

Budget Speech Competition Essay

Small business is praised for its potential to create jobs and grow the economy. Do you believe that overall policy in the form of the newly released New Growth Path and the Industrial Policy Action Plan together with the budget support the development of small business in South Africa? Substantiate your answer with references to the relevant documents.

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1) Introduction:

This essay will contend that overall policy in the form of the New Growth Path, the Industrial Policy Action Plan and the budget, does support the development of small business in South Africa. Firstly the barriers to small business development will be established and the primary inhibitors of small business development in South Africa will be identified. Then the New Growth Path, the Industrial Policy Action Plan and the Budget will be examined, critically analysed according to their potential to help small businesses counter the several barriers identified and conclusions of the level to which they achieve this will be drawn.

This essay concludes by examining the policies as overall policy and this essay will test the level of coherence these policies achieve together. Overlaps and inefficiency's will be discovered and the reasons overall policy does support small business development in South Africa will be determined.

2) Requirements to develop Small Businesses:

Small and medium enterprises (SMEs) are extremely vulnerable to their business environment and as a result South African SME's have experienced a 75% failure rate; one of the highest in the world (Olawale and Garwe, 2010: 1). To develop SME's government intervention is necessary and this section highlights the several methods authorities can employ to promote the development of SME's.

2.1) Recommendations from External expertise

According to the CACCI¹ Recommendations on SME in 2003, the steps that governments can take to develop SME's are:

- Establish training programs to increase the skills of staff in SME's, specifically in computer and research skills.
- Provide cheap and accessible financing to firms, possibly from a government fund.

¹ The Caribbean American Chamber of Commerce and Industry

- Provide fiscal assistance to SME's by granting tax benefits to these firms and providing training or investing incentives.

2.2) Conclusions from studies in South Africa

Other studies have identified the bottlenecks that impede SME development in South Africa specifically and found that the many obstacles South African SME's face are: poor management skills, financing, imperfect competition and long bureaucratic processes (Kongolo, 2010: 1); as well as a lack of: access to international markets, access to information, technology and machinery (Abor and Quartey, 2010: 1).

From the journals referenced above it can be empirically concluded that to develop SME's in South Africa the government must aid local SME's by the methods outlined above. Specific attention must be paid to training, technology and financing. An analysis of whether the government policies contain any of these methods will help conclude the level to which overall policy is developing SME's in South Africa.

3) The New Growth Path: Does it develop Small Business in South Africa?

3.1) Fundamentals of the New Growth Path

The New Growth Path (NGP) can be summarised to contain one fundamental and essential goal: to create employment. The NGP aims to create 5 million jobs by the year 2020 (NGP, 2010: 8). SME's in South Africa contain 56% of South Africa's private sector employment (Olawale and Garwe, 2010: 1), and therefore when targeting employment one could make the rational assumption that the NGP will also target SME development to create this employment.

3.2) Positive NGP developmental strategies

The NGP dictates plans to assist the development of SME's and the strategies laid out on page 21 of the NGP attempt to solve several of the fundamental bottlenecks SME's face. It most importantly creates a one-stop shop and single funding agency that will allow SME's to get cheaper funding as well as plans for a state owned bank (NGP, 2010: 27) which will allow government to supply SME's with lower interest rates and relieve a portion of the burdens of debt on SME's. "Financial markets on their own often don't provide adequate funding for SME's" (Stiglitz, 2010) and the NGP certainly provides solutions to this problem. These low interest rates will greatly increase private sector investment and as a result increase the number and efficiency of SME's in the market.

The NGP also addresses the numerous problems of bureaucracy that SME's face. The NGP specifically outlines plans to eliminate "red tape" as well as increase the number of patents (NGP, 2010: 21-23). The elimination of costly and impeding bureaucratic processes will create a far easier entry into the market as well as create innovation through the use of patents. This will be encouraging to potential entrepreneurs and will increase the confidence of salesman to enter the market.

Jobs driver 3 in Appendix A of the NGP, also states a plan to diffuse new, green technologies to SME's. The distribution of technology to SME's will help them compete with larger firms and reduce the competitive barrier between large and small firms allowing SME's to gain a competitive edge in the market and spur SME innovation (Phaho and Pauris, 2008: 2-3).

On the three matters of financing, bureaucracy and technology, theoretically, the NGP confronts these problems successfully.

3.3) Inefficiencies in the NGP policy

With employment as the NGP's fundamental goal and SMEs accounting for over half of South Africa's private sector employment (Olawale and Garwe, 2010: 1) I feel that the development of SMEs should be somewhat of a priority; yet the NGP does not specifically acknowledge the important role SMEs play in employment and seems to render the large failure rate of SMEs as a lesser priority. The NGP appears to assume that indirect employment will occur by the multiplier effect (IPAP, 2010: 86) and does not place enough attention into direct employment of SMEs. With such a high failure rate of SMEs in South Africa, indirect employment will not likely occur by the projected multiplier (IPAP, 2010: 86) until the success of SMEs increases.

Severe impediments to SMEs are management skills and access to information. Firms need these skills to compete in the market and traditionally SMEs are weak in these areas (Berry et al, 2002: 79). The NGP does not state any plans to counter these barriers to SMEs and inefficiency in the policies effects will arise.

In conclusion, despite several inefficiencies the NGP does address several of the core issues facing South African SMEs. The attention paid to their need for financing, as well as, the elimination of unnecessary bureaucratic processes and technology distribution does meet the objective to develop SMEs.

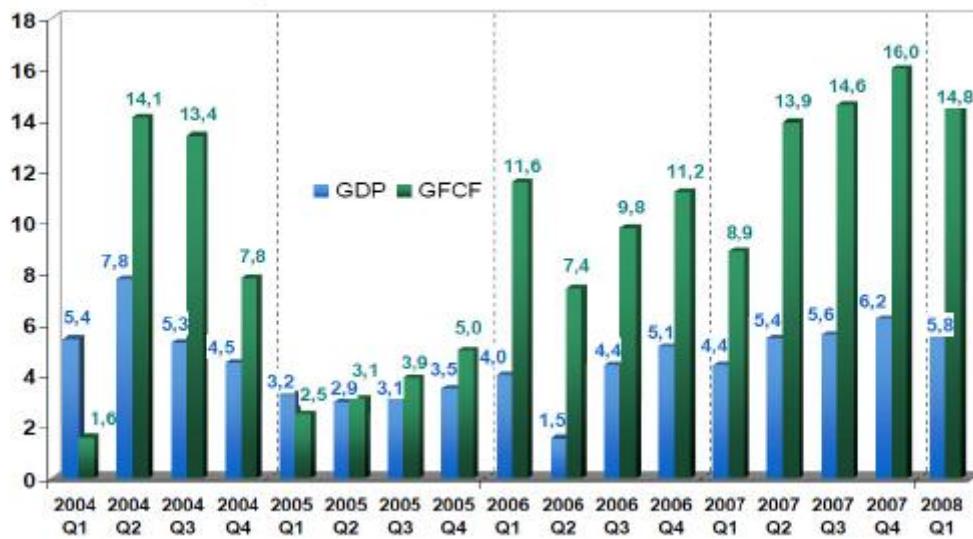
4) The Industrial Policy Action Plan: SME developer or inhibitor?

4.1) The Industrial Policy Action Plan: a likely catalyst of SME growth

The Industrial Policy Action Plan of 2010 (IPAP) is a well structured and detailed approach to South Africa's economic problems. Its attention to each specific industry and cohesive plans of action will help South African industries grow, and most importantly: SMEs.

Small business owners and potential entrepreneurs will be encouraged by the plans laid out in S7 of IPAP which is entitled: Industrial Financing. The focus on financing and the impending promotion of Development Finance Institutions (DFI) will create potential investment into productive sectors that will undoubtedly surge SME growth (IPAP, 2010: 16-17). Any doubt of this likely trend is contradicted by evidence given by a country in similar circumstances: Brazil. Brazil adopted a very similar financing drive with extreme attention paid to DFIs and government funding and the growth rates since their inception have provided evidence that government investment initiatives can be successful (de Lima Ribeiro, 2007: 15-20); this evidence is represented by the graph below²:

Brazil's investment growth: 2.5 times faster than GDP



The graph above shows the positive effect DFIs had on investment with the surge in growth witnessed in Growth Fixed Capital Formation (GFCF), a reliable measure of investment.

²Graph taken from (IPAP, 2010: 19)

Economic movements in Brazil are relative to South Africa as their economic environment is very similar to South Africa's (i.e. both a third world country and a developing country).

The correlation between an increase in investment and DFIs to an increase in the success of SMEs will theoretically be positive as this will solve the financing and capital barrier to SMEs. Financing and capital is recognised as the primary constraint on SMEs and IPAP's industrial funding and DFI program will develop SMEs in this manner (Kongolo, 2010: 1).

Economically, one can applaud IPAPs approach to imperfect competition in the market. Entrenched and established firms pose a major barrier to entry where the market is controlled, largely, by them and new firms lack the technology and management skills to compete (IPAP, 2010: 33). Imperfect competition creates an inefficient market (Bernheim and Whinston, 2008: 665-667) and the technical assistance and skills and management training that the government intends to distribute to SMEs³ will reduce this competitive barrier and allow greater SME entry and growth into the market. The training to staff and management will not only assist in reducing this competitive barrier but will open South African SMEs to foreign direct investment (IPAP, 2010: 86).

In conclusion IPAP will greatly enhance the development of SMEs through effective plans of financing, technology, competition and training initiatives. While it does not eradicate all barriers to SMEs; its plans, specifically in productive financing and investment initiatives, achieve the primary objective of developing SMEs.

³Examples of these intentions exist on pages: 51, 57, 66 and 86 of IPAP.

5) The budget support and its effects on Small business:

5.1) Hypothetical Goal for the Budget

To develop SMEs the budget will have to state the intended allocation of resources into either direct investment into SMEs or by reducing costs and barriers to entry.

5.2) The level to which the budget achieves the goal

The budget does create certain levels of relief for small businesses. For micro-enterprises with small revenue turnovers a tax relief shield will increase to R63 556 as well as a decrease in the tax rate from 10% to 7%. This fiscal assistance will decrease the costs of small businesses and therefore create potential to grow and most importantly: potential for new firms to enter the market (Gordhan, 2012: 7-8). The budget also states that bureaucratic tax processes will be reduced and the number of tax returns and payments will be reduced from 18 to 2 (Gordhan, 2012: 8).

5.3) Policy inefficiencies of the budget:

With the exception of a simplified tax regime and bureaucratic processes the budget does not fully support SME development. For the budget to support SME development the government must provide fiscal assistance in the form of tax incentives for training and investing as well as a government fund for SME financing (CACCI, 2003: 4). The budget does not support these initiatives and therefore fails on the whole as a small business developer. While tax benefits are granted to the business they are not granted to individual investors who, if they were given tax incentives, would invest in small businesses rather than the existing larger, more established firms (CACCI, 2003: 7-8).

In conclusion the budget provides some relief to small businesses and will allow for some level of growth in this manner. However, the ignorance of the budget to some of the fundamental and more serious barriers to SME development renders the budget as mostly unsupportive to SME growth on the grounds of limited training and investment incentives.

6) Overall Policy Cohesion: Successes and failures

6.1) Successful integrations of overall Policy:

On the whole a satisfactory level of coherence exists between the NGP, IPAP and the budget to bring about the development of SMEs.

Specific levels of excellence in potential SME development are found in plans for financing with the NGP and IPAP both releasing extensive plans for micro-financing through DFI's and government support as well as tax relief to small businesses from the budget. In effect, the three policies complement each other in the matter to spread finance to small businesses; and the overall policy successfully solves the fundamental barrier facing SMEs.

The assistance of government policy in other matters is not absent. All three policies share the goal of slashing unnecessary bureaucratic processes. Overall policy is complementary in this matter and the combined vendetta against administration issues achieves the objective of developing SMEs.

6.2) Inconsistencies and inefficiencies in the overall policy

The policies, if analysed individually, will counter most of the barriers facing SMEs. However, when the policies are analysed as a single unit, inconsistencies and a lack of support for each other arise.

The NGP and IPAP together appear to have correlated plans to address the issue of poorer technology in SMEs, IPAP in particular. There is no mention of spreading technology to SMEs in the budget and the support of the budget is essential for overall policy to successfully reduce the competitive barrier in the market.

The overall policy severely fails in providing SMEs with access to information and training for staff. IPAP produces several incentives and support for SMEs to train their staff and management; yet there is little mention of these incentives in the NGP and the budget. The absence of incentives in the budget will greatly inhibit SMEs in this manner. No mention or drives are created in the NGP and the Budget to increase SME's access to information. This will enhance the competitive barrier between small and large businesses and the lack of

cohesion of overall policy to reduce the market's inefficient competition hinders its ability to develop SMEs.

7) Conclusions:

In conclusion, the overall policy in the form of the NGP, IPAP and the budget does support the development of small businesses in South Africa. However, the severe problem of poor management and competition is not successfully addressed and needs such as training, access to information and personal income tax incentives are not supplied to small businesses. Yet, despite these inefficiencies; the meticulous improvements made to the financing, bureaucratic processes and technology of SMEs conquer the primary barriers to SMEs and it can, therefore, be empirically concluded that the overall policy is largely coherent and it collectively produces enough successful policy to develop small businesses in South Africa.

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