

Financing Small-Scale Manufacturing in South Africa – The Egg and Chicken Problem

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Abstract

Finance is a notable barrier to the growth of small businesses in South Africa. Scholars agree that accessible and affordable finance can help grow small businesses and develop the economy. Even with such evidence South Africa still has a poor record of manufacturing besides the progress made in agro-processing, automotive assembly, and mining. The country imports large amounts of clothing, home goods, and equipment. This paper investigates the quest to create a growing manufacturing sector by the South African government through funding. This paper is a desk review of the funding processes at the Industrial Development Corporation, Small Enterprise Finance Agency, and Gauteng Enterprise Propeller. It provides an overarching view of requirements, processes, and context. The analysis juxtaposes the requirements versus realities of manufacturing as cited in the introduction and the literature review. It is evident from this review research that South Africa does indeed have a problem of what comes first in its quest for growing small-scale manufacturing. The type of requirements, support available, and contextual understandings must be studied by policymakers equally or more like technical abilities of manufacturers. This paper further suggests that a developmental approach to financing small scale-manufacturing be adopted.

Keywords

Finance(ing), Manufacturing, Small-scale, Growth and Funding.

1. Introduction

This paper tackles the challenge of funding and financing of small-scale manufacturing in South Africa. The country has a small manufacturing sector, and this is besides many attempts to create new manufacturers (Matthee and Heymans, 2013). Funding and financing are scarcely available for small scale manufacturers and hard to access due to stringent financing criteria (Marwa, 2014). The preparedness of small-scale manufacturers to fulfill the funding criteria is another challenge.

Small scale manufacturers fall in the category of small and medium enterprises. They acquire financing and funding within the provisions made for small and medium enterprises (Khoase and Ndayizigamiye, 2018). Small scale manufacturers are not exempt from the stiff competition of funding and financing that affects all sorts of small and medium sized businesses. The points at which an enterprise meets the funding criteria vary and is dependent on a lot of factors such as: readiness of the business to apply for funding, compliance with tax laws, up-to-date registration documents and financial records that show viability (Alexander, 2011).

Funding and financing are part of a broad range of challenges that face small and medium business (Cant and Wiid, 2013; Ramukumba, 2014; Zondi, 2017). The broad range of challenges (like the financing criteria) include stringent regulations that govern businesses, levies that choke cashflow in the context of small businesses, lack of funding and finance products directed at small and medium enterprises, and a meager small scale manufacturing sector. Relative research has shown a relationship between finance, funding, and growth (Cant and Wiid, 2013). If the funding and finance challenge is not tackled the small-scale manufacturing sector in South Africa will rarely experience growth (Mboniyane and Ladzani, 2011).

The rest of the paper consists of a literature review, methods, data collection and a data analysis. Implications for the industrial engineering and operations management research are shared at the end of this paper.

1.1 Objectives

This research is a contribution into debates about funding and financing of manufacturing activity in developing country contexts. It is a specific reference to South Africa's three major players in the financing of small-scale manufacturing. The following are the research questions and objectives of this desk review.

The research questions are:

- What are the components of developmental funding or financing process(es) for small and medium enterprises?
- If at all, does the funding or financing process(es) assist small scale manufacturers?

The research objectives are:

- to unpack the challenge of funding and financing the small-scale manufacturing
- and explore requirements, processes, and context of funding manufacturing in South Africa.
- to juxtapose the work of financing and funding agencies in relation to small scale manufacturers.

2. Literature Review

This paper is foregrounded in the small and medium enterprises literature. It appreciates the scale and complexity of the challenges that face small businesses with specific reference to the case of small-scale manufacturing. The challenges that face small and medium enterprises in South Africa are complex and exacerbated by the raging economic inequalities that exist (Zondi, 2017). As a result South Africa has the highest failure rate of small and medium enterprises (Rodney Nkwini and Mashau, 2020). The challenges that small and medium enterprises face are not purely an economic inequalities issue but a combination of issues such as stringent business regulations, rigid labour laws that prevent small business from accessing affordable labour, unreasonable funding requirements and exclusive selections in enterprise financing (Rasiah, 2011).

Ramukumba, (2014), an optimistic scholar, suggests that besides structural problems that small and medium enterprises face they play an enormous role in the economy and exclaims that the product(s) on offer are the course for sustenance of these businesses. This analogy and similar others fail to consider the challenge of getting a product through all the different phases and trying it out until it is successful. Succeeding on the basis of a product and gaining market access is tied to the entrepreneurial character of the new business owner or product producer (Slavec and Prodan, 2012). In a funding scarce context attracting support and overcoming the structural problems or challenges is difficult; and costly (Mboniane and Ladzani, 2011).

Malaysia, China and India are countries that achieved sustainable economic growth because of manufacturing (Rasiah, 2011). South Africa's policy makers look up to these countries and several others for practices to grow the country's economy through manufacturing (Gumede and Rasmussen, 2002). However, the breaking point and a disjuncture occurs in adopting foreign practices that differ by context, level of development and modelling. The other country practices are practical and useful, but limited by region, country and business culture (Slavec and Prodan, 2012; Rodney Nkwini and Mashau, 2020). The pre-existing conditions for growing manufacturing activity and focusing on developing small scale manufacturers require a tailor made approach, that unlocks both local and external investment (Sasidharan, Lukose and Komera, 2015). It is not enough nor helpful for policymakers to borrow practices from elsewhere without exhausting all local channels of development.

Government budget allocations for financing of small and medium enterprises is an emerging body of research that provides a basis for scrutinizing government agency functions (Girma and Vencappa, 2015). The government advocacy for financing economic activity runs short of ideas and is self-exposing to scrutiny. For example in South Africa the failure of government led Local Economic Development Initiatives creates an impression that the state is incapable and cannot support small scale manufactures (Black Economic Empowerment Commission (South Africa), 2001). Ordinarily the small-scale manufacturers produce everyday products such as furniture, food packaging and building materials. Their time is bound, and they are constantly concerned about customer numbers.

The responsibility of growing the small-scale manufacturing activity cannot be placed squarely on government. Large corporations in the private sector must adopt small manufacturers to help them develop (Khoase and Ndayizigamiye, 2018). The large corporations instead advance themselves, create monopoly in the various sectors and profit at the suffocation of small ventures. It is true that the government has the primary task of leading developments, protecting property and labour rights – but is also dependent on big business to pay taxes (Dean, 2017). This shows that private sector has and is continuing the path of being untouchable, while maintaining their monopoly positions.

This literature can be summarized as one that shows the ugly and the good of funding and financing support for the small business sector. The theoretical problem of small and medium enterprise finance is situated in the challenges and problems literature on challenges facing small and medium enterprises (Cant and Wiid, 2013; Ramukumba, 2014; Zondi, 2017; Rodney Nkwini and Mashau, 2020). To make any significant contribution into addressing the problem more time must be spent on research that is interested in context, process and those problematic conditions presented by pre-set criteria for financing and funding.

3. Methods

This research is a desk review of finance and funding products from three government agencies. The products cover regional, national, and sectoral offerings. The desk review sources are:

- Funding and Financing process of Gauteng Enterprise Propeller (GEP), Small Enterprise Finance Agency (SEFA) and Industrial Development Corporation (IDC).
- Annual 2019/2020 reports of the three agencies.
- Supporting information available on the web-platforms of the specified agencies.

This research focuses on the recent funding and financing processes as published by GEP, SEFA and IDC. The desk review allows for an independent query (Hjertman, 2017) into the contextual application of these processes and explores the criteria for accessing the funding and finance offerings. The query is within the premise of the multiple challenges facing small businesses. This approach acknowledges that finance and funding is not an absolute vehicle for small scale manufacturers to achieve success and growth, but it is a positive contributor to enterprise development.

The desk review method of this research takes into consideration the quantitative and qualitative elements of the documents reviewed (Hjertman, 2017). The quantitative information includes the range of amounts available for funding small and medium enterprises, the values of funding already injected into manufacturing during the specified reporting periods and funding or financing by sector. The qualitative detail provides summaries of the work done by the different agencies and juxtaposes critically the funding criteria, process and the promise of funding and financing.

The two-pronged approach to this desk review distances itself from the other approaches that seek to suggest that government interventions always yield results (Sileyew, 2019). In the same breadth this research does not assume weakness about the funding and financing offerings that the agencies reviewed have to offer. Instead, the two-pronged approach shows a full picture and reflection about the experiences that small and medium enterprises undergo to access funding and financing. In turn this study carefully explores the relevance of the set criteria, the navigability of the processes and the contextual matters of the different funding and financing offerings.

The applied methodological approach is an arena within which the different financing and funding concepts are explored. The exploration is two pronged and recognizes both the qualitative or quantitative elements relevant to the case of funding and financing small-scale manufacturing. It overcomes limitations of desk reviews that take a single and a strict approach (Sasidharan, Lukose and Komera, 2015). For this research a single approach would be limited by (1) the necessity to provide contextual information and background, (2) juxtaposing the financing and finance requirements, criteria and process which is qualitative; then the (3) funding ranges and (4) the financing and funding spending on manufacturing by the three agencies reviewed.

4. Data Collection

Data is collected from the websites, reports, and publicly available documents of three funding and financing government agencies. Data is carefully selected and covers the following categories:

- Funding and financing ranges

- Offerings
- Criteria and requirements
- Process(es)

The documents and reports reviewed are for the 2019/20 reporting period. The documents and publicly available data are from the following set of records:

Table 1: Sources of Data

Data Source	Location	Agency
Annual Report 2020	sefa.org.za	Small Enterprise Finance Agency
Integrated Report 2020	idc.co.za	Industrial Development Corporation
Integrated Annual Report 2019/20	gep.co.za	Gauteng Enterprise Propeller
<ul style="list-style-type: none"> • Financial Support – Webpage • Funding (Loan) Application Process • Interest rate 	gep.co.za/what-do-we-do/financial-support	Gauteng Enterprise Propeller
<ul style="list-style-type: none"> • Small Enterprise Manufacturing Support Programme • Direct Lending Products • Finance Solutions Brochure 	sefa.org.za/services/SEMSP sefa.org.za/services/direct	Small Enterprise Finance Agency
<ul style="list-style-type: none"> • Light Manufacturing Sector • Funding Across Multiple Industry Sectors • How to apply for Funding 	idc.co.za/light-manufacturing idc.co.za/who-how-we-help	Industrial Development Corporation

The sources of data show the ranging sets of records considered in this study. In the analysis various extracts are considered and juxtaposed with the contextual reality. The sources help explain the “egg and chicken” conundrum since enterprises must be in particular ways investment ready before they can access or become eligible for funding and financing. This then is a conundrum in terms of what comes first. A struggling small-scale manufacturer may not have all the requirements while the government agencies use such to determine eligibility and the same agency promotes itself as a development financier or funder (Cant and Wiid, 2013; Ramukumba, 2014; Girma and Vencappa, 2015). Such leaves the funding and financing agency fraternity with the question of what really comes first and the various funding and financing process considerations.

5. Results and Discussion

Funding and financing made available by IDC, SEFA and GEP in the year 2019/20 are presented. Their presentation does not withstand the covid-19 outbreak that sunk the global economic activity. It considers the already budgeted and utilized funds by these agencies. In the quest to provide a full and a clearer picture of the processes that small and medium enterprises undergo the following analysis of results are co-presented and discussed:

- Eligibility
- Funding/Financing criteria
- Process(es)
- Challenges
- and suggestions for improvement

The results show a table and a graph focusing on the scoring of the different funding and financing criteria. The suggestions for improvement emanate from the set of results and provides ideas worthy of further exploration by researchers, decision makers and small-scale manufacturers.

5.1 Numerical Results

This section explains numerically the funding and finance processes employed by the three agencies studied here. The funding process entails the following as summarized from Small Enterprise Finance Agency, (2020); Gauteng Enterprise Propeller, (2021); Industrial Development Corporation, (2021):

1. learning about the available funding and financing offers
2. establishing eligibility and funding requirements
3. deciding on a suitable offer
4. assessing the enterprise’s eligibility and ability to meet the set requirements
5. determine submission channels and make submission or take steps to meet requirements

These steps are not always followed in the order stated above because at different points enterprises may consult the agencies and source advise that can either fast-track an application decision or provide reasons a small enterprise cannot apply. However, enterprise capabilities to comprehend and follow through the application process are a key determinant of participation in the funding processes. At step 5 enterprises that are incapable of meeting the requirements will self-exclude from the process even if they had a good product. Thus, the eligibility and requirements present an egg and chicken problem. In this case a product may be good but cannot attract funding because of the other factors or requirements not directly related to production capabilities.

The table below scores the eligibility criteria and requirements by agency based on importance. The importance determines from the analysis of publicly available web data and information. The scoring uses a 1-10 points scale, 1 is less important a criterion and 10 extremely important.

Table 2: Funding/Finance eligibility and requirements

Agency	Security/ Collateral	Compliance (Tax etc.)	Shareholder Contribution(s)	Sustainability	Refinance	BEE
GEP	6	10	1	8	0	10
IDC	8	10	10	9	5	5
SEFA	3	10	5	7	3	5

These agencies share a common policy guide, and this is reflected by the adopted set of eligibility factors and requirements. However, some of their practical approaches differ. GEP, is a provincial fund and smaller than IDC and SEFA. It adopts a strict eligibility criterion with no compromise on compliance (business registration and tax), including the sustainability of the product manufactured as well as the practices. IDC unlike SEFA and GEP requires shareholders to match the financing it offers and a 50% focus on the Black Economic Empowerment. SEFA follows a developmental approach to financing small and medium enterprises. SEFA places little emphasis on collateral in the earlier stages of the application process but works with applicants to develop collateral.

5.2 Graphical Results

The funding and financing eligibility requirements play a key role in the design of the small and medium enterprise support programmes (Snyman *et al.*, 2014). Both political and economic reasoning has to be considered in the crafting of these requirements if the interest is to create access to finance (Alexander, 2011). The role of political reasoning in this instance is ensuring fair and equitable access – at present the Broad Based Economic Empowerment is considered a model for this but still presents challenges for investment driven projects, with pure economic intentions (Srai *et al.*, 2016). In the same way that pure economic intentions in manufacturing can exclude the marginalized groups while benefiting from funding that is set aside for both economic and political emancipation.

The graphical results show the following:

- All agencies require full compliance in terms of tax, business registration and accreditations.
- IDC requires full commitment from all enterprise shareholders by way of financial contribution.
- Unlike the IDC and SEFA, GEP does not guarantee refinance to most of its finance or funding recipients.
- The Black Economic Empowerment (BEE) is an important consideration in the financing prospects of all the agencies. Even though there’s varied scoring in this category – it remains as recorded a governmental directive that the BEE policy be enacted in the finance processes.

- The sustainability factor is of interest to all agencies, it begins with evaluating the product offer and wide set of verifiable information to back the viability of the investment, and possible returns.

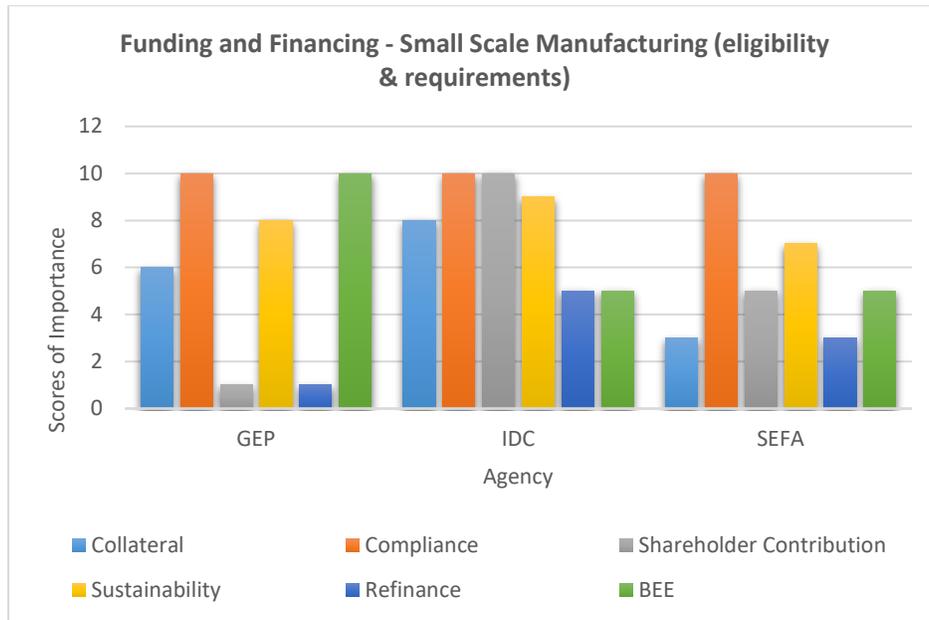


Figure 1 - Funding and Financing Eligibility and Requirements

5.3 Proposed Improvements

The eligibility criteria and requirements prove in the case presented in this paper to be a specific barrier to accessing finance and funding by small and medium enterprises. Zondi, (2017) shows that for small businesses to thrive funding and finance must be available for the different stages of enterprise development. While the agencies offer different funding packages, they remain locked into the stringent requirements and are less developmental in their approach. They insist on collateral, that is not readily available in the small but promising manufacturing enterprises – including shareholder contributions, unreasonable proofs of sustainability and leaving no room for development.

Following the review of the various offerings, processes, and requirements it is recommended that funding and financing agencies in South Africa and elsewhere, consider the following:

- Adopting a developmental approach to financing small-scale manufacturing
- Learning about the production processes of the enterprises needing finance
- Drop the step-by-step funding and financing process but increase focus on product sustainability and viability
- Equip potential enterprises with alternatives and offer experimental grants.

In Malaysia and India, the developmental funding approach supported by government and private sectors has demonstrated success. According to Padachi, Howorth and Narasimhan, (2012) traditional sources of financing incorporated into the modern-agency driven sources of finance increase the success of small businesses in Malaysia. A developmental approach would further allow GEP, IDC and SEFA to assist small businesses to diversify their funding sources and achieve productivity in return as it has been the case in the Malaysian context (Rasiah, 2011).

6. Conclusion

This review shows that there is an opportunity to explore the role of financing and funding agencies beyond the three selected here. From this review it can be concluded that finance and funding agencies cannot on their own meet the needs of small-scale manufacturers. The work of financing and funding agencies when juxtaposed with the manufacturing requirements, the need for refinance and grants it does not enable small-scale manufacturing activity to thrive. The funding and financing sector is obsessed with stringent requirements and in process is inhibited from

adopting a developmental approach. Future research can adopt an empirical approach and address the possibilities of adopting a developmental approach to financing small scale manufacturers.

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Biography

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