A DEBATE AROUND DIFFERENT PATHWAYS TO JOB CREATION IN SOUTH AFRICA

PART 1: MEDIUM SIZED ENTERPRISES ARE THE MOST EFFECTIVE AND EFFICIENT ROUTE TO JOB CREATION FOR SOUTH AFRICA

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OVERVIEW

- South africa is in a well-researched predicament when it comes to its struggle with sustainable job creation, even as africa's most advanced economy. One fundamental job growth inhibitor is how the country's education and training systems are out of sync with the economy. The country is also losing ground, over the long term, in historically labour intensive industries like mining, manufacturing, and construction. The covid-19 pandemic has made the existing focus on the fourth industrial revolution (4ir) even more critical.

- To address these challenges, entrepreneurship has long been lauded as a key job creation and skills development lever. Agreeably mass entrepreneurship, specifically, offers people the most agency over meaningfully transforming their socio-economic circumstance given its seemingly low barriers to entry. However, despite the lower barriers to entry, starting and growing a small or micro-enterprise remains challenging in the south african context. The historically slow traction in driven jobs, likely indicates that mass entrepreneurship is incredibly inefficient when it comes to job creation.

- In contrast, while mass entrepreneurship is traditionally positioned as the "missing middle" between survivalist enterprise and large companies mass entrepreneurship is incredibly inefficient when it comes to job creation. The case for greater focus on assisting established, mid-sized companies is both is anchored on scale and sustainability and less so pace of job creation. Some key opportunity areas apply to both domestic, export, and hybrid mid-sized businesses. For entrepreneurship to truly realise its job creation potential, we need to start betting on entrepreneurs with traction and reliable, predictable success

South Africa is in a well-researched predicament when it comes to its struggle with sustainable job creation even as one of Africa's most advanced economies. According to the broad definition of unemployment that rightly includes discouraged job seekers, the country boasts a staggering 43.1% unemployment rate as of quarter 3 of 2020. Paradoxically, this is the cumulative effect of Covid-19 knocking 2.2 million people into unemployment amidst an already struggling economy and major sectors increasing their employment numbers. Formal sector employment increased by 242,000 (2.4%); informal sector employment by 176,000 (7.7%); private households by 116,000 (11.5%); and employment in agriculture increased by 9,000 (1.1%). This accordion-style ebb and flow of the South African job market means there is an equilibrium of people flowing in and out of stable employment in a way that has kept pre-Covid unemployment rates at a near-constant 29-30% since July 2019. This plateau is antithetical to growth, which is undoubtedly what South Africa needs but is battling to realise. (Gqubule, 2020)

One fundamental job growth inhibitor is how the country's education and training systems are out of sync with the economy. While South Africa outputs more high school/tertiary graduates and trained artisans than the economy can absorb, there remain significant skills shortages in key strategic sectors (Kalie Pauw, 2006) . So not only are students graduating into automatic redundancy, but important growth sectors are scrambling for talent. This cross-cutting mismatch is further crippled by structural xenophobia that does not sufficiently facilitate foreign nationals with critical skills easily plugging skill shortages in ways that are complementary to the local workforce. Instead, the labour and employment landscape is perceived on both a governmental and societal level as zero sum, i.e. if foreigners get jobs; it means South Africans do not. This approach is neither productive nor expansive in its thinking.

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The country is also losing ground, over the long term, in historically labour-intensive industries like mining, manufacturing, and construction. Momentum around the fourth industrial revolution is not matched by a sober assessment of what innovation-driven transitions away from more legacy sectors and operations mean for the jobs we relied on those sectors for. In quarter 3 of 2020, for example, manufacturing shed 30,000 jobs, construction lost 24,000, trade dropped by 21,000 and utilities decreased by 18,000 jobs, for example (Krugel, 2020). This can be attributed to an inability to maintain a globally cost-competitive resource base, work becoming less labour intensive due to technology – particularly in secondary industries such as manufacturing, a shift in global priority and demand to renewables, and the reduced competitiveness of local manufacturing, both in technology and the scale of production.

The Covid-19 pandemic has made the existing focus on the fourth industrial revolution (4IR) even more critical but embracing 4IR has not nearly been swift and comprehensive enough. For example, the rise in demands for renewable energy presents an opportunity for South Africa given that most wind turbines are made of advanced steel alloys that require metals such as manganese and chrome, of which South Africa has the world's largest mineral reserves of. Complementing this natural endowment with a talent pool of technologists, engineers, environmentalists, scientists, and other workers to make the sector commercially viable and internationally competitive is a logical next step - but can the country coordinate efforts to take it? (Schwab, 2016)

To address these challenges, entrepreneurship has long been lauded as a key job creation and skills development lever. This is typically by creating work opportunities for graduates and others, building new high growth sectors to make up for declining ones, or innovatively addressing skills gaps. There are two forms of entrepreneurship typically touted in regards to the pathways to job creation:

1. ***Mass entrepreneurship***
   these are typically small local businesses that generally use local inputs to meet the needs of consumers, with a moderate impact on job and wealth creation within their sectors and local communities. These generally have viable business models with proven profit potential, and due to their high volumes have potential to create a large number of direct jobs.

2. ***High growth entrepreneurship***
   defined for the purposes of this document as established medium stage enterprise that typically produce hundreds to thousands of jobs across a relatively small number of businesses. They typically operate with high barriers to entry, require large capital and human resources, and tend to have value chains that span multiple geographies.

In this article we explore the case for high growth entrepreneurship as the pathway to job creation in South Africa. We seek to make a case for High Growth as a key strategic levers for actors in the job creation ecosystem to coalesce and pull on to drive job creation at both the pace and scale at which it is required. We also discuss the limitations of a focus on mass entrepreneurship as an alternative pathway to job creation.

Why not Mass Entrepreneurship?

Agreeably mass entrepreneurship, specifically, offers people the most agency over meaningfully transforming their socio-economic circumstance given its seemingly low barriers to entry. The appeal of the relatively straightforward maths of having millions of diverse entrepreneurs creating work for just a few others is understandable and gaining traction in India, Senegal, and China (Venkatesan, 2018). The latter saw 13 million new businesses registered in just the three years between 2014 to 2017. And yet, The Global Entrepreneurship Monitor is seeing a year-on-year decline in people who believe they can become successful entrepreneurs and instead prefer the stability of being employed given how tough it is to be the employer. (Advisors, 2019)

A 15-year longitudinal study focused on South Africa found that only about 1% of micro-enterprises who employed less than five employees at founding could grow to employ 10 people.

However, despite the lower barriers to entry, starting and growing a small or micro-enterprise remains challenging in the South African context. A 15-year longitudinal study focused on South Africa found that only about 1% of micro-enterprises who employed less than five employees at founding could grow to employ 10 people (Solomon, 2013). 73% of SMEs surveyed in the International Labour Organisation's 2016 Enabling Environment for Sustainable Enterprises believe that the regulatory environment is making it more difficult for small businesses to compete with larger businesses. To add to this, a 2014 MSME Growth Index study showed that business owners needed around eight working days a month to sort through with regulatory red tape. Running a small and micro-enterprise is also inherently risky given unproven viability of their business models and how little financial buffer most businesses have at the onset to survive their teething stages. These businesses also face the uphill battle of competing for market share in South Africa's monopoly-driven economy, where the average worker has only ~R14,577 in monthly take-home pay to spend. Bigger actors certainly make a habit of quickly and easily outcompeting niche, artisanal competitors to leave mostly gaps in the volatile SME/survivalist space. Survivalist enterprises generally do not create significant incomes, and often do not pay the entrepreneurs themselves a fair market wage. Even opportunity-driven SME entrepreneurs are cash strapped, such that creating and validating a business model on the job are unlikely to be able pay significant salaries.

The historically slow traction in driven jobs, likely indicates that mass entrepreneurship is incredibly inefficient when it comes to job creation. The South African small and micro businesses that make up the mass entrepreneurship ecosystem created a steadily unchanging 16 - 17% of total jobs between 2011 and 2016 but were 92% of formally registered firms in that same period. By comparison, the Small Business Institute reports that as many as 56% of jobs in South Africa are created by the 1,000 largest employers, including the government. (Smit, 2004)

Why high growth stage businesses?

In contrast, while mass entrepreneurship is traditionally positioned as the "missing middle" between survivalist enterprise and large companies, there is, in fact, a far more missing, more genuine "middle": established, mid-size businesses i.e. high growth entrepreneurs. Internationally, 101 - 999 full-time employees and a turnover above USD 10 million is the spectrum of "mid-sized". In the domestic context, 51-250 employees and as low as USD 2.1 million in turnover in agriculture, for example, qualifies. Turnover that qualifies a business as midsized can be as high as USD 13.5 million for wholesale, USD 12.9 million for mining and quarrying, and USD 10.5 million for construction and manufacturing. For consideration as an established, mid-sized business, passing the 2 - 5 year business survival milestones is also key. Compared to mass entrepreneurship, mid-sized businesses offer more reliable job creation potential but are still neglected in terms of national priority and dedicated support for scale. These businesses bring established business models with traction; a greater level of income security through more sophisticated instruments like debt, trade credit, or cash; are subsequently significantly more resilient during downturns; tend to pay higher wages than smaller businesses; and more reliably contribute to overall productivity by providing the government a gainfully employed tax base and simultaneously reducing the number of unemployed people the state needs to provide welfare for.

At the absolute least, ~1,200 mid-sized businesses that employ the upper boundary of 250 employees need to realise sustainable success to meet the Government's target.

The case for greater focus on assisting established, mid-sized companies is both is anchored on scale and sustainability and less so pace of job creation. A 2016 Global Entrepreneurship Monitor study estimated that of South Africa's 2.9 million entrepreneurs, 2.1 million are early stage and just 800,000 are established (Entrepreneurial Behaviour and Attitudes, 2019). Given these numbers, the relatively conservative targets from key actors like Government and Business for South Africa (B4SA) ranging from the creation of 300,000 to 1.5 million jobs should not be as unattainable as they currently are. At the absolute least, ~1,200 mid-sized businesses that employ the upper boundary of 250 employees need to realise sustainable success to meet the Government's target. The questions to answer are what is difficult about this and what would it take to make this happen? To start, we need to identify growing, strategic sectors that are less constrained by politico-economic binds like volatile commodity prices, a declining exchange rate, the privileging of certain state-owned enterprises over private competition, and oligopolies. Strong sectors can include manufacturing (automobile, chemical, textile, and food), services (tourism, financial services, legal, communications, and transport), and energy (fossil fuel and renewables). The next question to ask is what established, mid-sized businesses are serving the growing needs of this sector well? What are the characteristics of their success that can help develop indicators of predictive success in other businesses? What would it take to get them to meet demand more consistently? This is a sharp pivot from the value chain analysis approach, where stagnant sectors are scrutinised to see what other jobs can be created within them regardless of their marginal utility or genuine relevance.

Already, some key opportunity areas apply to both domestic, export, and hybrid mid-sized businesses. First is operational support; governments need to leverage data science and market intelligence expertise to predict and plug key resilience gaps as it did with the Temporary Employer/Employee Relief Scheme (TERS) that has helped various sized businesses keep its doors open and pay employees during the pandemic. Second is bridging the digital divide to allow established mid-sized businesses to more efficiently expand their reach by leveraging technology. Access to the right basics like affordable data, hardware and software, and sufficiently skilled professionals like data scientists and software engineers has always been critical but is so now more than ever given the digital-first paradigm shift brought on by Covid-19. Third, special development mandates are key for giving high potential mid-sized actors the necessary boost. Fiscal incentives like tax breaks and grant/loan facilities, favourable labour regulation updates, and protections against oligopolies that encourage diverse competition that is not easily pushed out of the market by large players.

For entrepreneurship to truly realise its job creation potential, we need to start betting on entrepreneurs with traction and reliable, predictable success. Focus on developing fewer businesses with a medium to high likelihood of job creation success offers a far more effective and efficient route than casting lots across hundreds of thousands of smaller, riskier ventures and holding on to hope that enough succeed to achieve the multiplier effect South Africa and the rest of the continent needs to make the most of its demographic dividend.

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