme has been in implementation for longer than the BIS. In addition, the IDC is still reversing a legacy of prioritizing upstream industries relative to more diversified and labor absorptive downstream industries, and is increasingly aligning its key projects with IPAP sectors.

Table 6: BIS Number of approvals per sector

Sector	Approvals	
	2016/2017	**2017/2018**
Aerospace, rail and automotive components	2	2
Agro-processing	7	8
Chemicals, pharmaceutical and plastics	6	11
Clean technology and energy		2
Clothing, textiles/leather and footwear	1	3
Designated sectors for localisation	7	2
Industrial infrastructure	2	5
Manufacturing related logistics	3	6
Mineral beneficiation	4	3
Oil and gas		5
Pulp, paper and furniture	4	3
	36	**50**

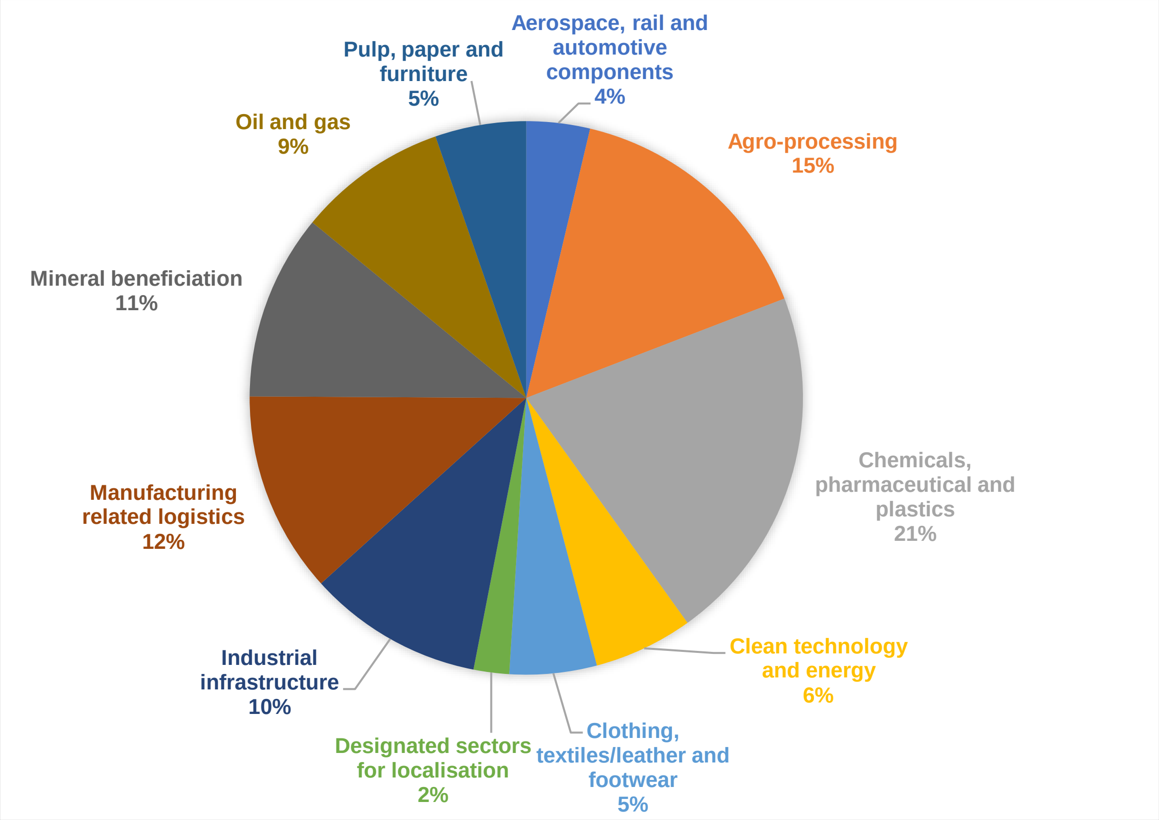
Source: IDAD (2018)

Figure 1: Grants per sector, 2016/2017



Source: IDAD (2018)

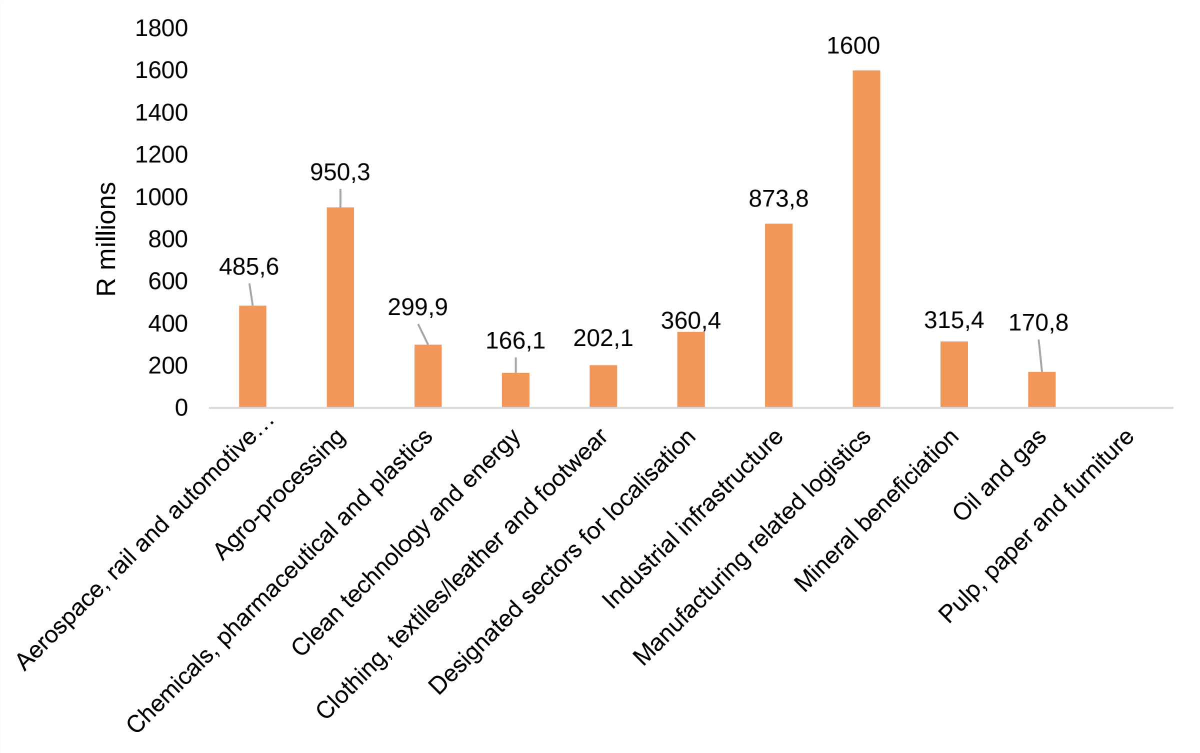
Figure 2: Grants per sector, 2017/2018



Source: IDAD (2018)

All sectors in which grants were approved have shown positive multiplier effects on investment. A simple multiplier effect on investment is calculated by the DTI from each approved grant. For the year 2017/2018, investment multipliers ranged between 2 and 10.7 across all sectors (IDAD, 2018). The average investment multiplier is 4, showing that on average, for every R1 provided as a grant to a black industrialist, an associated investment of R4 was made in the business (IDAD, 2018). However, the simple multiplier does not take into account any leakages or taxes. For this reason, it is difficult to conclusively assess the impact of the BIS on investments made in the businesses.

Figure 3: 2017/2018 projected investment



Source: IDAD (2018)

Manufacturing related logistics, agro-processing and industrial infrastructure are leading sectors in terms of expected investments made following disbursement of a grant. The investment multiplier for manufacturing related logistics was relatively high at 5.4 yet agro-processing and industrial infrastructure had associated multipliers of 2.3 and 2.5, respectively (IDAD, 2018). Mineral beneficiation had an investment multiplier of 10.7 despite an expected investment of R315.4m.

6.2 Employment

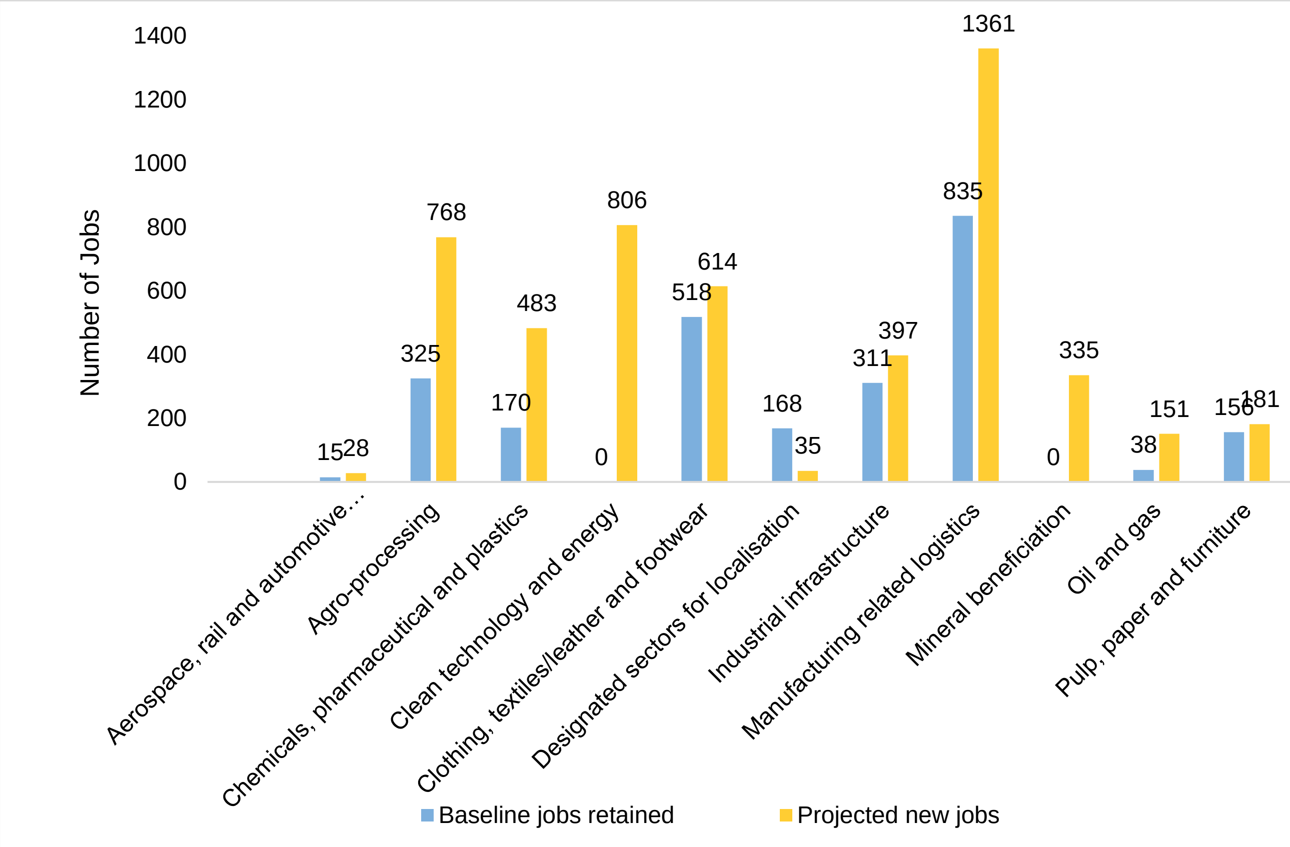
Increased employment is a key objective for South Africa and is highlighted in various industrial policy strategies including the criteria for the BIS. For a black industrialist to receive a grant, they need to show they will secure, retain or increase jobs following receipt of the grant as stipulated in the economic benefit criteria for access to capital.

In 2016/2017, the BIS approved companies accounted for 3837 baseline jobs and 3979 projected new jobs across the 11 manufacturing subsectors, effectively a doubling of existing employment. Projected new jobs for 2017/2018 grants increased significantly by 30% from 3979 to 5159.

The manufacturing related logistics sector had the largest number of projected new jobs of 1361 in 2017/2018, with a 12% share of approved grants. On the other hand, the clean technology and energy sector had the largest job impact between baseline jobs and projected new jobs with an increase of 806 jobs despite receiving only 6% of total grants for the same year. This may be due to the industry still growing, and resulting in faster employment generation (where activities are labour intensive) as companies expand.

The chemicals sector received the largest share of grant approvals for 2017/2018, but only accounts for 9% of total projected jobs; and performance of the agro-processing and mineral beneficiation sectors in terms of job creation has also been less impressive at 443 and 526, respectively.

Figure 4: Baseline and projected employment, 2017/18



Source: IDAD (2018)

Despite the short implementation time and relative to the number of approvals, the BIS has shown some significant progress overall in terms of grants, investments and employment. However, due to all approved grants not being disbursed, forecasted investment and employment numbers will not be realized in the near future. It will be important to establish why grants may not have been disbursed and whether this means they will not be disbursed at all. In addition, in assessing the performance of the BIS it will be important to test whether the forecasted figures based on grants have indeed been realized over time. The performance of the BIS is therefore heavily reliant on both the scale of industrialists that apply as well as the scale of disbursements against approvals.

7. Cross-cutting challenges facing Black Industrialists

The National Development Plan (NDP) states that SMEs should create 90% of the new jobs needed to bring unemployment to 6% by 2030, however there is still a lot to be done to ensure that SMEs are supported to grow and be able to compete in our economy successfully. While SMEs contribute nearly 98.5% of the number of formal companies in the economy, they only account for 28% of the jobs compared to the 60%-70% observed globally (Seed Academy, 2018). Thus, a supportive environment needs to be created to facilitate small business survival and growth in order to ensure increased, sustainable job creation (SA SME Fund, 2018).

The key barriers to entry and challenges facing business development in South Africa range from access to capital, access to markets, achieving economies of scale, government bureaucracy, onerous labour laws, to issues of skills and infrastructure (Banda et al, 2015; BER, 2016; Hawthorne et al, 2016; Makhaya and Nhundu, 2016; Ncube et al, 2016; SA SME Fund, 2018; Seed Academy, 2018). Moreover the application process for finance is cumbersome and tends to affect small and medium enterprises more, since established companies are able to make use of consultants to manage that process (Bosiu et al., 2017).

In this context, there are specific issues which have emerged from the interviews conducted and the BI Ministerial Dialogue which need to be assessed further through the survey and firm level interviews. This is important for assessing the extent to which the issues are specific to some industries or companies, or generally a concern across different SMEs and black owned businesses.

Working capital

The key issue raised by almost all the companies which presented is the challenges of working capital.[31] This component of overall capital requirements is very critical for small and medium companies since, unlike with large companies, they cannot afford to prolong operations without consistent cash flow.

For instance, the CEO of Kevali Chemicals, Mr Bongumusa Kunene, notes that large corporate customers tend to take too long to pay suppliers (as long as 120 days), partly because of their relatively high buyer power. The situation is the same with government entities, including a challenge of non-payment and cancellation of contracts by SOEs, for example. This suggest that reforms in this regard can actually address the cash flow challenges of BIs, rather than a focus on primarily funding large scale capital investments. Raw materials typically need to be ordered two months in advance, which often involves paying for them in cash because of lack/poor credit score especially for smaller players.[32] Then after converting raw material into finished products, they are transported to the customer, whom is then invoiced. It then takes period of time before the invoice is paid, up to 90 days,[33] which means smaller players effectively subsidise large corporations for close to six months. The problem of cash flow is further worsened by the bureaucratic processes of SARS. It takes time for SARS to effect tax refunds to companies.[34]

These challenges discourage entrepreneurs and lead to business exits from the market. When Kevali started it had 8 shareholders, currently only 5 are left after 3 dropped out due to challenges with cash flow and profitability.[35] To some extent, the IDC is able to bridge the working capital gap through its Revolver product. United Industrial Cables (UIC), a recipient of this facility, was able to go back to the IDC for working capital purposes, and the facility assisted them with raw materials, labour for production and other necessary consumables. According to UIC, the way the facility works is that when payments are eventually made, the IDC deducts whatever is due to them and pays the rest to the company.

[31] Inaugural Ministerial Black Industrialist Dialogue, 3 October 2018
[32] Presentation by Kevali Chemicals, 3 October 2018 – the Inaugural Black Industrialist Dialogue
[33] Presentation by United Industrial Cables, 3 October 2018 – the Inaugural Black Industrialist Dialogue
[34] Presentation by Africa Blaize Apparel, 3 October 2018 – the Inaugural Black Industrialist Dialogue
[35] Presentation by Kevali Chemicals, 3 October 2018 – the Inaugural Black Industrialist Dialogue

Cumbersome and lengthy application process

Linked to the issue of cash flow is the cumbersome and lengthy application process (i.e. due diligence) for funding. This often causes companies to lose out on opportunities especially in situations where a company may need a breakthrough in a short period of time. While the importance of a proper due diligence cannot be overemphasised, there is equally a need for timely decision-making. This can be mitigated by the establishment of a one-stop shop of funders that consists of industry experts to assist to shorten the decision-making process, which in some ways is what informed the design of the BIS as a 'central office' for funding access. Moreover innovative ways of conducting due diligence and assessing risk need to be developed, as opposed to the traditional methods typically used by commercial banks and DFIs.

Private funding initiatives such as ProfitShare Partners are already trying to overcome this challenge. ProfitShare Partners places more weight on the bankability of the project itself as opposed to overemphasis on the bankability of the individual, as is the case with commercial banks and DFIs.[36] The rationale is that if ProfitShare Partners can sufficiently mitigate risk on the project/transaction and not necessarily the client, then a return can be gained. However, it is important to note that ProfitShare Partners works with clients that already have contracts or tenders to supply, so the risk assessment dynamics will be different for start-ups with no signed contract, which is what DFIs mostly fund. Moreover, ProfitShare Partners does not fund projects in which it does not have control over the quality of the product being transacted, and these are typically in manufacturing and construction. This is an important distinction to make since the BIS primarily targets manufacturing enterprises, thus making its risk-exposure inherently different to that of ProfitShare Partners. Nonetheless, the important point to note is that there is a need to review the existing traditional methods of risk-analysis and their underlying assumptions, towards more innovative risk management mechanisms.

Access to markets

Small businesses are further faced with challenges relating to access to markets. Some BIs have pointed out that SOEs and other government entities do not implement government policy pronouncements such as those relating to procurement.[37] On the private sector side, it was noted that big private corporations are coming on board with supplier development programmes. This is in contrast to the view that there has been no progress in terms of integration into established value and supply chains, although the experiences of companies are likely to differ depending on the industries in which they operate, as will be assessed through the baseline survey.

The issue of access to markets has been highlighted by Black Industrialists. For instance, UIC has been struggling to reach end customers, such that their products have only been stocked by distributors. They are interacting with the DTI to explore opportunities with SOEs, especially since their facility is designed more for SOEs such as Transnet, Eskom, ACSA, etc.

Electricity, fuel and labour costs

Other challenges limiting business growth include high cost of electricity and fuel, and labour related issues. Representing the textile industry, the CEO of Africa Blaize Apparel Mr Sizwe

[36] Interview with ProfitShare Partners, 1 October 2018
[37] Inaugural Ministerial Black Industrialist Dialogue, 3 October 2018

Mbanjwa indicated that fuel levies have a huge impact on the company, and on the employees since most of them commute to work using public transport in the form of taxis and buses. He also highlighted that electricity costs and supply remain a huge challenge for the textile industry especially when running long shifts, also with effects on companies such as United Industrial Cables, in industrial cabling.[38]

8. Conclusion and preliminary issues for firm survey

It is challenging at this stage of the research, and given the constraints in terms of access to data, to draw firm conclusions on the progress and outcomes of the BIS. However, the assessment above has set out issues to do with the design of the programme and its implementation mechanisms which raise concerns, but also those which are positive from the perspective of providing support to BIs. It is clear, for example, that the issues around the funding can present difficulties for BIs, although it is also evident that the existence of a framework such as the BIFF has helped to facilitate a more sustainable funding approval process. The various issues, as set out above, will be tested against the actual experiences of beneficiaries in the different programmes in the next phase of research. This is important as the perceptions and representations by the different agencies interviewed, may not match with the reality faced by BIs in accessing support. This is precisely the purpose of conducting such a review – that lessons from the experiences of firms can be translated back into the workings of the BIS and other government initiatives, to improve outcomes in the economy overall.

The assessment in this first phase has raised a number of key issues to be considered further in the detailed firm level interviews and baseline survey of beneficiaries, as set out below:

- *Working capital* – there is potentially a need for a syndicated BIS facility to address this issue. This should be over and above the current capex facility. Lessons from ProfitShare Partners and the IDC's 'Revolver' facility can be drawn out to assess the potential in this regard.
- *BIS application process* – there is a need to understand the length and complexity of this process. Should the duration of the process be the same whether a company is applying for capex or working capital? This issue will be tested with respondents to the interviews and survey, to consider the extent to which it is a widespread challenge and the whether there are innovative ways of shortening and simplifying the process if necessary.
- *Co-funding model* – the design of the model is critical for deriving maximum benefit from the programme. The issue regarding the timing of disbursements and the claim-based model applied may create challenges for businesses that cannot access further funding to make investments. However, it is of course critical that DTI funding be availed for 'de-risking' projects, as long as there are firm commitments from DFIs to provide funding in a timely manner.
- *The BI Funding Forum* – the make-up of this is critical for efficient application process. It is important to determine how the application process is divided among funders, and who is responsible for conducting due diligence; as well as the potential for rivalry between the funders in 'bidding' to fund strong projects (which means favourable financial terms for the BI potentially).

[38] Presentation by United Industrial Cables, 3 October 2018 – Inaugural Ministerial Black Industrialist Dialogue

- *Access to markets* – it is important for the BIP to have a clear and structured programme to address market access issues. Interventions should not be ad hoc and a structured and proactive framework may need to be explored particularly in dealing with access to retail supply chains. There may very well be many BIs who are not reporting these issues, which the survey aims to assess.
- *Linkages with the State-Owned Enterprises Procurement Forum (SOEPF)* – Strong collaboration between this and the BI funding forum has the potential to unlock some important markets. Markets in government are low hanging fruit in terms of access to markets, although there have been significant challenges with this area in man sectors of the SA economy.
- *Linkages with other initiatives* – the success of the BIS is dependent on a close collaboration with other initiatives (government and private) such as SEFA, NEF, SEDA, Black Umbrellas, Incubators, etc. These have a potential to unlock a bigger pool of BIs to feed into the BIS, if there is a coherent framework for linking the activities of the different agencies in practice (not only in design as per the current policies).

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