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World Education Ntinga Ntinga LINK Programme

SECTOR SCAN REPORT on the South African Economy

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Executive Summary

World Education's planned Ntinga LINK initiative aims to test and demonstrate an emerging model for facilitating small enterprise growth and success via a strategy of market oriented Business Linkage services. With the overlay of a sub-sector framework – through which information and analysis of value-adding operations and business relationships within a targeted sub-sector are obtained – the programme will design interventions that promote the demand and supply of commercially viable Business Linkage services.

A first step in launching this initiative is to select a sector that has a high potential for success, keeping in mind the broader aims of the IGP in terms of targeting poor micro-entrepreneurs and going “down market.” This report has been commissioned to help World Education make an informed selection of a sector to be studied in-depth, via a sub-sector perspective and a market assessment of the demand and supply of key business linkage services.

To achieve its mandate, this document provides an overview of the South African economy, placing its performance and prospects in context. Utilising information from a range of secondary sources, as well as from key informants, this report scans the economy through an SMME lens, and highlights pertinent sector issues in relation to the role and potential of small, medium, and micro-enterprises. The choice of five specific sectors for more detailed exploration is influenced by factors such as sectoral growth prospects; current or potential involvement of small business; employment characteristics; and entry requirements among others. These factors all have a bearing on the proposed strategy and objectives of Ntinga LINK and its target clientele.

At this point, perhaps it is not premature to note that the Sector Scan process concludes that World Education would benefit by considering or exploring the *Construction* sector, or as a second option, the *Tourism* sector, for the implementation of its linkage facilitation intervention. In support of these suggestions, a comparative ranking is presented of the five main sectors per selection criteria described in World Education's proposal submission to USAID earlier this year.

This report is divided into three sections:

- **Section I** provides an overview of the South African economy, after noting the methodological constraints to the research process. It discusses the role of small, medium, and micro-enterprise in the economy, as well as explores the potent issue of BEE (Black Economic Empowerment).

It notes that SMMEs are by far the largest number of private formal institutions – in general, comprising almost 98% of all private sector establishments. Their contributions to employment are substantial – and very important in a country where the unemployment rate is over 30%. SMME contributions to overall GDP is also not negligible – and certain sectors show themselves as more heavily weighted in terms of the SMME component.

- **Section II** provides detail on the five selected sectors, in alphabetical order, as below:

(Primary) Agriculture:

While demand is growing, especially in key export markets, there has been an overall decline in agricultural production. This is exacerbated by post-apartheid issues surrounding land ownership and title. Uncertainty around government land redistribution policies is critical.

On the other hand, a sizeable proportion of the rural population do make their living from basic agriculture – often as subsistence or labour, so this is a sector via which poverty can be and should be addressed. However, the concentration of productive land in few hands, combined with the needed investments in technology for economies of scale, as well as the low skills level among the majority population, make agriculture a complex sector for facilitative interventions of the nature of Ntinga LINK. (There appears to be ver large linkages programme operating in this sector, which appears to have the benefit of substantial resources and is engaged in direct linkage promotion and deal-making.)

Construction:

This sector includes three main sub-sectors, namely building construction, civil engineering construction, and other. Public sector commitment to increase spending on infrastructure and low-cost housing initiative, together with recent private sector commitments to increased construction investment, contributes to the upbeat trend in this industry. The South African government is very cognisant of the role that construction starts can play in kick-starting the economy.

Given that 91.55 percent of firms in the construction sector consist of small and micro enterprises, there is vast potential for SMME growth and development in this sector. Individual working as independent contractors or small firms stand to benefit from sweeping changes in procurement policies, and the involvement of the public sector in increasing gross domestic fixed investments. Spatial development initiatives (SDIs) and Industrial Development Zones in several large municipalities, as well as tourism-related hotel and casino developments, hold promise of opportunity for business.

Clothing:

The clothing industry is very labour-intensive, and informal sector employment in clothing manufacturing is significant. Barriers to entry are low and SMMEs can enter the market with relative ease, compared to some of the other sectors. However the overall outlook is uncertain, given the reduction in protective tariffs, large-scale importation (both legal and illegal) of cheaper goods, and consolidation of the industry. The majority of micro and small enterprises in this sector feature primarily in the informal distribution of clothing, although there is considerable manufacturing potential – especially for small cut, make, and trim (CMT) firms.

Secondary Agriculture (Food Processing)

This sector accounts for 15% of the country's manufacturing sector. Although many of the 11 food processing sub-sectors are very labour intensive, they also required large capital investments into appropriate machinery and equipment, especially to keep processing up to hygienic standards. There is currently little knowledge on the SMME component of this sector, though those just initiating research estimate that the number of small firms is much higher than originally thought. For now, large firms predominate.

The competitive skills and technology requirements of this sector hinder the entry of SMMEs, as it is doubtful whether such enterprises can in fact exploit the opportunities that do exist.

Tourism

Although not considered a discrete economic sector until recently, tourism has the potential to be South Africa's largest employer, foreign exchange earner, and overall GDP contributor, according to some sources. While the sector is characterised by micro- or small firms (for example, B&Bs or little cafes), it is not necessarily amenable to 'poor' micro-entrepreneurs.. This is due to a range of requirements such as capital, information, communication skills, and services skills – which are currently in short supply among PDI firms. However, with the concerted effort by government and the private sector to market South Africa (i.e. the Proudly South African campaign is the latest in this line), as well as the favourable Rand exchange rate, it is likely that tourism will continue to grow in size and importance and absorption capacity. In fact, there is already a large-scale linkages programme operating in this sector.

- **Section III** basically reviews some of the sectoral SMME characteristics, and compares the five sector along key positive criteria and negative criteria. Among the former are: growth trends, SMME involvement, ease of entry for SMMEs, enabling environment, willingness of large firms to work with SMMEs. Negative criteria include factors such as fraud, corruption, poor policies etc; and, from an Ntinga LINK programme perspective, the existence of other Linkage programmes particularly ones that may be offering incentives or subsidies against which Ntinga LINK could not compete.

The ranking table is summarised below (full version available towards the end of the document).

TABLE 1

Ranking: 1 = low; 2 = medium; 3 = high (positive)

Criteria/characteristics	Primary Ag.	Construction	Clothing	Secondary Agric.	Tourism
Sub-sector Growth Trends (public, private and other levels of activity)	1	2.5	1	1	2
Proportion of PDI Small and Micro-Enterprises currently participating in the sector	2	3	2	1	2
Ease of Entry of Small and Micro PDI firms (incl. factors of capital; skills; technology)	2	3	2	1	2
Positive/ enabling regulatory environment	1	2	1	2	2
Degree of openness of large firms to working with smaller firms	2	2	2	1	3
SCORE	8	12.5	8	6	11

TABLE 2: REVERSE RANKING (Higher score indicates greater negative weighting)

Comparative intensity of negative factors – fraud, corruption, poor policies, capacity etc.	3	2	2	2	2
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Competition from other Bus Linkage Progs.	3	1	1	2	3
SCORE	6	3	3	4	5

Based on the above scores, the Construction sector clearly leads in terms of potential and prospects for a targeted, market-led linkages intervention. Spending and growth trends are positive, and the sector is characterised by a dominance of micro and small size enterprises, in both urban and rural areas, and a highly positive regulatory environment.

Tourism also scores positively on several points, but there is a question as to “depth” of outreach in terms of the micro-size enterprises or poverty related criteria. Also, a relatively small-scale World Education intervention could be overshadowed by a current, multi-million Rand Tourism Enterprise Programme (TEP) project.

Lastly, while both the construction and tourism sectors could provide an arena in which demonstrate a workable market development model for World Education Ntinga, it must be kept in mind that the South African economy – although sound in its essentials – appears prone to external shocks and perceptions over which it has little control. Afro-pessimism, combined with the global stock market downturn, could mean that promised foreign investment and inflows decline in coming months. Increasing inflation has been a concern to the Reserve Bank, and if this trend continues, an interest rate hike could adversely affect demand for higher-end construction products. Thus, the onus is on World Education to triangulate or otherwise cross-check key data in the course of its in-depth market assessment and sub-sector study in the coming weeks.

SECTION 1: The South African Economy and Small Business

Introduction

This section provides an overview of the South African socio-economic condition, as a prelude to detailing the key issues pertaining to the role of self employment (via micro and small enterprises). In many respects, the south Africa economy displays first world characteristics – the stock exchange was among the 10 largest in the world (before the recent London listings of several conglomerates); the communications, technology, and infrastructure availability is probably unsurpassed in Africa; and the government appears to have sound, if conservative, monetary and fiscal policies in place.

Against this backdrop, however, the country is confronted by a host of socio-economic problems that parallel, if not exceed, the magnitude of those in any other developing country. What sets South Africa's development issue apart is the dire threat and toll of the HIV/AIDS pandemic, as well as the massive skills deficit, which means that a large cohort of the currently working age population will never reach their full productive potential as they not have access to the various programmes that are coming on line. Large-scale unemployment – and unemployability – could portend unrest in coming decades, if not addressed soon.

The section also introduces the purpose and rationale for conducting the Sector Scan, noting some of the key considerations when trying to undertake cross-sectoral data tabulation and comparative analyses. Despite the difficulties of sometimes conflicting data, or differentiated presentations of the same information, the consultant has been fortunate in that considerable research and data are, in fact, freely available. The onus is on World Education to triangulate or otherwise cross-check key data in the course of its in-depth market assessment and sub-sector study in the coming weeks.

1. INTRODUCTION TO SECTOR SCAN REPORT

1.1 The Planned World Education Business Linkages Programme

World Education (South Africa) intends launching a sector focused business linkage programme in October of 2002. Funded by the United States Agency for International Development (USAID), this programme aims to mainstream micro and small businesses into the broader economy and to stimulate the provision of effective, commercially viable business linkage services by service providers. World Education has designed a programme that builds on key successes achieved under its original BDS Programme in the area of tendering access and performance and effective business linkages.

Known as Ntinga LINK, the new Business Linkages initiative is unique in that it will:

1. Operate along a well-defined model of “mainstreaming” micro and small business into an economic sector or industry that takes into account the differing demand and supply of specific business linkage support during a business’s developmental stages. These include: readiness to compete, competition, performance, sustained access, and growth of an enterprise.
2. Initially identify and work in one promising sub-sector of the economy, taking into account the entire value chain, the nature of business relationships, and the enabling environment in a particular industry or sub-sector.
3. Achieve micro and small business impact via a network of select private and non-profit service providers who will be supported and skilled in designing and delivering effective, appropriate, and affordable business linkage services to the micro-entrepreneurs – as well as the larger players (business and government) in the chosen sector.

Within the overall context of Black Economic Empowerment (BEE), Ntinga Link plans to achieve the end goal of access to business opportunities for up to 5,000 firms (of which 75% will be PDI-owned¹ micro-enterprises). This will be done through a combination of research, training, technical assistance, and information-sharing inputs that will improve supply of quality BL services and enhance demand for the same among the community of emerging entrepreneurs and service providers.

Key objectives of Ntinga LINK are to:

- Stimulate the provision of value-added Business Linkage services by supporting providers to develop and market commercially viable services to a range of clients, including but not limited to micro and small businesses.
- Catalyse demand and use of Business Linkage services by unblocking key informational or environmental constraints that prevent access and informed use of such services by micro and large businesses.
- Track the benefits realised by PDI micro-businesses and key provider performance areas so as to develop and test an effective, efficient, replicable market-based model for

¹ PDI (previously disadvantaged individuals) – refers to the Black, Coloured and Indian race groups who have been disadvantaged by apartheid.

promoting commercially viable Business Linkage services to PDI micro-enterprises within a range of industries or sectors.

Delivery under the new Business Linkage programme is due to start in December-January. In the preceding months, World Education Ntinga has planned to:

- Conduct research to identify the most promising sub-sector for intervention, which is the object of this report.
- Carry out an in-depth sub-sector study and assessment of the markets for BL-focused Business Development Services among various sector players
- Identify and introduce potential partners to the programme
- Examine high-potential interventions in areas such as compliance, labour-service brokering, materials supply, joint venture planning and management, project management, procurement systems design and management, etc.
- Identify and communicate with key stakeholders within the chosen sub-sector – including associations, federations, local and provincial government, and large corporates.

The new programme expects to operate in the provinces of Eastern Cape, Gauteng, KwaZulu-Natal, and Mpumalanga. This Sector Scan Report forms part of the research phase of the proposed new business linkage programme.

1.2 Sectoral Research And Analysis In The South African Context

The purpose of this document is to provide an overview of the South African economy, placing its performance and prospects in context of the recent past, emerging trends, and the imperatives of the immediate future. In the process, the document provides snapshots of key sectors or sub-sectors of the economy – which may have particular relevance to the strategy and objectives of Ntinga LINK, and its overall aims and target clientele.

By utilising information from a number of reputable secondary sources, as well as from key informant interviews,² this report scans the economy primarily through the SMME³ lens. In selecting the escorts for more detailed exploration, the choice was influenced by factors such as growth prospects for the sector; current or potential involvement of small business in the sector; employment characteristics; and entry requirements; among others.

However, it must be noted, that a complicating factor when attempting to draw comparisons and conclusions within his report is the fact that there is no standard definition or agreement on the sectoral breakdown of the economy. The various statistical and census-related data that are collected by various government and other agencies, including the main ones such as Department of Trade and Industry (DTI), the Industrial Development Corporation (IDC), Stats South Africa, the Ntsika Enterprise Promotion Agency, and the South African Institute of Race Relations (which publishes an annual socio-economic survey), offer differing interpretations of what specific economic activities fall into a specific sector.

2 . A Bibliography of secondary sources is attached. A database of the key informants is available.

3 . SMME in South Africa refers to Small, Medium, and Micro-enterprises. (For definitions, see.....) This report, as a consequence of the Ntinga LINK emphasis, attempts to draw out those factors most relevant to the role and performance of the lower end of the scale – namely, the micro and very small enterprises.

To illustrate, the Industrial Development Corporation in its *Sectoral Prospects* (1997) lists 31 different economic sectors, -- while Ntsika in their *Small Business Review* (2000) mentions just 9 sectors, which defined quite differently from the IDC.

An important governing document -- the South African Skills Development Act No 97 of 1998, promulgated under the Department of Labour -- provides for the establishment of 25 Sector Education & Training Authorities (SETAs). Since many of the SETAs are yet to conduct comprehensive and up to date research on their respective sectors, it is unclear what the overlap or gaps between their definitions and content are as compared to the existing research data.

Thus, this report has had to rely on putting together related information from a number of different sources who appear to have undertaken the sectoral or economic research in a piecemeal fashion and with a very specific focus in mind.

Another difficulty in the carrying out of sectoral analysis is in attempting to unravel the various domains of the different sectors. For instance, tourism is an economic sector or activity that cuts a range of other sectors. Tourism requires services and inputs or purchases outputs from the construction sector; from the secondary agriculture/processing sector; from various manufacturing sectors, and various services. Thus, trying to tease out those activities or values that apply specifically to one sector from those that may be the conglomeration of work across sectoral boundaries is neither simple nor always possible.

That said, in broad terms, the mere fact of the availability of basic data and information on key economic indicators is a major plus. The documentation, and subsequent clarifications, have enabled the consultant to present a broad framework and approach to understanding more about the performance of South Africa's economic sectors, within the context of the shifting national policy environment, emerging enterprise structure and size characteristics, and the overall globalisation trend.

This report, if used as a basis to inform further in-depth study that sets the stage for Ntinga LINK's targeted interventions, will have fulfilled its purpose.

2. AN OVERVIEW OF THE SOUTH AFRICAN ECONOMY

2.1 Geography and demography

With a population of some 43 million, and a diverse natural landscape covering some 1.22 million square kilometres, South Africa is possibly one of the best placed African nations in terms of current living standards and potential for economic growth and development. About 63% of the population is between the ages of 15 and 64 years, with 32 percent being under 15.

Taking indicator averages, South Africa is a middle-income country with an abundant supply of resources, well-developed financial, legal, communications, energy, and transport sectors, a stock exchange that ranks among the 10 largest in the world, and a modern infrastructure supporting an efficient distribution of goods to major urban centres throughout the region.

However, these averages obscure the true distribution of wealth and economic access among the different population groups, as the distribution is so skewed in favour of the minority white population. In fact, approximately 57% of the South African population is estimated to be living in poverty. Economic growth in recent years has not been strong enough to cut into the high unemployment, and daunting economic problems remain from the apartheid era, especially the problems of poverty and lack of economic empowerment among the disadvantaged groups.

The population is classified along four main groups with African/blacks constituting 78%; whites – 10%; 'Coloureds' – 9%; and Asians – 3 %. Together, the African, Coloured, and Asian/Indian groups are referred to as PDI – previously disadvantaged individuals – a term that helps establish differing policies and government and private efforts to address the inquiries in the country. The proportion of women to men is slightly higher – 52% to 48%. In terms of socio-economic factors, the best off group of the population would be white males, with African females ranking at the lowest end of the scale.

Table 1: Portion of Population that is Economically Active (in millions of persons)

Population Group	African	White	Coloured	Asian	Total
Youth and Elderly	11.33	0.94	1.20	0.29	13.77
Other not economically active	10.12	1.57	0.99	0.35	13.03
<i>Of the economically active, those who are...</i>					
- Employed in Formal Sector	4.81	1.68	0.95	0.27	7.72
- Employed in Informal Sector	0.93	0.18	0.19	0.10	1.40
- Unemployed	4.23	0.09	0.30	0.05	4.67
Total	31.42	4.48	3.63	1.06	40.58

Source: Population Census 1996, SSA; Employment Series, De Lange and Viljoen 1996; OHS 1996, SA In State of Small Business in South Africa, 1998 Review, DTI / NTSIKA

Arguably, the impact of the HIV/AIDS pandemic is this country's greatest threat to national development, as the death rate is increasing, the population growth rate is declining, and the generations in their most productive years are the most negatively affected. According to official

estimates, some 20% of the population is living with HIV, although in some circles that percentage is deemed to be considerably higher.

The country is divided into nine provinces, each with its own provincial administration and with differing characteristic in terms of population size and (racial) breakdown; natural resources and land availability and quality; and GDP and poverty levels. The more well-resources and better performing provinces are Gauteng, the Western Cape and KwaZulu-Natal. The poorer least resources are Limpopo and Eastern Cape.

The country's average population growth rate of 2% per annum, is showing a decline with the toll being exacted by the HIV/AIDS pandemic. As of 1999, the Department of Health estimated that 17% of the population was living with HIV – a figure that is placed considerably higher by other sources.

2.2 Economic Indicators

The Growth, Employment and Redistribution (GEAR) macro-economic strategy forms the foundation stone of the country's basic economic policy. GEAR is frequently described as 'conservative' or 'neo liberal', and proposes creating conditions for sustained economic growth and for rapid expansion of employment opportunities. Central to GEAR is the reduction of fiscal deficit, a monetary policy aimed at curtailing inflation, the opening of the economy (for instance by relaxing exchange controls), and stimulating new investment, especially by the private sector.

2.2.1 Gross Domestic Product (GDP)

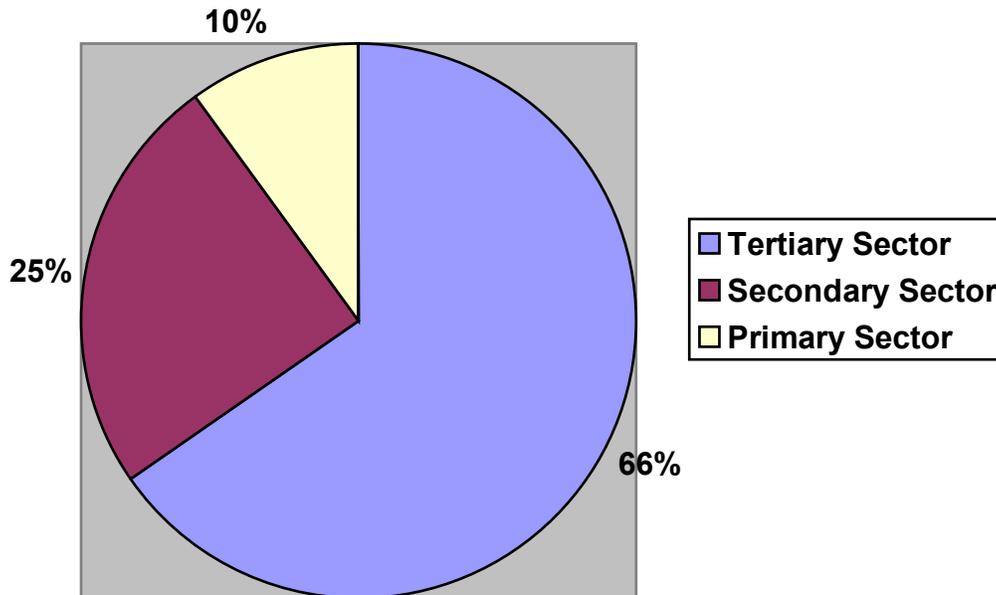
In 1999 the South African economy grew by 1.9% in real terms, which was more than double the 1998 rate of 0.7%. The official projected figure for 2000 was 2.4%. The Gauteng region's gross domestic product was some R 349 bn in 1998 -- equivalent to 42% of South Africa's total GDP (at current prices) in that year. The 2000/01 budget made provision for net government expenditure of some R 243 bn, equivalent to 27.5% of GDP.

South Africa's economy has changed considerably over the past decade, most notably in respect of the decline in contribution of the primary sector (agriculture & mining) to gross domestic product (GDP), and an increase in the relative size of the tertiary or services sector.

Among important structural changes to South Africa's economy have been the increases in tourism since 1990; and the expanded provision of water to communities, that were formerly without adequate supplies, which has had a range of largely positive consequences. The transport, storage, and communications sectors have grown rapidly (as a result of the expansion of the taxi industry), as have the provision of communications infrastructure in under serviced areas, and information technology generally.

Inflows of foreign capital, investment in South Africa helped expand the country's financial and business services considerably. The informal sector also expanded and was estimated to make up about 7% of GDP by the end of the 1990s and to provide employment to some 1 million people.

Figure 1. Proportional contribution of economic sectors to GDP: 1999



(Note: Tertiary sector = services, Secondary sector = processing/manufacturing, Primary sector = agriculture & mining)

2.2.2 Unemployment and Inflation

One of the biggest challenges facing the South African economy today is that of structural unemployment. South Africa's unemployment rate was 23.3% in 1999 according to the official or 'strict' definition of unemployment. The expanded unemployment rate was 36% in 1999, a small improvement compared with 1998 (37.5%)⁴.

Between 1998 - 1999, total employment in the formal non-agricultural sectors of the economy fell by 3.7%. This trend continued into 2000, with figures released by Statistics South Africa showing that a further 63,635 jobs were lost between March and September 2000. However the 1999 October Household Survey shows that the underlying employment creation capacity of the economy may be somewhat understated by these figures.

From the 1940s to the end of the 1960s, inflation tended to be fairly light, varying between 1.4% and 9.8% although typically remaining in the lower end of the range. Between 1974 and 1992 it was consistently in double figures. Since 1993 the inflation rate has declined steadily, scoring 5.2% in 1999. (with a similar projection for 2000). The South Africa Reserve Bank adopted inflation targeting as a policy, setting desired levels of inflation to be achieved within particular periods.

However there has been a rising inflationary trend since 2000, largely due to adverse weather conditions (1999/2000), the depreciation in the Rand/dollar exchange rate, and the increase in international oil prices.

⁴ SA Institute of Race Relations (2001), South Africa Survey 2000/2001, SAIRR

2.2.3 International Trade and Exchange Rates

The value of the Rand dropped by some 20.49% against the US dollar during 2000, reaching a record daily average low of R 7.845 to the dollar, in November that year. In 2001, the Rand was further battered, sinking to R 13.85/\$ in December, losing almost 37% of its value against the dollar. It has subsequently regained about 20%, and is currently trading at slightly over R10 to the dollar. Naturally, such severe exchange rate fluctuations have implications for the economy with export sectors benefiting in global price terms, but imports (particularly oil/petroleum) being negatively affected.

The value of South African exports in 1999 was some R 174 bn, and that of imports R150 bn. The World Economic Forum attributed South Africa's increased competitiveness in 2000 (compared with 1999) largely to creativity and innovation in the economy despite the prevalence of a poor education system, a skills deficit, and high unemployment. The deficit on the current account of the balance of payments narrowed from R 12.9 bn in 1998 to R 3.4 bn in 1999. (from 1.8% of GDP to 0.4%). South Africa's credit ratings improved during the period under review and South Africa was generally seen as an 'investment grade' country.

Globalisation has also effectively changed the way the world does business. While the sheer volume of trade has increased remarkably over the past few decades the composition has shifted to favour high value-added products. Since 1995 the World Trade Organisation (WTO) has championed the liberalisation of world trade, entailing a substantial reduction in tariffs and non-tariff barriers and extending rules to include trade in services and ideas.

The African Growth & Opportunity Act (AGOA) enacted by the United States could provide major export opportunities for South African manufacturers, particularly in the clothing and agriculture sectors (e.g. exports of fruit) AGOA related exports are expected to generate R 14 billion to SA's gross domestic product this year- up from R 10 billion in 2001.⁵

2.3 Summary Economic Indicators

The table on the following page provides key economic indicators for the year 1999, the latest year for which definitive figures are available.

⁵ Business Times, 18 August 2001.
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	1999	1998
GDP (at current prices)	R 795. 58 bn	
Real GDP growth at market price	1.9%	0.7%
Agriculture etc (3.4 % of GDP)	3.4 %	7.3%
Mining etc (6.1% of GDP)	-1.0%	0.8%
Secondary Sector (24.7% of GDP)	-0.3%	1.0%
Manufacturing (18.8% of GDP)	-0.2%	1.6%
Tertiary sector (65.8% of GDP)	3.3. %	2.3%
GDP per capita	R 18,576.00 (Down 0.3% on '98)	
Gross domestic savings as a proportion of GDP	14.6%	14.3%
Gross domestic fixed investment (GDFI)	R 121.24 bn	
GDFI as a proportion of GDP	15.2%	16.8%
GDFI by public authorities (constant prices)	Down 5.1% as of 1998	
By public corporations	Down 18.3% as of 1998	
By private business	Down 3.6% as of 1998	
Inflation rate	5.2%	6.9%
Food inflation rate	4.9%	6.2%
Producer Price Rise	5.8%	3.5%
Value of merchandise exports (including gold)	R 163.18 bn (Up 10.6% on 1998)	
Real prime overdraft rate	12.12%	13.96%
Average exchange rate	R1=\$0.16	R 1=\$0.18

3. THE ECONOMIC CONTRIBUTION OF SMALL, MEDIUM, AND MICRO-ENTERPRISES (SMMEs)

This section provides an analysis of the role that the small, medium, and micro-enterprises play according to their absolute and relative contributions to the economy.

3.1 The role of SMMEs

Most available official data indicate that there are around 1 million enterprises in South Africa. Of these, only 2% are medium and large – with the remaining 98% being micro and small, and accounting for 45 – 50% of all private sector employment .

Under the prevailing definitions in South Africa:

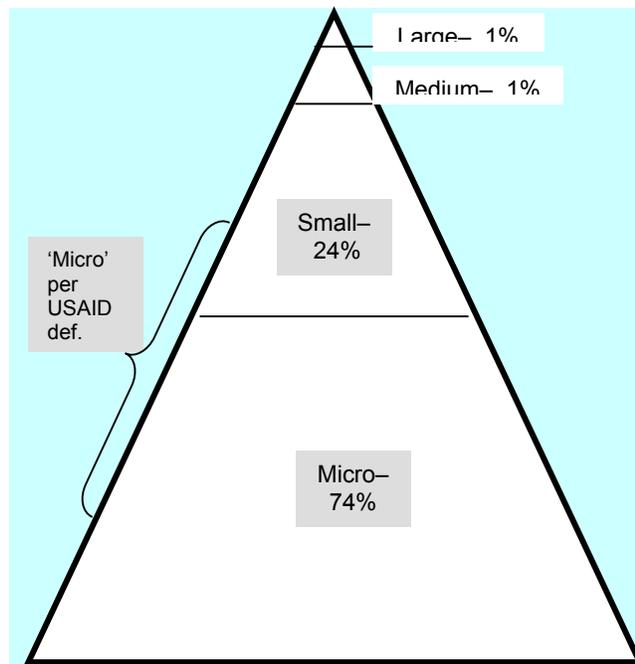
- A micro-enterprise is one which has fewer than 5 employees, and is very informal in nature, not registered nor paying any taxes or dues. It's turnover is less than R 150,000 annually (approx. US\$ 15,000 at current exchange rates.)
- Small enterprises are constituted of “very small” (5 to 19 employees) and small (up to 49 employees), and are usually somewhat formalised in terms of registration, though not necessary in operations.
- A medium enterprise may have up to 100 employees (200, in the case of mining and certain other industries)
- A large enterprise has in excess of 100 employees.

In terms of the USAID definition of micro-enterprises -- firms with up to 10 employees, and owned/headed by the poor -- there would be an overlap between the two smaller size categories in South Africa, that would constitute the target clientele for the World Education Ntinga Business Linkages Programme. (See right.)

In terms of economic activity, the largest proportion of enterprises (some 33%) are engaged in retail trade – with micro and small firms making up nearly 100% of this number.

Other sectors where micro- and small enterprises are dominant include:

- Agriculture: Nearly 100,000, of which 56% are micro, and 39% are small
- Services: More than one-tenth (100,000) of all enterprises, of which 99% are micro and small.
- Construction: Some 90,000 enterprises of which 81% are micro and 18% small.
- Manufacturing: Also more than one-tenth, with 62% being micro, and 34% being small.



3.2 Sectoral Distribution of SMMEs

(Formal & informal businesses)

Table 1: Overview of Private Sector Size and Distribution

Characteristics	Micro ⁶	Small ⁷	Medium	Large
Definition (# of employees/ enterprise)	Less than 5	5 – 19, or 5 – 49	50 – 100 50 – 200	> 100 or > 200
# of enterprises per category	> 650,500	240,000	12,000	7,000
#s employed (in millions)	1.03	2.37	1	3.1
% share of employment	15%	31%	12%	43%
Number & % of enterprises per sector	650,500	238,900	11,322	6,017
- Agriculture	54,500 56%	38,800 39%	3,240 3%	1,520 2%
- Catering & accommodation	11,300 50%	10,050 46%	385 2%	124 1%
- Community, Social, personal svcs.	72,800 81%	33,300 18%	525 1%	388 0%
- Construction	71,600 81%	15,600 18%	996 1%	320 < 1%
- Finance & business services	48,200 52%	28,900 37%	301 <1%	425 1%
- Manufacturing	65,300 62%	35,400 34%	3,840 5%	1479 4%
- Mining	3,600 81%	631 14%	112 3%	137 3%
- Retail trade (incl. Motor trade)	265,200 82%	56,400 17%	970 < 1%	744 < 1%
- Transport	50,600 86%	7,600 13%	293 1%	303 1%
- Wholesale trade	7,400 35%	12,170 59%	660 3%	577 3%

Source: South Africa Survey, 2000-2001

While various data sources may not agree on the exact number or percentage breakdown among SMMEs, they do agree that SMMEs are by far the largest number of private formal institutions – in general, comprising almost 98% of all private sector establishments.

However, it is at this point, that agreement on actual numbers and distribution appears to disintegrate. Per the table above, it is in the retail trade, services, construction, and manufacturing sectors that micro-and small enterprises are particularly large in number.

6 . For brevity, the “micro” column combines data on: survivalists, micro with no employees; and micro with up to 4 employees.

7 . Similarly, the “small” column combines data for : “very small” (1 – 19 employees) as well as “small” (up to 49 employees).

Data from another source, and using slightly different sector divisions, indicates that micro-sized institutions are dominant comprising approximately 67% of all institutions. Approximately 66% of all micro-sized enterprises are either trade, transport, business or other services. The construction sector tends to consist mainly of small enterprises, while agriculture tends to be medium sized enterprises. (This last is in sharp contrast to data in the preceding table – underscoring a clear need for very detailed primary research into whichever sector World Education Ntinga decides to intervene.)

Table 2: Percentage contribution of SMMEs to the number of establishments per sector

	MICRO	SMALL	MEDIUM	LARGE	TOTAL
Agriculture	24.88	28.35	40.96	5.82	100.00
Mining	57.89	18.98	7.24	15.90	100.00
Manufacturing	61.27	18.92	14.11	5.70	100.00
Electricity	0.00	0.00	0.00	100.00	100.00
Construction	24.50	67.05	4.84	3.61	100.00
Trade	82.57	14.59	1.75	1.09	100.00
Transport	64.66	28.39	5.34	1.61	100.00
Business Services	84.99	13.03	0.99	0.99	100.00
Other Services	89.25	8.95	1.02	0.77	100.00
Average. all sectors	67.41	19.35	10.74	2.50	100.00

Source: Ntsika 2000

3.3 SMME Contribution to GDP

On average, 34.8% of GDP is generated by SMMEs and 65.2% by large enterprises. Sectors where SMMEs contribute more than 40% to GDP include agriculture, construction, trade and transport. It is in the construction, trade and transport sectors particularly, where the role of small and very small enterprises is significant – much more so than that of medium sized enterprises.

Table 3: Percentage Contribution Of SMMEs To GDP per Sector.*

	MICRO	SMALL	MEDIUM	LARGE	TOTAL
Agriculture	4.13	8.67	43.71	43.49	100.00
Mining	1.01	1.74	2.55	94.70	100.00
Manufacturing	5.27	7.37	21.02	66.34	100.00
Electricity	0.00	0.00	0.00	100.00	100.00
Construction	3.14	35.60	12.20	49.06	100.00
Trade	2.27	23.41	17.12	57.21	100.00
Transport	7.07	18.50	20.30	54.13	100.00
Business & Other Services	14.90	12.90	2.90	69.30	100.00
Average - all sectors	5.82	13.90	15.05	65.23	100.00

Source: Ntsika 2000

*Note: total real GDP for 2000 is estimated to be approximately R 565 000 million.

3.4 SMME Contribution To Employment

Irrespective of the importance of SMMEs in terms of their contribution to GDP, arguably their biggest single contribution to the South African economy is in terms of employment. Currently employment in the formal, non-agriculture, private sector is estimated to be approximately 2.6 million people -- while the informal sector employs a further 2.7 million people.

The role of SMMEs as an agency for employment in South Africa cannot be overemphasised, especially within the context of a developing nation. The contribution of SMMEs to employment in the respective economic sectors is portrayed in Table 2. SMMEs employ 57% of all formal, private sector enterprises, compared to 43% in large enterprises.

Table 2: Proportional Distribution of Employment by Sector and Size

	MICRO	SMALL	MEDIUM	LARGE	TOTAL
Agriculture	7	43	19	30	100
Catering & Accom	10	48	12	29	100
Community, soc, personal svcs	20	44	6	31	100
Construction	22	30	15	33	100
Finance, bus svcs	12	34	3	51	100
Manufacturing	5	23	23	49	100
Manuf & Quarrying	1	2	4	93	100
Retail trade	30	33	5	33	100
Transport	30	27	8	36	100
Wholesale trade	30	27	8	36	100
All	15%	31%	12%	43%	100%

Source: South Africa Survey 2000-2001

Viewed within the respective sectors themselves, micro and small enterprises account for more than 50% of sectoral employment in the catering, services, construction, trade and transport sectors. SMMEs contribution to employment is much higher within each of these four sectors than for small enterprises as a whole. The small enterprises in these four sectors are comparatively more important in terms of employment.

It is clear that the dominant size class cohort in each sector differs to the characteristics of the specific size of enterprise and of the sector. It is these features and natural trends that should be kept in mind when deciding on policy or programme options that promote the development of micro, small, or medium enterprises in the various sectors.

3.5 SMMEs and poverty

Vast socio-economic disparity among South Africa's major population groups is an undeniable fact. Ten percent of the population is largely constituted of wealthy, well-educated, well-resourced whites. The majority "PDI" population – consisting of Africans (77%) Asians (2.5%), and Coloureds (8.7%) – is characterised by much lower levels of wealth, education, access, and opportunity.

The micro- and small business sector is populated primarily by PDIs (which equate with the poorer sections of the population) -- a feature consistent in comparison to other developing countries, where the majority of micro businesses are also constituted of the poor.

Of all PDIs, it is the African segment that has had the least access to services and opportunity, generally of very poor quality, and strict limitations on where and how they could participate in economic activity, under apartheid. The legacy of this system is evident today. For example:

- Using example of income distribution or Living Standards Measures – in 1996, 99% of those at LSM 1 (the lowest in terms of income and consumption) were Africans, while 79% of those at LSM 8 (the highest) were white.
- In addition, some 60% of South Africa's population (23 million people) live in poverty⁸ -- which primarily affects PDIs.

Thus, arguably, in the South African context, one can quite easily equate micro/small entrepreneurs with poor/previously disadvantaged. Recognising the implications of this is critical both to current efforts by public and private sector in South Africa to “level the playing field” – and to the design, targeting, and success prospects of the World Education Linkages programme.

The next chapter provides an overview of the push to redress this skewed distribution of resources, skills, and access – through black economic empowerment and support for “affirmative” business enterprises.

8 . Average monthly living level of R 431 for a single-person household to R 1,840 for an 8-member household..

4. BLACK ECONOMIC EMPOWERMENT – AND WHAT IT MEANS FOR BUSINESS

'The domination of business activities by white business and the exclusion of black people and women from the mainstream of economic activity are causes for great concern for the reconstruction and development process. A central objective of the RDP is to deracialise business ownership and control completely through focused policies of Black Economic Empowerment.'

'These policies must aim to make it easier for black people to gain access to capital for business development. The democratic Government must ensure that no discrimination occurs in financial institutions. State and parastatal institutions will also provide capital for the attainment of BEE objectives. The democratic Government must also introduce tendering out procedures, which facilitate BEE. Special emphasis must also be placed on training, upgrading and real participation in ownership' (RDP paragraph 4.4.6.3)

4.1 The Impetus behind BEE

The words above, from the Reconstruction and Development Programme (RDP), South Africa's blueprint for transformation, encapsulate the vision and values of Black Economic Empowerment (BEE). However, several years after the advent of majority rule, and despite significant achievements by government on many fronts, the vision articulated in the RDP has not been realised.

Most studies suggest there has been virtually no change in the overall inequality in wealth distribution, and that that black people remain in poverty and marginalised from ownership, control and management of economic resources. This crisis is seen by many to be hindering South Africa's growth prospects and its competitiveness as a nation.

The idea of a BEE Commission (BEECom) arose out of a resolution taken at the Black Management Forum (BMF) National Conference in November 1997. The prevailing view at the Conference was that black people should direct and take charge of a new vision for BEE, a process that, until then, had been conceptualised, controlled and driven by the private sector (which is still mainly white controlled).

Thus, BEECom was established in May 1998 under the auspices of the Black Business Council (BBC), a body representing 11 black business organisations. BEECom's objectives were:

- To investigate and analyse the BEE process through empirical research into the pace and results of BEE initiatives during the 1990s.
- To draw conclusions as to the obstacles to meaningful participation of black people in the economy.
- To develop a strong case for an accelerated National BEE Strategy and make recommendations on policies and instruments required to guide a sustainable strategy.
- To develop benchmarks and guidelines to monitor the implementation of the National BEE Strategy.

After conducting extensive research and wide-ranging consultations, BEE Com held a conference in September 2000. The views of these and subsequent discussions with stake-holders were incorporated into a report.

The BEE discussion document contains recommendations that call for significant changes in the way South Africans do business. It also makes suggestions on ways to accelerate economic growth and deepen transformation.

4.2 BEECom Recommendations

The BEECom proposed the adoption of an Integrated National BEE Strategy comprising guidelines and regulations that provide clear targets and demarcate roles and obligations pertaining to the private sector, public sector, and civil society over a period of 10 years or more.

The Strategy, according to the commission, should incorporate the supporting institutional arrangements and an oversight body -- the National Empowerment Commission (NEC) -- which would report to the Presidency and relevant cabinet clusters.

The key components of the Integrated National BEE Strategy include:

- An Investment for Growth Accord between business, labour and Government aimed at reaching agreement on a concrete strategy to lift the country's levels of fixed investment and economic growth.
- The design and implementation of an Integrated Human Resources Development (HRD) Strategy.
- A National Procurement Agency located within the Department of Trade and Industry aimed at transforming the public and private sector procurement environment.
- A National Black Economic Empowerment Act - Enabling Legislation to create uniformity in policy and establish institutional support and instruments to drive the BEE strategy. The Act should define BEE and set uniform guidelines that facilitate de-racialisation of economic activities in the public and private sectors.

Defining Black Economic Empowerment

The BEE Com decried the tendency to equate Black Economic Empowerment with the development of a black capitalist class. Such a definition focuses on the entry and transaction activities of black people in business, primarily through BEE investment companies.

The consequence has been an inadequate response to the limited inclusion of black people in meaningful economic activities. The growth of the black middle class and the black business strata since 1994 has been far from spectacular. There has been a marginal increase in the number of black managers in the private sector over the past seven years and barely any evidence of black people in controlling positions in capital (with the exception of the public sector).

The broader definition, around which the Commission anchored its research, argues that the fundamental crisis in the South African economy is that black people remain excluded from financial and economic resources.

BEE Com defines BEE as "*an integrated and coherent socio-economic process. It is aimed at redressing the imbalances of the past by seeking to substantially and equitably transfer and confer the ownership, management and control of South Africa's financial and economic resources to the majority of its citizens. It seeks to ensure broader and meaningful participation in the economy by black people to achieve sustainable development and prosperity.*"

Accordingly, BEE strategies should increase access to productive assets whilst ensuring the productivity of those assets. BEE should seek to promote new opportunities for and increase the levels of participation of black people in the ownership, management and control of economic activities. Strategies should support individual enterprise, as well as social and collective capital.

- An Empowerment Framework for Public Sector Restructuring that outlines empowerment principles to be followed.
- An enabling framework to improve access to finance for households and businesses through disclosure and reporting requirements in the banking sector and targets to encourage service delivery and the enhancement of existing State capacity in the Post Bank.
- Recommendations on the streamlining and co-ordination of public sector funding initiatives through a National Empowerment Funding Agency (Nefa).
- Recommendations on building the capacity of business structures especially black business structures.

4.3 Recommended Targets – and the implications

Within a 10-year period, the BEECom proposes several targets to be achieved, including **at least:**

30%	...of productive land to be in black hands, including individuals and collective enterprises
25%	... black equity participation in each sector of the economy. ⁹
25%	...of shares of JSE listed companies held by black people
40%	...of directors of companies listed on the JSE to be black
50%	...of parastatals and government procurement to go to black firms
30%	...of these firms should be black-owned small, medium, and micro enterprises
30%	...of private sector procurement by companies with more than 50 employees should be from black-owned companies, including SMMEs
40%	...of senior and executive management in private sector companies with more than 50 employees to be black.
40%	...of people in the professions and in professional training to be black, under the aegis of the National HRD strategy.

The government is presently considering the recommendations of the BEE Commission and an appropriate process is to be agreed upon to take forward the development of this integrated plan.

The imperatives and the implications BEE targets – and the possibility of their legislation – is transforming the way that big business operates in South Africa. Some sectors or firms, apparently more prescient than their peers, have already put in place their own strategies and targets – particularly in relation to out-sourcing, procurement, and skilling of black staff or associates. Yet, for these, the difficulty lies in matching their quantitative and quality requirements for goods and services with the availability and ability of SMMEs to provide those.

Demand for services or interventions that might make the BEE achievements of big business – and the access to those opportunities by SMMEs – easier and less costly, is likely to increase steadily in the foreseeable future.

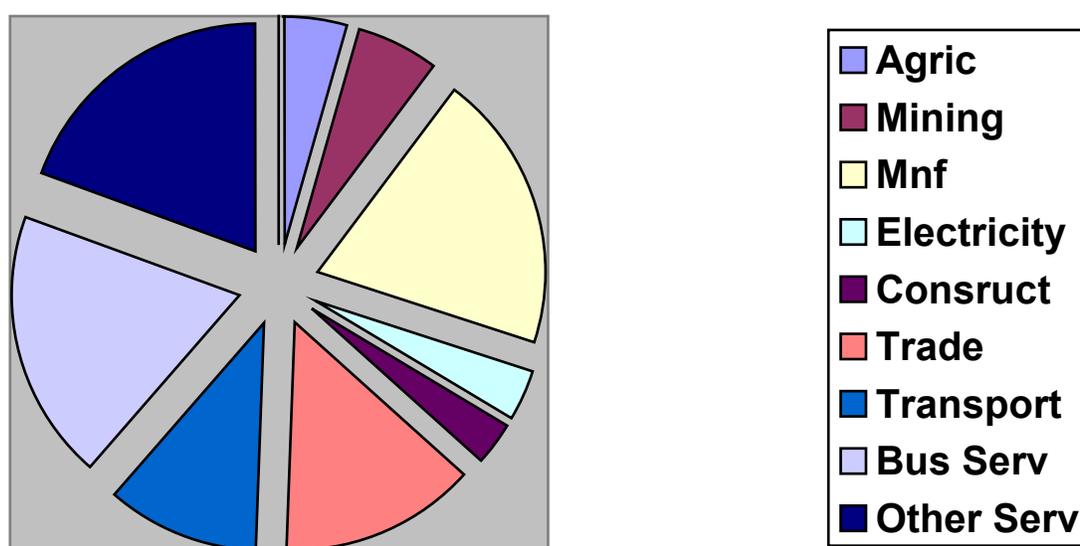
9 . Where equity is near 25%, efforts to be made to increase the equity by an additional 25%.

SECTION II - SECTOR SCAN

Introduction

The economic structure of the formal sector in South Africa seems to resemble that of many industrialised or developed countries. The chart below compares nine main industrial sectors to each other in terms of their contribution to GDP (Gross domestic Product).

*Figure One: Sectoral Contribution to GDP
(Shows the contribution of each sector to GDP after the third quarter in 2000)*



Primary		Secondary			Tertiary			
Agriculture	Mining	Mnf *	Electricity	Construct-ion	Trade	Transport	Bus Svcs	Other Svcs
4.4%	5.9%	19.8%	3.6%	2.8%	13.9%	11.0%	19.0%	19.5%

* Includes range of value-adding activities, ranging from agro-processing to high-technology component manufacture.

Source: South African Reserve Bank Quarterly Bulletin, December 2000.

South Africa's tertiary or services sector contributes 69.9% to GDP of which the largest single contributors are business and other services, including the public sector (19% and 19.5% respectively) and to a lesser extent trade & transport, (13.9% and 11% respectively).

Following the large tertiary sector is a well-developed manufacturing sector. This is the single largest sector in the country, contributing 19.8% to GDP. Unlike the other developing countries, the contribution of the primary sector (agriculture & mining) is very small namely a total combined contribution to GDP of 10.3%. The total real GDP for 2000 is estimated at approximately R565,000 million.

Selection of Sectors for Study

Based on a number of key characteristics, five sectors of the economy were selected as worthy of further study in relation to their possible targeting for interventions by the planned World Education Ntinga programme. The characteristics considered included features such as contribution to GDP and/or employment; growth trends in expenditure, production, and/or employment; and the relative contribution or dominance of small, medium, and/or micro-enterprise firms within these sectors.

The sectors that are explored in some detail on the following pages are:

- **Agriculture** - which includes forestry and fishing.
- **Construction** - includes three sub-sectors, namely, building construction, civil engineering construction and other construction activities
- Manufacturing, under which we look at the overall performance of this sector and examine two sub-sectors in more detail namely:
 - **Clothing**; and
 - **Secondary agriculture** (processing)
- **Tourism** – which was previously not recognised as a separate sector, being incorporated into Trade, Catering and Accommodation or Business and Other Services. However this has changed with the establishment of the Tourism and Hospitality Education & Training Authority (THETA) and the recognition of the importance of the tourism inflows to the economy.

5. AGRICULTURE - Primary

5.1 Description

This economic sector or “industry” includes:

- farming, landscape gardening and production of organic fertiliser;
- agricultural services, excluding veterinary services;
- hunting, trapping and game propagation;
- forestry and logging; and
- fishing.

This sector contributes 3.7% to the national GDP, is responsible for 4.5% of the economy’s exports, and 12.2% of direct employment (852 000 people)¹⁰. Despite its relatively small contribution to GDP, the influence of agriculture on the overall economic conditions is key, as fluctuations in production cause wide-ranging effects in a number of other sectors – not least through price inflation and the cost of raw materials/inputs.

Additionally, through forward and backward linkages, primary agriculture is pivotal to the existence of sectors such as food & beverages, chemicals, manufacturing, energy and many more. The traditional division between agriculture and foodstuffs tends to cause a distortion of agricultural statistics as an increasing amount of value is being added close to farm level and imports of many value added products such as rice, certain oilseeds and chicken products, for example, may not be reflected in the figures for this sector.

Economies generally grow by shifting human and capital resources out of the primary sectors (agriculture, mining), first into the industrial/manufacturing sector and later into a services sector. This has also been the case in South Africa, where the transition to a post-industrial age is well under way. Yet there is evidence that, in this process, agriculture either failed to reach its full potential or did so in a distorted manner resulting in large numbers of people being excluded from the benefits of modernisation.

The reasons for this are rooted largely in the policies of the apartheid past. For instance, as with many developing countries, South Africa’s rural areas are characterised by high levels of poverty. Incomes are constrained because the rural economy is not sufficiently vibrant to provide them with remunerative jobs or self-employment opportunities. Yet, the agricultural sector is especially important to the rural population, a large proportion of which are dependent on it for their livelihood.

It has been argued that if the South African economy had followed a different, labour intensive, inclusive, and non-discriminatory development and settlement path in the past, rural poverty would not have become such a pervasive feature of the present society and economy.

South African commercial agriculture has followed a very capital-intensive growth path, while significant agricultural resources (human and material) lie unused or under-utilised in the former homeland areas. Both these factors have affected the income-earning potential of rural people.

For one, the entrepreneurial abilities of Black farmers were suppressed, by their exclusion from the commercial land market and because commercially viable freehold farming was almost impossible

¹⁰ Sectoral Prospects: 1997-2001, IDC: Riaan Coetzee & Theo Janse van Rensburg 1998
September 2002

in the former homeland areas. Furthermore, this development path has meant that upstream (input firms) and downstream (processors of food and fibre) industries relating to agriculture were stunted, therefore depriving rural people of economic opportunities.

These factors together were largely responsible for creating the extreme dualism and inequality in agriculture. This dualism has created a polarisation that has resulted in an approach to policymaking and service delivery that focuses on two agricultures — one for commercial farmers and one for so-called 'emerging farmers' -- rather than for a single unified sector.

Employment opportunities in commercial agriculture were and still are largely limited to unskilled, low-wage labour, and a large share of total employment in commercial agriculture is of a seasonal and temporary nature only.

5.2 Demand

Demand for a number of agricultural products is growing fast, although this tends to be masked by its inclusion in other sectors such as meat products, eggs, dairy products, fish and other marine products. Due to much higher prices abroad, production of deciduous, tropical, citrus, and sub-tropical fruits, flowers and vegetables is increasingly geared to supply the market in Europe. Albeit from a low base, the demand from the Middle and Far-East is increasing.

Despite competition from other Southern hemisphere countries such as Chile, Australia, New Zealand & Argentina, exports of the above-mentioned perishables are growing at more than 10% per annum. Exports to Europe, the main market, are still encumbered by high import tariffs and other non-tariff barriers.

Deciduous and citrus fruit exports have recently been fragmented due to deregulation, and price fluctuations have occurred. There is, however, again a strong tendency for the formation of umbrella export organisations. This should lead to more stable prices. Of total agricultural production, 13% is exported while, of the balance, 24% is consumed by households, 21% goes to the meat processing industry, 9% to the agricultural industry itself and 7% is consumed by the grain mill production sub-sector.

The demand for marine products as well as forestry products remains high. Over 60% of roundwood goes into pulp, paper and board. The country is self-sufficient regarding requirements for forestry and saw milling products. South Africa remains one of the 20 largest producers of forestry products in the world.

5.3 Supply

South Africa is largely self-sufficient many food products. The agricultural sector is normally able to provide for most of the needs of our growing population apart from imports of oilcakes and fish meal for broiler, egg, dairy and pork production as well as rubber, cotton, rice, vegetable oils and barley for the beer industry. Rising input costs such as fertilisers, pesticides and fuel are causing shrinking margins for many products.

The institution of minimum wages is contributing towards a challenging labour relations environment for the agricultural sector. The wage levels in the tea and certain other industries are six to eight

fold higher than in competing countries. A new law which guarantees residential rights to farm labourers, could further prompt the farming industry to increase mechanisation and reduce employment.

The high cost of liming soil, due to the abolishment of government subsidies, is cause for concern due to the chemical erosion of the soils over a large part of South Africa, causing decreasing yields of annual crops. The area under irrigation cannot be expanded much further, apart from a few areas in Northern KwaZulu-Natal and the former Transkei. Dryland production of annual crops is subject to seasonal climatic variations as most of South Africa is semi-arid with high fluctuations in rainfall.

Despite a number of disadvantages, production in South Africa nevertheless enjoys a number of competitive advantages, which are expected to accelerate exports further.

These include:

- sophisticated road and shipping transport handling systems,
- a wide range of climates,
- advanced technical support as well as labour and management training.

Ongoing capital investments ensure increased competitiveness on the world market. These include:

- more mechanisation,
- improved handling facilities,
- redevelopment of irrigated areas for the production of high value crops,
- co-operative manufacturing of packaging materials,
- provision of hail nets and covered areas of production,
- other value adding structures such as local abattoirs and food processing.

5.4 SMME Component

The agriculture sector tends to consist mainly of medium sized enterprises as can be seen from the table below.

	MICRO	SMALL	MEDIUM	LARGE	TOTAL
Agriculture	24.88 %	28.35 %	40.96 %	5.82 %	100.00

However, employment or labour absorption capacity is not very high, given the current levels of unemployment and the size of the rural population. Figures provided by the Primary Agriculture Sector Education & Training Authority (PAETA) show that that the primary agricultural sector employs:

- 20 000 people on a permanent basis in the commercial sector; and
- a further 300,000 on a contract and seasonal basis.

These employees work on 60 000 farming units which implies that the average farming enterprise is very small; on average 10 to 15 persons per enterprise. It is further estimated that there are more than 1.2 million people who work and live on sustainable farms.

For micro-enterprises, prospects in this sector appear to be scant, partly because of high start up and operating costs and because of skill shortages in all but the fishing sub sector. However the uneven distribution of fishing licenses is problematic for the fishing industry. Subsectors such as timber harvesting and saw milling appear to lie beyond the technical and financial competence of

micro-enterprises ¹¹.

¹¹ Review of Sectoral Opportunities for MSE Growth, Micro Enterprise Alliance, (June 2000),
September 2002

5.5 Constraints

Sector challenges include the following 12:

- **Global Competitiveness And Low Profitability.** Indications are that the South African agricultural sector is responding positively to the challenges of increased competition. However, the progress remains partial, and there is evidence that some sub activities are uncompetitive in the local and international market. This is caused by factors such as high input costs combined with low productivity, sub-optimal business strategies and inefficiencies, and unfair trade practices. The lack of international competitiveness also leads to low investment in certain sub-sectors. This is perhaps the major challenge that needs to be addressed.
- **Skewed participation.** Given the legacy of exclusion and discrimination, the challenge is now to unlock the talents and creative energy of people and improve their participation in all aspects of the sector and rid it once and for all of the many entry barriers rooted in its historical dualism.
- **Low investor confidence.** This is caused by the low returns mentioned as well as the definitive impact of factors such as farm murders, evictions and illegal occupations. In addition there are negative perceptions of agriculture, aggravating the situation. Investor confidence is necessary to achieve a vibrant and growing agricultural sector.
- **Inadequate, ineffective and inefficient support and delivery systems.** The weakness of delivery and implementation of a wide range of government measures, regulations and programmes as well as ineffective support systems—all of which are critical to ensure an enabling environment for agriculture—is a major concern. Aspects that contribute to this problem are the fragmentation of certain services, inadequate resources, weak governance and accountability as well as poor executive decisions and often long delays in taking decisions.
- **Poor and unsustainable management of natural resources.** Unused land of good potential is very scarce in South Africa, and there is a limit to the horizontal expansion of agricultural production. In addition, the infrastructure and services to support sustainable land use are inadequate. Government programmes aimed at protecting the resource base (i.e. LandCare and Working for Water) are successful but insufficient. Land degradation remains a problem on good and marginal lands. With increasing pressure on agriculture to raise output per unit of land, it is a major challenge to ensure that this does not take place to the detriment of the natural resource base.

5.6 Prospects

Since 1990, several processes have taken place to reverse discriminatory legislation and to improve participation, while other initiatives have been implemented to deregulate and liberalise the sector. The main policy shifts in this regard include ¹³:

12 The Strategic Plan for South African Agriculture, National Department of Agriculture, 2001

13 The Strategic Plan for South African Agriculture, National Department of Agriculture, 2001

- Deregulation of the marketing of agricultural products
- Fiscal changes, including the abolition of tax concessions that favoured the sector
- A reduction in direct budgetary expenditure on the sector
- Land reform, consisting of the restitution, redistribution and tenure reform programmes
- Trade policy reform, which included the tariffication of farm commodities and a general liberalisation of agricultural trade including free trade agreements
- Institutional reform influencing the governance of agriculture
- The application of labour legislation to the agricultural sector.

These changes have, on balance, led to increased productivity and a more competitive agriculture, although many farmers are now more vulnerable to international shocks, unstable weather conditions, a worsening debt situation and deteriorating terms of trade. This, together with new labour, water and land reform legislation, has skewed perceptions regarding the aims of the legislation, and heightened expectations of labour. Public statements by various pressure groups have contributed to a negative reaction among commercial farmers and a reduction in the number of full-time employees on farms.

The rapid process of deregulation and liberalisation in the past decade has also exposed the limited capacity of many farmers to adjust to policy and market changes. Greater exposure to international competition has affected their competitiveness negatively, causing many farmers to leave the industry. In this much more competitive and open economy, small-farming systems are also failing or finding it difficult to become part of mainstream agriculture.

Although a number of constraints and problem areas prevent the agricultural sector from operating at full potential, some farmers are doing well under the current circumstances. It is also evident that there is a good base and a positive attitude and willingness among farmers, agribusiness enterprises, and government to tackle the challenges and turn them into opportunities.

There are also various land related / agriculture programmes which have been initiated by the government in order to promote land redistribution and small-scale black farmers. These include:

- Land Reform for Agricultural Development (LRAD) – A Department of Agriculture Project which provides matching funding for people who use land productively.
- Local Economic Development (LED)– Dept of Provincial Affairs & Local Government.
- Land Redistribution Scheme.
- Settlement & Land Agricultural Grants Scheme (SLAG).

Exports for the agriculture industry as a whole are expected to increase by 2% p.a. over the period 1997 to 2001. Although this is a slowdown on the figure of 4.4% recorded over the period 1991 to 1996, the decrease may be attributed to the anticipated effects of El Niño on the sector.

6. CONSTRUCTION

6.1 Description

Although not separately distinguished here, the construction sector includes three main sub-sectors:

- Building construction,
- Civil engineering (“civils”) – such as road works, dams, sewerage, etc.; and
- Other – such as drilling of oil or gas wells and water bore-holes, erection of fences and steel structures, telephone and electricity lines, and the installation of hoisting, ventilation and pumping systems in mines.

The SA construction industry is a labour intensive industry, employing 5.3% of South Africa’s workforce and contribution nearly 3% to its GDP. Exports and imports are low due to the nature of production. The sector contributes about 35% to the country’s gross domestic fixed investment (GDFI), with projections of future infrastructure requirements indicating that its contribution to GDFI could double within 5 to 10 years (*White Paper*).

6.2 Demand

Demand in the construction industry is largely dependent on the state of the private sector economy, government investment policy and perceptions and expectations in the consumer and investment markets. This results in considerable volatility in production trends. Private sector construction accounts for almost half of this sector’s demand, while government sector construction has grown to 40%.

Demand for building construction is influenced, in the longer term by demographic factors such as population growth and urbanisation. These, together with the extent of government spending on socio-economic development, affect the demand for residential construction, socio-economic buildings (such as schools and hospitals) and other goods and services. This, in turn, influences the demand for commercial, retail and industrial space.

The government-housing programme, predominantly aimed at low cost housing, has boosted demand for building construction. However, poor delivery has been a problem. Some of the factors contributing to poor delivery are:

- inadequate support from government, on which the low-income group depends, resulting from the lack of funds and excessive demand due to the large numbers;
- a lack of interest from large firms, due to relatively low profits in the provision of low-cost housing; and
- resistance to accept new construction methods, despite progress made in the development of alternative building materials.

Government is also investing a substantial amount of its resources in the building of hospitals and clinics in areas where such facilities have not been available. Growth in middle and higher income residential construction has particularly been underpinned by the demand for cluster housing (related to security considerations) as well as the growth of the middle-income group.

The building of hotels to house an increasing number of tourists in South Africa has boosted local demand for building construction. Furthermore, although the bulk of construction work takes place in South Africa, the industry is currently involved in a number of projects within the SADC region as well as in East Asian and Middle Eastern countries.

In South Africa, most of the demand for civil engineering construction arises from the need to maintain and upgrade the country's infrastructure, of which the deteriorating road network forms a significant portion. The National Public Works Programme (NPWP), which was launched by government as a means of employment creation whilst enhancing the country's infrastructure, has increased demand for civil engineering construction. To date twelve pilot projects have been completed. A further area of increased demand is harbours and airports, some of which are currently being upgraded to meet increases in the demand for larger and more efficient facilities.

6.3 Supply

Enterprises operating in this sector vary from relatively few large contractors to many small and very small contractors and subcontractors. The production processes are highly labour-intensive, mainly involving lower occupational groups and skill levels. Consequently, labour expenses constitute a significant 24% of the sector's cost structure. A decline in employment levels has been noted – primarily due to the increase in sub-contracting or outsourcing.

The construction industry has had to face a number of other structural difficulties in the past, notably the negative effect of a shortage of skilled labour on productivity, the upward pressure of a weakening Rand on the prices of imported capital goods, increased foreign competition and the overhauling of tendering procedures.

The industry has embarked on a massive manpower development programme so as to alleviate the shortage of skilled labour. The shortage is reported to have been caused by several factors, including emigration of qualified workers, early retirement of top-level management and an absence of a development programme for the previously disadvantaged. A number of industry associations are currently involved in training programmes to address the shortage of skilled labour.

Civil engineering projects have traditionally been financed predominantly by the state. However, a structural shift is taking place. In an environment of declining government and public corporation spending on capital projects, the private sector in conjunction with the State introduced the Build-Operate-Transfer concept, which has already led to the construction of several toll roads by the private sector. The private sector subsequently operates the road to recoup incurred costs and after an agreed period of time hands it over to government or the community. This concept can also be applied to other infrastructure projects such as dams and water supply projects.

With the opening up of the South African economy to the rest of the world has come export opportunities and import threats. Several international construction consortiums have entered the South African market with a view to launching themselves into the rest of Africa. This has caused local players in the industry to improve on their methods of delivery to enable them to compete with foreign firms.

A side effect of this is that the industry has increased productivity significantly. A number of local companies have entered into partnership with foreign companies when bidding for large projects both locally and abroad. This has been done so as to take advantage of the international companies' experience in the rest of the world and allowed the foreign companies to benefit from

South African companies' local experience.

Tendering procedures in the construction industry have been altered to encourage participation by previously disadvantaged groups in an industry that is important to the national economy. Although not always taken well by the major players in the industry, Government has put into place tendering procedures that are aimed at increasing the diversity of participants in the construction industry. This could ultimately reduce the control of the industry by a few large companies and allow new entrants into the market.

6.4 SMME Component

The construction sector tends to consist of small and micro enterprises. However definitions can be misleading as there are many one-man contractors who sub-contract work to various other enterprises.

	MICRO	SMALL	MEDIUM	LARGE	TOTAL
Construction	24.50 %	67.05 %	4.84	3.61	100.00

The construction sector presents an area of relatively high growth potential, especially for the smaller firms, with lower overheads and lower skill and performance requirements.

For instance, the provision of low cost housing is a priority for the government. The government is stimulating low cost housing through two main policies: (1). A housing subsidy for lower income individuals and (2). Facilitating access to finance by small borrowers through provident fund guarantees, which facilitates bank lending in the sector, as well as promoting the development of micro-lenders in the housing industry.

Micro and small enterprises related directly to the provision of low cost housing include:

- production & sale of building materials (bricks, blocks, nails, boards, tin roofing, sand gravel etc)
- construction services (masons, contractors, carpenters)
- utility services (electricians, plumbers) and
- related services to the sector such as transport.

SMMEs have an opportunity to develop and deliver low cost housing, for which tender preferences are available. With growing Black urbanisation, low cost housing will remain a growth area. Entry barriers are not prohibitive especially if consortia are formed. The problem with individual competition is the probable lack of critical mass and continuing stagnation. It is expected that 1 million new houses will be built in the next few years

6.5 Constraints

Challenges facing the SMMEs and the construction industry include the following:

- **Short Life Cycle.** The construction sector is relatively volatile with a short life cycle. This results in unpredictability and risks for new entrants into this sector.

- **Cost Of Capital Equipment.** Capital and operational costs can be extremely high for this industry. Since SMMEs cannot invest in expensive machinery and capital equipment, they have to hire machinery and equipment at exorbitant rates from larger companies that can afford to purchase them.
- **Access to Bridging Finance.** Most SMMEs that have been awarded tenders usually lack the necessary capital & finance with which to start up operations, purchase machinery & supplies and contract staff.
- **Technical Skills Requirements.** The construction industry requires skilled professionals (project managers, engineers, surveyors estimators) and artisans (bricklayers, plasterers, masons, tillers, electricians, plumbers etc). However the 'brain drain' from South Africa, the cyclical nature of the industry and the closure of a number of technical training institutions has resulted in a shortage of these skilled individuals.
- **The Variety of Procurement Practices & Documentation used by Clients** 14. The White Paper has identified uniformity in procurement practices as one of the key practices to improve in the construction industry. One of the major obstacles in and cost to the industry is the variety of procurement practices and documentation currently used by clients. This leads to additional cost to the project and increases the risk on project delivery.
- **Public Sector Capacity and Performance.** The public sector has lost a significant amount of knowledge and capacity about construction, essential and basic government processes and particularly construction procurement processes. The Ministers of Finance and Public Works have expressed the government's concern about bottlenecks, which affect both emerging and established players. The decline in public sector spending is not due to a decline in effective demand but rather due to the inability of government to spend their budgets.
- **Tight Profit Margins.** Profit margins are very narrow particularly in the low cost housing segment, which provides the greatest opportunities for SMMEs at present.

6.6 Prospects

Undoubtedly the future of the construction industry is closely linked to the well being of the national economy. Local demand for the sector was forecast to grow at 3.1% p.a. over the period 1997 to 2001 with the creation of more than 3 000 jobs annually over the same period. The achievement of these goals will only be promoted by the fulfilment of housing promises made by government, a brisk performance of the tourism industry and the success of the National Public Works Programme (NPWP). However, sluggish growth in the economy can have serious detrimental effects on the industry, which could result in a static job market or even job losses.

According to the government's Medium Term Expenditure Framework, the aim is to strengthen the capital-spending trend, increasing the amount available for the upgrading of infrastructure over the next five to ten years. This will inter alia be channelled through the NPWP, which the government has prioritised in terms of employment generation in civil engineering construction.

The shift away from government to private enterprise as far as construction activities is concerned together with privatisation of state corporations has generally been welcomed, although in the short term it could involve the scaling down of the important counter-cyclical effects of public works and cutbacks by public corporations to boost profitability. The effects on the industry of proposed reforms such as the public sector procurement process and increased legislation for the building industry are also yet to be felt.

Backlog and insufficient infrastructure, past sources of growth such as the building of suburban corporate office parks and town and cluster housing is expected to continue their contribution to building construction. Declining interest rates should support this. Other private sector growth areas are the upgrading of harbours and the provision of water, sanitation, electricity and telephone facilities to rural and suburban areas.

The issuing of licenses to casinos is expected to be worth approximately R9 billion to the industry. Furthermore, the finalisation and construction of toll roads and projects expected to flow from the Spatial Development Initiatives should further contribute to demand in this sector. Growth in the demand for tourist accommodation should also provide a further stimulus to the industry.

The export market, especially into the rest of Africa, looks very promising. Exports were predicated to grow at more than 15% p.a. from 1997 to 2001. For the next few years the industry can expect to be involved in projects in the South African Development Community (SADC) region, valued at around R9 billion. The involvement of foreign companies in local construction is also forecast to increase.

Other opportunities for SMMEs include; affirmative procurement procedures by the public sector, the building of infrastructure – roads, clinics, hospitals and schools in the various provinces by the government, casino developments and spatial development initiatives (SDIs). One possible negative effect of affirmative procurement could be on the long-term prospects of small business – as government empowerment policy favours spreading the awarding of tenders. As a result SMMEs may incur up front capital costs, without the guarantee of securing sufficient repeat business. However, some stakeholders have recognised this issue and are taking it up with local government, which awards most of the tenders.

The establishment of the Construction Industry Development Board (CIDB) is an important development for the industry. The industry will in future fall under strict regulation. Among the issues that the board will address are: investment and spending, the state of the industry, skills formation & quality construction procurement, public sector delivery management, transformation the development of a statutory register for all contractors & projects and the establishment of a code of conduct for all members.

A major challenge facing the industry and the board is the development of public-sector delivery, which accounts for about 40% of all building and construction work. Since the public sector remains the single largest of the industry, delivery capacity is crucial to the sustainable growth and development of the industry.

7. MANUFACTURING

South Africa's manufacturing sector is relatively well developed. As the single largest sector in the country, it contributes 19.8% to GDP¹, and is very diverse – incorporating numerous subsectors ranging from clothing and textiles to food processing, from chemical products to motor vehicles assembly and manufacture.

Table: Manufacturing

	MICRO	SMALL	MEDIUM	LARGE	TOTAL
% contribution to GDP	5.27	7.37	21.02	66.34	100.00
% of SMMEs by size	61.27	18.92	14.11	5.70	100.00

Manufacturing output grew slightly by 2.7 % year on year on average in the first half of 2001, due mainly to the rise in real domestic and stronger export demand in certain sub categories of manufactured goods such as South African produced vehicles. the motor vehicle, glass and manufacturing equipment sectors remain the main contributors to the overall performance within the manufacturing sector. Other manufacturing sub sectors where output strengthened were food processing, clothing manufacturing and basic metal products.

Capacity utilisation in the manufacturing sector is approximately 80%, indicating potential sectors to expand output further without overstraining resources. Insufficient demand has remained the primary reason for the under utilisation of productive capacity in the South African economy.

According to the Survey of Total Employment and Earnings by Statistics SA approximately 4.8 million workers were employed in the formal non-agricultural sectors of the economy at the end of 1999. The acceleration in job losses, which started in the second quarter of 2000, was more pronounced in the private than the public sector. However labour productivity has continued its upward trend, exhibiting faster rates of increase than those recorded over the post 1994 period to mid 1997.

Despite the declining trend in general employment levels, there were some employment gains in sub sectors such as transport, equipment, beverages and furniture. The sub sectors that experienced more job losses were basic metals, footwear and other chemical products.

7.1 Clothing

7.1.1 Description

The clothing sector covers the manufacture of all types of clothing such as fabrics, leather, fur, plastic, rubber and other materials, but excludes manufacture of knitted products and footwear. Since the clothing industry is a very labour-intensive industry, it is responsible for almost 1.8% (125 000 people) of employment in South Africa ¹. Informal sector employment in clothing manufacturing is significant.

However, large-scale importation and illegal goods have adversely affected the clothing industry. The industry agreed on an import tariff phase down period of 7 years, starting 1995, and the 41% end rate will be in line with the World Trade Organisation (WTO) requirements.

Clothing production contributes 0.8% to South Africa's GDP and 0.4% to exports. Clothing imports are 0.4% of total imports. Past policies have created an environment of import replacement and employment creation at almost all cost, resulting in a non-competitive environment. However, industry stakeholders have agreed that the long-term strategy for the clothing industry should support international competitiveness and an export drive, especially in the middle- and higher-priced garment sectors and niches.

7.1.2 Demand

Local demand for clothing, like most semi-durable and durable consumer demand, is of a cyclical nature depending to a large extent on the personal disposable income of consumers. In line with the far-reaching changes taking place in the country regarding income distribution and demographic shifts, the clothing market is also experiencing significant changes in tastes and preferences.

Historically, exports have been insignificant at less than 0,1% of world exports and only 4% of total production. Although developing an export culture is a slow process obstructed by foreign competition, trade barriers and seasonal differences with the Northern Hemisphere, the export potential is promising due to the opening up of markets in Southern Africa and beyond. The major destinations of South Africa's clothing exports are the UK, USA and Mozambique.

Since 1974, much of world trade in textiles and clothing has been regulated by the Multi-Fibre Arrangement (MFA). Negotiated as an exception to normal WTO disciplines, the MFA has provided the basis on which industrial countries have established quotas on imports of clothing from more competitive developing countries. The African Growth & Opportunity Act (AGOA) enacted by the United States could be the key to major export opportunities for South African manufacturers. The US government is behind a new Africa policy, which aims to promote trade with and investment in progressive African economies. AGOA which exempts certain South African manufactured clothing products from US customs duty has been beneficial to South African companies who have taken advantage of this scheme.

A reduction in import duties to access the US market will be a significant stimulant to the South African industry, while overseas firms could invest in South Africa to benefit from the preferential tariff agreement with this country.

7.1.3 Supply

Although clothing manufacture is spread across the country, manufacturing activity in this sector is mostly concentrated in KwaZulu Natal and the Western Cape. Significant relocation to other parts of Southern Africa has taken place in search of lower labour cost, to compete with mainly “lower end” imports from the Far East. Apart from normal import competition, the domestic industry has also been adversely affected by the influx into the country of new and second-hand clothing, distributed mainly by the informal retail sector.

Although the barriers to entry are low, the clothing industry’s competitiveness has been affected by low productivity and high raw material costs. Raw materials contribute on average about half of the total production cost of clothing products. The extension of the duty credit certificate scheme has helped clothing manufacturers to source raw material at competitive prices in an effort to adapt to international competition. Productivity and training issues are also high on the agenda of the restructuring process taking place in the industry, offering some signs of the industry being willing to break out of its defensive-protection mould and adopting a more proactive attitude in dealing with foreign competition.

Efforts by the DTI to prevent trade in second-hand clothing, in order to prevent the destructive effect on the local industry as has happened in neighbouring countries, have been hampered by illegal imports. Progress has however been made in reducing illegal imports, because of efforts by the customs law enforcement task group, which is partly sponsored by the Textile and Clothing Federation. Imports of cheap clothing are likely to promote a shift by the local industry towards production for the higher end of the market while consolidating lower end production.

7.1.4 SMME Component

Barriers to entry are low in the clothing sector, and SMMEs can enter the market with relative ease when compared to some of the other sectors. The majority of micro and very small enterprises feature primarily in the informal distribution of clothes, though there is an important manufacturing potential. Small cut, make & trim (CMT) firms are an important part of this manufacturing potential.

A noticeable trend in the sector is that of large clothing companies shutting down their manufacturing plants and outsourcing the manufacturing of garments to SMMEs. These large clothing companies are focusing on making sample garments and marketing these overseas specifically for the export market. Therefore for small-scale firms offering high quality at competitive prices, sub contracting for larger clothing firms is an opportunity.

Incentives available through the DTI also encourage linkages between large companies and small businesses. For example if a large company buys fabric from overseas and outsources the manufacture of garments from this fabric to SMMEs for export purposes, then they do not pay any import tariffs on that fabric. The DTI also allows a 10% rebate on training undertaken within the clothing sector.

7.1.5 Constraints

- **Cheap/Illegal Imports.** Globalisation has increased the threat of dumping and illegal imports by unscrupulous countries, companies and individuals. Some countries where clothing can

be produced cheaply due to the preponderance of so-called 'sweat shops' have been tempted to exploit this low cost advantage. Apart from normal import competition, the domestic industry has also been adversely affected by the influx into the country of new and second-hand clothing, distributed mainly by the informal retail sector.

- **Low Productivity and High Raw Material Costs.** The clothing industry's competitiveness has been affected by low productivity and high raw material costs. Past government policies have created an environment of import replacement and employment creation at almost all cost, resulting in a non-competitive industry. Raw materials contribute on average about half of the total production cost of clothing products.
- **Training And Skills Development.** Training And Skills Development issues are high on the agenda of the restructuring process taking place in the industry, offering some signs of the industry being willing to break out of its defensive-protection mould and adopting a more proactive attitude in dealing with foreign competition.
- **labour-intensive Industry.** The clothing industry is a labour intensive industry with labour overheads contributing a large proportion of the costs of clothing manufacture. A highly unionised environment with minimum wage levels makes it difficult for smaller entrants to conform to the standards agreed to by the larger manufacturers and the Clothing Textile Trade Union.
- **Cyclical Demand.** Local demand for clothing, like most semi-durable and durable consumer demand, is of a cyclical nature depending to a large extent on the personal disposable income of consumers.
- **Relocation of Manufacturing Plants.** Significant relocation to other parts of Southern Africa has taken place in search of lower labour costs.

7.1.6 Prospects

In contrast to an average annual decline in domestic clothing production during the 1991-1996 period, growth of approximately 3% per annum is forecast. This is mainly the result of an improved export performance during the forecast period (14.1% average annual growth rate). The industry is already showing signs of focusing upmarket into value-added products in order to compete globally and also exploring the opportunities of working with our SADC partners on supplying in the lower end products where prices is the main criteria 15.

The opportunity of cumulation within the region (adding value to a product in various SADC countries in order to achieve originating status) offer many possibilities in textiles and clothing in terms of the imminent European Free Trade Agreement and also the USA legislation mentioned earlier because these sectors are labour-intensive and lend themselves to the developmental component of South Africa's commitment to SADC.

It is therefore expected that production for the domestic market will increase at an average annual growth rate of only 2%, compared to the high growth rate of 6,3% expected for imported goods. The

15 Sectoral Prospects: 1997-2001, IDC: Riaan Coetzee & Theo Janse van Rensburg 1998

higher cost structure of South African firms compared to some Far Eastern producers, prevents the local industry from supplying the sizeable lower end of the local clothing market unless local suppliers are able to effect a better trade-off between labour costs and productivity.

A much stronger export performance is possible as evidence suggests that the South African clothing manufacturers have the potential to export higher quality clothing into niche markets. The African Growth & Opportunity Act (AGOA) could create even more exciting opportunities for South African manufacturers.

As import penetration is expected to increase, customs controls will have to be improved in order to stop illegal imports. Although cheap (and illegal) imports and the lowering of high tariff barriers have hit the clothing industry hard, it now seems to be on the road to recovery. As a result of significant restructuring and the successful implementation of an appropriate industrial strategy, the clothing industry could start to experience expansion in production, investment, employment and exports.

7.2 Agriculture – Secondary (Food Processing)

7.2.1 Description

Food processing as a whole is an important sector in the South African economy, contributing 2.4% to total gross domestic product, 3.2% to total exports, accounting for 4.1% of total imports and 2.6% of total employment¹. The sector consists of eleven downstream agriculture sub-sectors: meat processing; dairy products; preservation of fruit and vegetables; canning and preserving of fish; vegetable and animal oils and fats; grain mill products; bakery products; sugar mills and refineries; cocoa, chocolate and sugar confectionery; other food products; and prepared animal feeds.

Food processing accounts for 15% of the manufacturing sector. But one of the difficulties of the secondary agriculture sector is in trying to unravel the domains of the food & beverage and agriculture sector which are interwoven with it.

Meat processing is the single largest food sub-sector, contributing one quarter of total food production, followed by the grain milling and animal feeds sub-sectors, accounting for 13% and 10% of food output, respectively. The other eight sub-sectors each contribute between 4% and 9% of overall food production.

The food-processing sector is influenced by a number of factors, including climatic conditions, overall economic growth, private consumption expenditure and the continued deregulation and liberalisation of the agricultural sector. This process of deregulation and liberalisation has raised competitive pressures, which, in turn, have accelerated the restructuring of the food processing industries. Import control on almost all agricultural products has now been lifted and replaced by import tariffs, whilst the new Agriculture Marketing Act, which was promulgated early in 1997, resulted in the dismantling of agriculture marketing boards.

7.2.2 Demand

As countries develop and prosper, their food processing industries become more sophisticated. At the same time, the more prosperous consumer develops a taste for quality, wholesome food products and tends to spend more on ready-to-eat, prepared products than on the traditional non-processed staple foods. The dual nature of the South African economy implies a diverse demand for food - from the middle to upper income levels there is increasing demand for healthier, convenient, quality foods, whilst the poorer sections of the population still demand staple foods to be provided at low prices. These divergent trends have important implications for each of the food processing sub-sectors.

Domestic food production is primarily aimed at the local market, with private households accounting for the largest share of domestic sales (up to 90% of sales in certain cases). Demand trends are therefore dominated by growth in private consumption expenditure and often tend to be relatively stable. The food-processing sector's main intermediate clients are agriculture, the catering and accommodation sector and the animal feeds sub-sector.

Food exports have in the recent past been bolstered by the deregulation of the local industry, by the opening up of international markets to South African products, the weakening of the Rand and by relatively low inflationary pressure on domestic cost structures. However, in total, only 8% of

¹ Sectoral Prospects: 1997-2001, IDC: Riaan Coetzee & Theo Janse van Rensburg 1998
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domestic food production is destined for the export market.

The largest share of the food export basket is attributable to the sugar-milling sub-sector, which accounted for almost 38% of total food exports in 1996. Prepared and preserved fruit and vegetable products contributed just over 19% to the sector's export earnings, followed by meat products with a 14% share. Most of the other food sub-sectors are, however, net importers and export only a small portion of their produce. Exports are fairly evenly spread across the top export destinations, with the top five - namely, the United Kingdom, Mozambique, Germany, Japan and the Netherlands accounting for approximately one-third of the total export value in 1996.

Preferential market access possibilities exist for the food sector and could further aid export growth in the sector. Tariff cuts are, for example, provided for a wide range of food products by countries such as the USA, Canada, Hungary, Switzerland and the EU, through their respective Generalised System of Preferences (GSP) programmes. In addition, better market access is currently being negotiated with the EU.

The signing of the Trade Protocol between SADC countries could also create a large export market for food processors. Africa is a largely untapped market with high urbanisation growth rates. In fact, it has been estimated that urban populations in the SADC region are growing at 6% per year, implying a doubling of urban markets over the next 12 years. Although a basic necessity, food production structures in many of the SADC member states cannot supply this growing need. This provides South African food exporters with market opportunities.

7.2.3 Supply

A common feature of most of the food processing sub-sectors is their dependence on inputs from the agricultural sector. Certain sub-sectors do, however, utilise lesser amounts of agricultural inputs, thus making them less susceptible to output and price volatility. These include, for example, the sub-sectors producing bakery products, confectionery items and "other food" products. Important intermediate inputs also emanate from the food-processing sector itself. One such example is the extensive use of grain milling products for the production of bakery products.

Primary factor costs represent 22% of total costs and the capital-to-labour cost ratio is 10 to 12. Although many of the food processing sub-sectors are very labour-intensive, huge investments also have to be made in the appropriate type of machinery and equipment to process basic agricultural inputs. This is evident in most of the food sub-sectors.

Due to the very nature of food products and the wide range of non-tariff barriers generally applied to these products (including stringent health measures, labelling requirements and so on), the food processing sector generally does not encounter very high levels of import competition. The import penetration ratio for 1996 was 10.2%.

The largest share of food imports originates from Argentina, which accounted for 15% of total food imports in 1996. The USA, Malaysia, Thailand and Australia together represented a further 31% of overall imports. The largest import shares in 1996 were claimed by sub-sectors producing oils and fats, grain mill and fish products. The other food products and the meat processing sub-sectors accounted for an additional 21% of total food imports.

A 2.3% average annual rate of decline in employment levels over the period 1991 to 1996 conceals

the food sector's relative employment stability since 1994. Driven by an increasingly competitive environment (partly as a result of tariff reductions) considerable productivity improvements have also been recorded. This has spurred new investments within the sector. According to *Business Map SA*, more than R3.8bn in foreign investment have flown into the food and beverages sector since May 1994.

However, South Africa's food sector faces unique challenges. Lower tariffs and freer trade have forced sectoral players to become more competitive, whilst consumers are demanding better quality, convenience, health protection and variety. The sector is also expected to promote "food security" and is being asked to assist in reducing malnutrition by feeding the poorer sections of the population.

In addition, the food sector is expected to contribute to economic empowerment through job creation and the provision of support to small businesses, especially in rural areas. Despite these challenges, the sector is likely to make an increasingly significant contribution to foreign exchange earnings through higher export volumes.

7.2.4 SMME Component

According to the Secondary Agriculture SETA, there is very little empirical data on the SMME component is available, except for the fact that it appears to be larger than originally estimated. SETASA has submitted a proposal to government for conducting a large-scale research project, which will accurately quantify the involvement and role of SMMEs in the sector.

Nevertheless, it is known that some sub-sectors consist mainly of SMMEs (e.g. Pest Control) whilst others have very few SMMEs (e.g. Fruit Packing). This insight is useful in terms of identifying focus areas for SMME development.

Some sub-sectors are male dominated (e.g. Red meat and livestock – 75%) whilst others are female dominated (e.g. Fruit Packing and Processing – 84%). And, as could be expected from a diverse sector such as Secondary Agriculture, numerous institutional structures (professional bodies, employer associations and labour unions) are active in the sector

7.2.5 Constraints

- **Highly Diversified.** The sector consists of eleven downstream agriculture sub-sectors. This impacts on the policies and strategies needed to promote the development of SMMEs within the various sub sectors. There are large number of SMMEs that already exist in some of the sub-sectors (such as pest control)
- **Capital Intensive Nature.** Although many of the food processing sub-sectors are very labour-intensive, huge investments also have to be made in appropriate machinery and equipment to process agricultural inputs. This can impede the entry of SMMEs into the sector.
- **Training and Skills Development.** In general the sector employs a very large component of elementary workers, ranging between 63% and 81%. Further technical training and skills

development is necessary in order to improve the competitiveness and productivity of the industry.

- **Competitive Skills and Technology Requirements.** The competitive & technological skills requirements of this sector hinder the entry of SMMEs. It doubtful whether really small-scale enterprises have the competitiveness skills and technology to exploit opportunities in the secondary agriculture sector.

7.2.6 Prospects

Although South Africa always had a well-developed food industry, it has now become a global player. The largest increases in export value came from mainland China, Somalia, Norway, Malaysia, Thailand and Denmark. The food industry, in its broadest definition, is a major export earner, exporting about R8,5 billion annually: approximately twice of what it imports.

Lower tariffs and freer trade have forced sectoral players to become more competitive, whilst consumers are demanding better quality, convenience, health protection and variety. The food sector's strong backward linkages with the agricultural sector imply that agricultural output and prices will have a direct impact on its own competitiveness.

According to IDC projections, demand for food products is anticipated to increase in future, not only due to overall population growth and rising incomes but also due to an expanding tourism industry. *And the sector's export performance is also expected to improve.*

Despite growing demand for South African exports, and improved access to European and other markets, it is doubtful whether really small-scale enterprises have the competitiveness skills and technology to exploit this opportunity. Small scale suppliers in rural areas and townships will have been hit by declining per capita incomes and continuing retrenchments, however, aggravated by considerable existing competition in areas such as the supply of meat, dairy products, grain milling and so on.

8. TOURISM

8.1 Description

The South African Government has identified tourism as the industry most capable of providing economic growth, leading to employment growth, through sector expansion and increased foreign exchange earning. The sector is seen by government as a vehicle for redressing unemployment by creating employment opportunities at all levels; and for redressing employment disadvantage through the application of Employment Equity and Labour Relations law.

Cognisant of the tourism sector's potential in contributing to economic growth, generating foreign exchange and creating employment, the South African Government has adopted a tourism strategy based on the principles that the industry should be Government-led, private-sector driven, community-based and labour-conscious. This strategy sets the following targets for the year 2000: (i) to raise the contribution of the tourism sector to 8% of GDP; and, among others (ii) to increase employment opportunities within the sector from the current 550 000 to 860 000.

International tourist numbers have increased significantly since the end of the apartheid government (from 3.7 million foreign tourists in 1994 to 5.8 million in 1999). It is largely believed that there was a "gearing-up" of capacity in the tourism industry in terms of facilities and services to meet the needs of the anticipated "tourism boom". This "boom" was not as large as anticipated in 1999 and resulted in the demise of smaller, and some larger, tourism organisations¹.

In terms of jobs, the Western Cape has probably had the highest increase in tourism industry employment levels, while Gauteng, Mpumalanga, KwaZulu-Natal, Eastern Cape and the Northern Province have also experienced a substantial increase. The North West, Free State and Northern Cape have the least number of new jobs created in the tourism industry.

Direct employment in the tourism industry is not widespread throughout the provinces. Instead, it is generally localised to urban areas and tourist attractions. Some new employment opportunities have come on stream recently with the licensing of additional casinos. Largely, however, such new employment has displaced informal employment in the former illegal casinos. The further development of the gambling and lotteries industry including the introduction of Limited Payout Machines (LPMs) and the issuing of additional casino licenses should create additional employment opportunities in this sector.

Sport is recognised in the economic sector as a potential growth industry, both directly and indirectly.

Estimating the total number of employers and employees in the sector is problematical due to the lack of accurate and up to date statistics for almost all of the industries in the sector. The tourism Sector Education & Training Authority (THETA), estimates that there are approximately 42 000 enterprises, both formal and informal and including SMMEs, that fall within the industrial categories covered by THETA. Hospitality organisations account for 85% of these employers.

8.2 Demand

In 1998 there were 1,4 million foreign visitors to South Africa, excluding visitors from other African countries, and the number of overseas visitors grew at 5% during January-August 1999. As might be expected, more than half of these came from Europe, and 4,3 million visitors came from African countries.¹⁶ Tourist number growth has almost doubled since 1994.³

The domestic tourism market is also significant, and is predicted to expand significantly as the South African middle class broadens. According to SATOUR, 16 million of the South African population took 30.4 million leisure trips in 1996, and domestic tourism represents 87% of South Africa's total visitor market.⁴

The primary purposes of domestic tourism are trips for holiday or pleasure, visiting friends or relatives, and business; and significant elements of domestic tourism activity are related to sports and wildlife conservation. The number of domestic visitor nights is expected to grow if the domestic economy improves.

South Africa's domestic and international sporting activity contribute to both tourism and general economic activity, creating demand for travel, accommodation and catering; and the maintenance of an attractive environment through conservation activities underpins the provision of tourism and recreational opportunities.

At the same time, tourism, is a notoriously fickle economic activity. Unrest in neighbouring countries, political instability or poor security in South Africa, inadequate marketing or negative journalism can very quickly dampen the market and destroy the sector's progress.

8.3 Supply

South Africa's physical, service, tourism and sporting infrastructure is well-developed, being far superior to most third world countries, though it lacks the coverage and some of the sophistication of developed first-world nations. The infrastructure is unevenly distributed, limiting access to economic development and leisure opportunities for large population groups.

Tourism infrastructure development has stagnated until recently, and international standards and expectations have not been factored into service provision. International tourists, sports people and businesspeople experience standards of customer service that are inconsistent and unreliable – sometimes excellent, but frequently well below international expectations.

The largest proportion of tourism, hospitality and sporting activity is concentrated in South Africa's urban centres, as might be expected. However, some of the country's major attractions are located in rural areas, and the development of tourism in these areas is a priority in order to address rural unemployment and economic disadvantage.

Almost all rural tourism operators are SMMEs and a high proportion of rural tourism and hospitality operators have limited or no formal qualifications and little management experience. Most wildlife conservation activity is located in rural areas, where the availability of training in rural areas is very

¹⁶ *Ibid*, and StatsSA (2000)

³ Editors Inc (1998), *op cit* p 153

⁴ Grant Thornton Kessel Feinstein, Tourism Fact Sheet (Department of Environmental Affairs and Tourism, 1999) pp 1-2

limited.

It is estimated that by the year 2000 there will be twice as many skilled job opportunities across all industry sectors as there are qualified, skilled workers available to fill them, and this situation is reflected in the Tourism, Hospitality and Sport Sector, especially in rural South Africa. The consequence is that unskilled workers are employed to fill vacancies. They perform at well below international best practice standards, impacting negatively on tourist experiences, business efficiency and, ultimately, business growth. Some key skill shortages in rural areas are in food preparation and cooking, food and beverage service, tour guiding and computing.

8.4. SMME Component

The tourism sector is touted to have the potential to be the largest in South Africa in terms of employment, foreign exchange earned and GDP. This sector is largely dominated by SMMEs and micro enterprises. Due to the lack of statistics and the fact that there is no formal registration of formal and informal employers in this sector, it is estimated that more than two thirds of the approximately 42 000 sector employers are SMMEs.

In addition, a substantial part of the sector is primarily involved in food preparation, food and beverage service and catering – for the general population, not only for tourists – so they are located where their markets are concentrated. (i.e. in urban areas). Small, micro or medium-sized enterprises employ most of the employees in the sector. It can be said that the small business sector is the potential engine-room of economic development and employment growth throughout much of South Africa's economy, and certainly in this sector. The industry and rural development issues for the sector, as well as the National Skills Development Strategy, indicate that SMMEs and rural enterprises must be high priorities for training.

8.5 Constraints ¹

- **Uneven Distribution Of Tourist Infrastructure and Stagnation.** The infrastructure is unevenly distributed, limiting access to economic development and leisure opportunities for large population groups. Tourism infrastructure development has stagnated until recently, and international standards and expectations have not been factored into service provision. International tourists, sports people and businesspeople experience standards of customer service that are inconsistent and unreliable – sometimes excellent, but frequently well below international expectations.
- **Marketing Performance And Image.** A massive marketing effort is required if South Africa is to compete for a larger share of international tourism. Tourists have to be able to believe that they are coming to a safe, secure destination. Action is necessary to improve security, address property and violent crime and make internal travel safe; and the message that South Africa is a generally secure environment for tourists must be conveyed consistently. The injection of very substantial resources into marketing effort by the Business Trust and in the current national budget is a good first step in this direction.

¹ Tourism, Hospitality and Sport Sector 2001-2002 Skills Plan, Tourism, Hospitality and Sport Sector Education & Training Authority, February 2001

- **Increased Competition.** Tourism has become a fiercely competitive business. For tourism destinations the world over competitive advantage is driven by technology, information and innovation. Yet South Africa is ranked only 42nd among 47 emerging and developed countries. There is much room for improvement in skills, customer service, security etc¹.
- **Afro-Pessimism.** The international view of Africa is negative. South Africa is seen in the same light as the rest of Africa by international consumers, and this view is sustained by media coverage. The SADC regional tourism product is not marketable at present because of recent dislocating events, though it could be under more normal circumstances.
- **Urban Rural Divide.** The overwhelming majority of the sector's businesses are located in urban settings. Many of South Africa's unique attractions are located in rural areas. For these to be appropriately developed, marketed and operated in order to maximise tourism activity, the rural tourism infrastructure must be provided. This means the skilled people, as well as the transport, accommodation and physical services, must be provided for the rural areas. The availability of training in rural areas is very limited.

The objective of providing employment growth is particularly urgent in rural areas. The sector is expected to contribute significantly to such employment objectives; but this requires both tourism development and the provision of a skilled workforce in these areas.

In addition to human resource development, local industry players have continuously manifested the need for a concerted effort in: (i) developing the range of tourism products and services that will meet the desires of targeted consumer market segments and niches; (ii) ensuring a commitment to quality; (iii) developing a customer-oriented culture; (iv) undertaking effective marketing activities; (v) incorporating, wherever possible, the unique selling features of Southern Africa, instead of those of South Africa on their own, in the marketing of industry products; and, among others, (vi) encouraging and participating in efforts to develop a co-ordinated approach to the industry under a unified vision and focus.

8.6 Prospects

Ntsika Enterprise Promotion agency predicated that the SMME sector would dominate South Africa's tourism sector in the future, because the sector was 'at the beginning of a long run growth process'. Ntsika said that the tourism sector had opportunities, which were 'immense and untapped'.

It is estimated that the global tourism industry, calculated at \$ 4.5 trillion/year, will grow to a \$ 10 trillion industry by 2010, with a 4.3% growth rate representing one of the fastest in the world. Tourism is also acknowledged as one of the biggest producers of foreign exchange with other multiplier effects including small, medium and micro-enterprise (SMME) development.

The current situation in South Africa, with relatively little marketing and strategic planning has seen foreign arrivals grow by 36% from 3.6 million in 1994 to 5.7 million in 1998. Estimates for 1999 were approximately 6.5 million foreign arrivals, which does not include the increasing domestic tourism with its new market segments.

¹ Dept of Arts, Culture & Technology, Tourism, National Research & Technology Foresight, 1999) p8
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South Africa is, poised to take a significant position in the list of the world's top destinations. From 54th in 1990, it's ranking within such a list improved dramatically to 27th in 1996. However, whereas the tourism industry is estimated to contribute approximately 11% to world GDP, in South Africa's case the ratio is thought to lie within the 4.5% to 5% range.

Domestic tourism has traditionally been the backbone of the South African tourism industry. Although expanding in absolute terms, its relative contribution to total tourism (compared to that of foreign tourism) has been watered down due to the fast expanding foreign component. The domestic segment of the national tourism market has also changed dramatically, both in composition and nature. Generally not as demanding and less quality-conscious than their overseas counterparts, domestic tourists are rapidly becoming more sophisticated and exhibiting characteristics and consumption habits, which progressively mirror international ones. Most importantly, holidaymakers demanding higher service standards and value for money.

Due to oversupply of high end accommodations, there are declining occupancy levels. These conditions have exacerbated by the sensitivity of the industry to overall economic conditions, as reflected by subdued domestic demand in recent times. Furthermore, encouraged by a depreciating currency and rising numbers of foreign tourists, local hoteliers opted for unbridled rate increases which the average South African could not afford.

SECTION III – COMPARISONS, CONCLUSIONS

Introduction

This section reviews the information in the preceding two sections, and weighs it up across the sectors as well as in relation to the targets and overall aims of World Education's planned Business Linkages Programme.

Once again, it is worth noting that comparisons between sectors are complicated by the fact of differing definitions and data that are available. Whichever sector is selected for intervention, it would merit an in-depth study with first-hand information obtained from key informants and players within the sector itself.

Taking into account the secondary research, as well as primary research through discussions and meetings, the consultant has provided his assessment or ranking of the five main sectors studies per the sector selection criteria described in World Education's proposal submission to USAID earlier this year. These criteria include:

- Sector growth trends
- Proportion of PD-owned small and microenterprises participating in the sector
- Ease of Entry of such firms
- Regulatory environment
- Openness to working with small firms
- Intensity of negative factors
- Potential competition from existing Business Linkage programmes

The comparisons above are summarised in table format – and the scores achieved clearly indicate that the Construction sector holds considerable promise or potential for a targeted Business Linkages intervention. Spending and growth trends are positive, and the sector is characterised by a dominance of micro and small size enterprises, in both urban and rural areas, and a highly positive regulatory environment.

The Tourism sector runs second as a possible area for Ntinga LINK intervention although the issue here would be one of ascertaining "depth" of target business in terms of micro-size enterprises or poverty related criteria. Also, a relatively small-scale World Education intervention could be overshadowed by the current, multi-million Rand Tourism Enterprise Programme (TEP) project, which encourages linkages and business deals with the provision of financial inputs or subsidies.

9. CONCLUSION & RECOMMENDATIONS

9.1 SMME characteristics

In selecting a particular economic sector as the focus of its Business Linkages programme it is important for World Education to consider the following:

- **SMME contribution to GDP:** On average for the entire country 34.8% of the GDP is generated by SMMEs and 65.2 % by large enterprises. Sectors where SMMEs contribute more than 40 % of the GDP share include agriculture, construction, trade and transport. It is in construction, trade and the transport sectors particularly, where the significant role of micro and small enterprises are remarkable, indicating involvement of the target PDI group in which both World Education and the donor are interested.
- **SMME Contribution To Employment:** Irrespective of the importance of SMMEs in terms of their contribution to GDP, arguably their biggest single contribution to the South African economy is in terms of employment. Their role as an agency for employment in South Africa cannot be overemphasised, especially within the context of a developing nation

Viewed within the respective sectors themselves more than 50% of the employment within SMMEs occurs in the agriculture, construction, trade, transport and business and other services sectors. SMMEs contribution to employment is much higher within each of these four sectors than for small enterprises as a whole.

80.4% of all people employed in micro-sized enterprises are employed in the business and other services and trade sectors. Approximately 57% of all the people employed in very small and small enterprises are employed in only three sectors, namely construction, trade and transport. And agriculture, manufacturing and transport contribute approximately 70% of all employment in medium-sized enterprises.

It is clear that the dominant sectors within each size class cohort are generally different, each with it's own unique features. It is these features and natural trends that should be kept in mind when deciding on policy options that promote SMMEs in various different sectors.

- **SMME Contribution To The Number of Establishments:** Approximately 66% of all micro-sized enterprises are either trade, transport, business or other services. Construction on the other hand, is by far the dominant sector regarding small enterprises. Agriculture with 53.7% followed by manufacturing with 18.5% of the total number of establishments in the medium sized category are the dominant sectors in this cohort. Therefore some sectors are more conducive to a particular size class than others.

9.2 Sectoral characteristics

- 9.2.1 **Agriculture** - The primary agriculture sector (which excludes forestry & fishing) is very diverse, covering a wide range of farming activities at various levels of sophistication and is spread all over the country. Unlike other developing countries, the contribution of the primary sector is very small.

There has been a declining trend in overall agricultural production. This is exacerbated by the uncertainty around government land redistribution policies and land ownership rights. There has been no major new investment in the agricultural sector. The low skills levels and lack of prime agricultural land & technology make entry into this sector by PDI firms very difficult.

South African commercial agriculture has followed a more capital-intensive growth path, while significant agricultural resources (human and material) lie unused or under-utilised in the former homeland areas. Both these phenomena have affected the income-earning potential of rural people. Further, the entrepreneurial abilities of Black farmers were suppressed, first by their exclusion from the commercial land market and then because commercially viable freehold farming was almost impossible in the former homeland areas.

- 9.2.2 **Construction** – 91.55% of firms in the construction sector consist of small and micro-enterprises. Public sector commitment to increase spending on infrastructure projects and low cost housing together with recent private sector commitments to increase construction investment spending contributes largely to the upbeat trend in this industry. The South African government recognises the role that the construction sector can play in kick-starting the economy.

Demand in the construction industry is largely dependent on the state of the private sector economy, government investment policy and perceptions and expectations in the consumer and investment markets. Despite the fact that the contribution of the construction sector to GDP is small, there is a lot of potential for SMME involvement in this sector. Individuals working as independent contractors or small firms can benefit from changes in procurement policies, the involvement of the public sector in the building of infrastructure & low cost housing, the Spatial Development Initiatives, and private sector construction like the casino developments and cluster housing.

- 9.2.3 **Manufacturing:** This is the single largest sector in the country, contributing 19.8% to GDP and is well developed. Insufficient demand has remained the primary reason for the under utilisation of productive capacity in the South African economy. Transport equipment, excluding the motor vehicle parts & accessories sector, reported the lowest utilisation rate in the second quarter of 2001 (below 67.1%). There has been a declining trend in manufacturing fixed investment growth.

- 9.2.4 **Clothing:** The clothing industry is a very labour-intensive industry. Barriers to entry are low and SMMEs can enter the market with relative ease when compared to some of the other sectors. However, large-scale importation and illegal goods have wrought havoc in the clothing industry. Informal sector employment in clothing manufacturing is significant. The majority of micro and very small enterprises will feature primarily in the informal distribution of clothes, though there is an important manufacturing potential. Small cut, make & trim (CMT) firms are an important part of this manufacturing potential. The African Growth & Opportunity Act (AGOA) enacted by the United States could be the key to major export opportunities for South African manufacturers.

- 9.2.5 **Secondary Agriculture (Food Processing) Sector:** Food processing (of which the processing of agricultural products is a large component) accounts for 15% of the manufacturing sector. This process of deregulation and liberalisation has raised competitive

pressures, which, in turn, have accelerated the restructuring of the food processing industries. Although many of the food processing sub-sectors are very labour-intensive, huge investments also have to be made in the appropriate type of machinery and equipment to process basic agricultural inputs. Very little knowledge on the SMME component is available, except for the fact that it appears to be much larger than originally estimated. The competitive skills requirements and technological skills requirements of this sector hinder the entry of SMMEs into this sector. It is doubtful whether really small-scale enterprises have the competitiveness skills and technology to exploit opportunities in the secondary agriculture sector.

- 9.2.6 **Tourism:** The tourism sector has the potential to be South Africa's largest employment sector, largest foreign exchange earning sector and largest economic sector in terms of GDP. In addition to the potential for tourism to increase foreign exchange earnings, it is a multiplier domestic industry. That is, domestic tourism and hospitality operations create economic activity and employment. This sector is largely dominated by SMMEs and micro organisations.

Due to the lack of statistics and the fact that there is no formal registration of formal and informal employers in this Sector, it is estimated that more than two thirds of the approximately 42 000 Sector employers are SMMEs. In addition, a substantial part of the sector is primarily involved in food preparation, food and beverage service and catering – for the general population, not only for tourists – so they are located where their markets are concentrated. (i.e. in urban areas)

9.3 Ranking of Sectors for Intervention

As the following table shows, the Construction sector holds considerable promise or potential for a targeted Business Linkages intervention. Spending and growth trends are positive, and the sector is characterised by a dominance of micro and small size enterprises, in both urban and rural areas, and a highly positive regulatory environment.

The Tourism sector runs second although the issue here would be one of ascertaining “depth” of target business in terms of micro-size enterprises or poverty related criteria. Also, a relatively small-scale World Education intervention could be overshadowed by the current, multi-million Rand Tourism Enterprise Programme (TEP) project, which encourages linkages and business deals with the provision of financial inputs or subsidies.

The other three sectors rank somewhat lower, particularly due to capital requirements, uncertainty over land ownership and reform, and uncertain policy environments.

While both the construction and tourism sectors could provide an arena in which demonstrate a workable market development model for World Education Ntinga, it must be kept in mind that the South African economy – although sound in its essentials – appears prone to external shocks and perceptions over which it has little control. Afro-pessimism, combined with the global stock market downturn, could mean that promised foreign investment and inflows decline in coming months. Increasing inflation has been a concern to the Reserve Bank, and if this trend continues, an interest rate hike could adversely affect demand for higher-end construction products.

SUB-SECTOR SELECTION MATRIX

RANKING: **1** = LOW **2** = MEDIUM **3** = HIGH

TABLE 1

INDICATORS	AGRICULTURE		CONSTRUCTION		CLOTHING		SECONDARY AGRICULTURE (Food Processing)		TOURISM	
	RANK/EXPLANATION	RANK/EXPLANATION	RANK/EXPLANATION	RANK/EXPLANATION	RANK/EXPLANATION	RANK/EXPLANATION	RANK/EXPLANATION	RANK/EXPLANATION	RANK/EXPLANATION	RANK/EXPLANATION
Sub-sector Growth Trends (public, private and other levels of activity)	1 -Declining production. -Land Redistribution bottlenecks. -No major new investment.	2.5 -Public sector commitment to increase spending in order to kick-start the economy -Building of large infrastructure projects. -Local Economic Development	1 -Increased competition from imports -Restrictive labour legislation. -Import tariff phase down -Highly unionised environment.	1 -Produces for the domestic market only. -Overall decline in disposable income and consumption demand.	2 -Sector has the most potential but is not yet to exploited fully. -Negative perception about crime in South Africa. -Lack of capacity and skills.	2 -Funds are available through the Land Bank, LRAD and SLAG schemes. -But the lack of prime agricultural land, and a lack of know how & technology make entry for PDI firms difficult.	3 -Skills capacity (although requiring improvement) and technology do exist within this sector.	2 -Business loans available through formal and informal financial institutions. -Skills levels adequate. -Technology can be an inhibiting factor.	1 -Prohibitive skills technological and capital requirements.	2 -Capital requirements high, but funds are available from various sources -Skills and technological requirements can be prohibitive.
Proportion of PDI Small and Micro-Enterprises currently participating in the sector	2 53.23%* (are small and micro enterprises)	3 91.55%* (are small and micro enterprises)	2 -Figures are not available -Consists of a number of small cut, make and trim firms and hawkers.	1 -Figures are not available -Large firms predominate	2 -60% are estimated to be small, medium and micro enterprises	Ease of Entry of Small and Micro PDI firms: Capital Skills Technology ✓ x x	✓ ✓ ✓ ✓	✓ ✓ ✓ ✓	✓ x x x	

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*Nisika. State of Small Business in South Africa- Annual Review 2001.

INDICATORS	AGRICULTURE		CONSTRUCTION		CLOTHING		SECONDARY AGRICULTURE (Food Processing)		TOURISM	
	RANK/EXPLANATION	RANK/EXPLANATION	RANK/EXPLANATION	RANK/EXPLANATION	RANK/EXPLANATION	RANK/EXPLANATION	RANK/EXPLANATION			
Positive/ enabling regulatory environment	1	-Extreme uncertainty around land redistribution, land tenure and property rights.	2	-Public sector pushing preferential procurement policy. -Private sector demonstrating a willingness to increase investment spending.	1	-Union and labour issues can be prohibitive. -tariff protection to be phased out.	2	-Plethora of health regulations adds greatly to the cost of entering this sector.	2	-Compliance with environmental and safety regulations can discourage entry of PDI firms.
Degree of openness of large firms to working with smaller firms	2	-Anecdotal evidence exists	2	-Documented evidence and examples.	2	-Evidence of outsourcing to small cut, make & trim firms	1	-Evidence unknown	3	E.g. casino developments
SCORE	8		12.5		8		6		11	

TABLE 2: REVERSE RANKING (HIGHER SCORE INDICATES NEGATIVE PROSPECTS)

INDICATORS	AGRICULTURE	CONSTRUCTION	CLOTHING	SECONDARY AGRICULTURE (Food Processing)	TOURISM
	RANK/EXPLANATION	RANK/EXPLANATION	RANK/EXPLANATION	RANK/EXPLANATION	RANK/EXPLANATION

Comparative intensity of negative factors – fraud, corruption, poor policies, capacity etc.	<input checked="" type="checkbox"/>	Poor land policies, land occupations, farm killings; lack of clarity on government intentions contribute to a high negative perception of the agricultural industry.	<input checked="" type="checkbox"/>	Some concerns exist around PDI capacity.	<input checked="" type="checkbox"/>	Lack of capacity, customs fraud, exploitation of labour, closure of a number of clothing manufacturers.	<input checked="" type="checkbox"/>	Capacity and technical skills issues are of major importance.	<input checked="" type="checkbox"/>	Afro pessimism, corruption, crime and poor customer service levels.
Competition from other BL Progs.	<input checked="" type="checkbox"/>	-Agrilinks	<input checked="" type="checkbox"/>	-SAIBL (?)	<input checked="" type="checkbox"/>	Unknown	<input checked="" type="checkbox"/>	Unknown	<input checked="" type="checkbox"/>	-Tourism Enrichment Programme (TEP); SAIBL
SCORE	6		3		3		4		5	

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