

# COVID-19 and post COVID-19 financing of MSMEs: A case of Johannesburg

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## Abstract

Micro, small and medium enterprises (MSMEs) are widely accepted as the backbone of economic growth and contribute towards job creation and poverty alleviation. The role that MSMEs can play is amplified in South Africa, given the poor performance of the economy, high levels of inequality and unemployment. The government has instituted several initiatives and policies aimed at fostering the growth of MSMEs. However, despite these efforts, MSMEs find themselves facing various challenges, including access to finance. COVID-19 threatened the survival and any growth prospects for MSMEs, but also prompted policy alterations in response to the crisis, aimed at delivering relief measures for the MSMEs. Therefore, this dissertation explored the impact of the COVID-19 policy responses on financing MSMEs in South Africa. Specifically, the study sought to understand the impact of COVID-19 on the financing of MSMEs in based in Johannesburg and the benefits and challenges that MSMEs experienced in their attempt to obtain debt relief or access to finance. The dissertation employed a qualitative research approach in which primary data is collected from participants through interviews with MSMEs in Johannesburg, South Africa.

The results of the thematic analysis found that financing options were required to support MSMEs with employee relief and retention, decrease in productivity, cash flow and supply chain issues, and information and communications technology (ICT) adoption. MSMEs encountered difficulties in trying to access finance, despite the credit guarantee schemes made available to them. A sentiment emerged that banks and government agencies exhibited a reluctance to attentively address the distinctive challenges faced by these enterprises, consequently constraining their ability to effectively communicate and navigate their specific circumstances. MSMEs also realized the importance of a compliant business as a prerequisite for accessing financial resources. An additional revelation pertained to the imperative of cultivating business resilience as a strategic imperative for enduring comparable crises should they transpire.

The results also found that there were some benefits and challenges that MSMEs experienced when exploring their financing options. The thematic analysis identified two key benefits that MSMEs experienced in their attempt to obtain debt relief or access finance during the pandemic. These included the increased resilience and diversification of MSMEs. The two main challenges

that MSMEs experienced where the inability to access employee relief schemes and access finance.

It is recommended that MSMEs be educated on bank processes and requirements, business management, financial literacy and alternative sources of finance so as to illustrate the profitability of their business more accurately and understand credit affordability metrics. It is also recommended that financial institutions make better use of the credit guarantee schemes and improve take- up on the funds available from these schemes.

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## **Abbreviations**

CIPC	Companies and Intellectual Property Commission
COVID- 19	Coronavirus disease 2019
GDP	Gross Domestic Product
GEM	Global Entrepreneurship Monitor
GEP	Gauteng Enterprise Propeller
DFI	Development finance Institute
ICT	Information and Communication Technologies
IFC	International Finance Corporation
IT	Information Technology
MSME	Mico, Small and Medium Enterprises
OECD	Organisation for Economic Co-operation and Development
SDG	Sustainable Development Goals
SEDA	Small Enterprise Development Agency
SEFA	Small Enterprise Finance Agency
PPP	Paycheck Protection Program
SARS	South African Revenue Service
TEA	Total Early-stage Entrepreneurial Activity
TERS	Temporary Employee/Employer Relief Scheme
VC	Venture Capitalist

# Chapter 1

## Introduction

### 1. Background

COVID-19 has and continues to grossly affect the world in ways we never anticipated. This devastating global and public health issue has resulted in a dire humanitarian and economic crisis which requires the global community to stand together and offer each other support to overcome this invisible enemy. Across the African continent there are reports of a resurgence in infections, characterised by new variants and non-adherence to the COVID-19 health and safety guidelines and protocols provided by the World Health Organization (WHO), which include social distancing, hand washing and wearing of masks. In the South African context, the department of health website ([2001, para 1](#)) reports that “COVID-19 has become a global pandemic, and it is continuing to spread across the globe.” The South African healthcare system also took strain as hospitalisations were on the increase, resulting in the introduction of regulations, by governments across the globe, to address, prevent and combat the spread of the virus. The introduction of these regulations has had a great economic impact on countries due to restrictions of trade, travel, alcohol ban and the curfew. This obviously has a significant impact on certain industries and sectors, like travel and tourism, entertainment, food and beverage, import and export of certain products. This study will help us understand which sectors, and to what extent, have been impacted by the pandemic.

According to the World Bank, formal micro, small and medium enterprises (MSME) make up about 40% of GDP in emerging economies (Beck et al., 2008). MSMEs are widely accepted as the backbone of economic growth and contribute towards the income and job creation (Abor, 2017). These MSMEs are in turbulent times because of the pandemic, justifying the importance of having a better understanding of the impact of COVID-19 on MSMEs, so we can identify opportunities for growth in the form of easier entry to funding and ensure that most existing businesses survive similar challenges in the future. The need to examine this impact is further supported by the OECD (2020) that African countries and South Africa, in particular, would be hit hard by the outbreak of COVID-19 and the ensuing national lockdowns in the short, medium, and long term. Furthermore, the South African economy had already gone into a recession prior to the pandemic and declared a national state of disaster (OECD, 2020). With

MSMEs generally accepted as engines of economic growth and the restructuring of society, they justify their focus in this study.

It has been widely accepted that to mitigate the impact of the COVID crisis, quick policy responses are required (OECD, 2020). Poor design and implementation of such policies and their related instruments could result in the worsening of the already adverse long-term effects of COVID (Brown et al., 2020). Globally, governments responded to address issues of job losses and business closures because of the pandemic (Bartik et al., 2020). To provide relief to MSMEs in the USA, the Coronavirus Aid, Relief, and Economic Security Act, also known as the CARES Act, was passed, and signed into law in March 2020, in response to the economic disruption caused by the pandemic. As part of the Act, the Paycheck Protection Program (PPP) was put in place to provide relief to MSMEs. Similar relief programmes were introduced in countries all over the world, characterized by issues relating to accessing the financial aid, red tape within governments and difficulties of determining eligibility (Bartik et al., 2020). A positive is that such programmes have seemingly reduced the financial pressures experienced by MSMEs through increased lending activities to these businesses (Beauregard et al., 2020).

## **1.2. Research Problem**

This study aims to address the following problem areas:

- The pandemic has brought much disruption to development progress in developing countries, African countries in particular, with MSMEs being more vulnerable to the crisis.
- Access to finance for MSMEs remains an issue in South Africa, stifling growth and job creation.
- There are limitations on previous studies in this area.

### **A. Case for Developing Countries**

Various studies have established that crises, like natural disasters, economic recessions and other catastrophes have a negative effect on small businesses, threatening their survival (Williams & Vorley, 2015; Archibugi et al., 2013; Herbane, 2010; Irvine & Anderson, 2004). The pandemic was predicted to sink close to 60 % of MSMEs if restrictions were to continue, given that only 32 % of MSMEs are classified as essential service providers (FinScope, 2021).

From a global perspective, there has been several studies conducted to assess the economic impact of COVID-19 on MSMEs, with many of them covering the short-term effects of the pandemic instead of the long-term effects or sustainability of MSMEs. MSMEs are key to providing employment and thus contribute towards poverty alleviation in developing countries where there's high unemployment rates and poverty levels. The sustainability of MSMEs in developing countries are therefore crucial to ensure that the poor don't lose their jobs and their livelihood. Production has been identified as one of the critical areas that have been impacted in the short- term, because of unexpected lockdowns and disruptions in supply chain, with liquidity preservation being another significant challenge faced by business in the short- term, because of lost sales and an inability to make timeous collections from debtors (Nair, 2022).

## **B. Case for South Africa**

In the case of South Africa, the role of MSMEs is just as important for the economy as they employ 61% of the country's workforce and contribute 40% to GDP (Bvuma & Marnewick, 2020). Businesses are located across urban and rural areas in the 9 provinces of South Africa, represented across different sectors. The South African government also established a relief program through the Department of Small Business Development to assist MSMEs during the crisis. Relief funds and aid were made available to MSMEs to assist with acquisition of input, labour and operational costs, and to provide much needed relief on existing debt obligations. These funds and facilities would be limited to the impact resulting from COVID- 19 and match the patterns of the MSME's cash flows. The relief was also structured to cover all sectors and geographies in the country, however a 2020 McKinsey report highlighted that very few MSMEs had access to low to medium cost funding, with 6% and 9% of MSMEs receiving government funding and private funding, respectively. According to the Finfind report of 2020a, 42.7 % of businesses closed due to the pandemic and the lockdown. Only 32 % of businesses in South Africa were classified as essential services providers during the lockdowns, further leading to the cashflow and liquidity issues experienced by many MSMEs (OECD, 2022).

Over 85 % of firms in South Africa are composed of MSMEs, and contribute towards employment, increased competition and stimulate innovation and digitisation. Therefore, the government must implement appropriate strategies to drive the National Development Plan, which aims to eliminate poverty and reduce inequality by 2030. This paper aims to understand

the impact of the COVID-19 outbreak on small businesses. The discussion particularly focuses on the impact of COVID-19 in the context of financing of MSMEs.

### **C. Limitations**

In South Africa, there is no study conducted to understand the agency problem of access to finance for MSMEs during and post COVID- 19, and while there have been several studies relating to access to finance for MSMEs, there's also no specific studies on financing of MSMEs during and post COVID – 19. Apedo-Amah et al. (2020) conclude that continued and high frequency data collection efforts are required to help us understand the long- term effects of the pandemic.

#### **1.3. Research questions and scope**

The overarching research question for this study is MSME finance under COVID- 19 in resource-constrained environments.

This study seeks to provide clarity and understanding on the following research questions:

- a) How have MSMEs been impacted by COVID-19 policy responses?
- b) What are benefits and challenges MSMEs experienced in their attempt to obtain debt relief or access to finance during the COVID-19 pandemic?

#### **1.4 Research objectives**

The objective of the study is to understand the impact of COVID- 19 on the financing of MSMEs in developing countries with evidence from South Africa. Therefore, the study aims to achieve the following:

- a) To understand the effect of the implementation of COVID -19 policy response on the demand side of MSME financing.
- b) To explore the benefits and challenges that MSMEs experienced in their attempt to obtain debt relief or access to finance.

#### **1.5. Justification of the Study**

According to the OECD (2020), African countries, including South Africa would be hard- hit by the outbreak and the lockdowns in the short, medium, and long term. The South African government has long identified the important role that MSMEs play in addressing unemployment, poverty, and inequality of the South African economy. In South Africa,

MSMEs employ 61% of the country's workforce and contribute 40% to GDP (Bvuma & Marnewick, 2020). Given the high usage and dependence of physical cash by MSMEs (Williams & Schaefer, 2013; Shafi et al., 2020), their business operations were heavily impacted by the pandemic. The result of the reduced productivity, demand of goods and services, shortage of raw materials and limited movement all had a negative effect on these businesses, thus having a major impact on the South African economy. Access to finance has been found to be a factor which hinders the performance and sustainability of MSMEs in South Africa (Fatoki, 2021), while better access to finance in developed countries is found to have contributed towards improved performance and sustainability in developed countries (Brown et al., 2020). Therefore, a need to examine the impact of COVID – 19 on the financing of MSMEs operating in South Africa is justified. Gauteng province is selected as a case study. There is currently no study conducted to examine this subject within the South African context, and this study also aims to assist policymakers and practitioners in identifying strategies required to assist MSMEs in the face of challenges arising from times of crises.

## **1.6 Organization of the dissertation**

Chapter 1 is an introduction to the study, inclusive of six sections. The chapter starts by providing a background on the research area of COVID- 19 and MSMEs, followed by a definition of the research problem and the limitations, the research objectives, scope, and questions, and ends with a justification and organisation of the study.

Chapter 2 is a full literature review. This chapter is made up of the definition of terms and concepts, overview, context, theoretical and empirical evidence of the financing of MSMEs. Chapter 3 discusses the research methodology, inclusive of the tools used to investigate the research problem. This chapter includes a description of the research approach and design applied in this study. The research is qualitative, inductive, and exploratory in nature. The target population and sampling techniques are defined and justified, along with the data collection and data analysis processes. Chapter 4 includes a description of the respondents and a discussion of the data results to make sense of the evidence from the investigation. Chapter 5 provides a summary of the study, including major findings and implications of the findings. This chapter also provides policy recommendations and recommendations for future research.

## Chapter 2

### Literature Review

#### 2.1. Introduction

This chapter starts by defining the terms and concepts that this study is based on. It starts with a comprehensive definition of MSMEs and related aspects, with a specific focus on South Africa, followed by an overview of MSME financing in South Africa. The chapter then proceeds to discuss the theoretical frameworks and theories related to financing of MSMEs from both a demand and supply perspective. The chapter concludes by reviewing existing empirical evidence and various studies on the impact of COVID-19 on the financing of MSMEs.

#### 2.2. Definition of terms: MSMEs

There is no universal definition of MSMEs, which can be applied world- wide. The Bolton Report (1971) is often referred to as one of the earliest attempts to come up with a definition for MSMEs (Berisha & Pula, 2015). The report firstly suggests an economic definition and then a statistical one for MSMEs (Abor, 2017). The report suggested that an entity is considered small when it meets the following criteria from an economic perspective:

- Entity has a relatively small market.
- Entity is managed by owners or part owners in a personalised way and not in a formalised management structure.
- Entity is independent and did not form part of a larger enterprise.

The following criteria applied from a statistical perspective:

- Size of the small firm sector and its contribution to gross domestic product (GDP), employment and exports.
- The extend to which the small firm sector's economic contribution has changed over time.
- Entity can apply the statistical definition in a cross- country comparison of the small firm's economic contribution.

Despite the Bolton Committee's acknowledgement that it is not easy to operationalize the qualitative definition, the report is still the main reference for the qualitative definition of

MSMEs in literature (Berisha &Pula, 2015). However, academics, policymakers and other institutions make use of the quantitative definition to define MSMEs.

The definition of MSMEs in Europe is found in the commission recommendation of 6 May 2003 made by the European Commission and took effect on 1 January 2005. The European Commission uses the number of employees as the main criteria for defining MSMEs but have added the financial criterion to better understand the performance and competitiveness of a firm. The specific criteria used by the European Commission to determine enterprise categories are as follows:

- A microenterprise employs fewer than 10 persons and has an annual turnover and/or balance sheet total not exceeding 2 million Euros;
- A small enterprise employs fewer than 50 persons, and has an annual turnover and/or balance sheet total not exceeding 10 million Euros;
- A medium enterprise employs fewer than 250 persons and has an annual turnover not exceeding 50 million Euros, and balance sheet total not exceeding 43 million Euros.

United Nations Industrial Development Organization (UNIDO) also defines MSMEs by the number of employees, but also provide different classifications for industrialized and developing countries (Abor, 2017). For developing countries, micro enterprises are those with less than 5 employees, small enterprises employing between 5 and 19, while medium enterprises employ between 20 and 99 employees.

In the South African context, Act No. 102 of 1996 of the National Small Enterprise Act defines MSMEs in South Africa as a separate and distinct business entity, together with its branches or subsidiaries, if any, including cooperative enterprises, managed by one owner or more predominantly carried on in any sector or subsector of the economy mentioned in column 1 of the Schedule and classified as a micro, a small or a medium enterprise by satisfying the criteria mentioned in columns 3 and 4 of the Schedule (Department of Small Business Development, 2019). The definition was updated in March 2019, with the new schedules defining MSMEs using two proxies as shown on figure 1 below; total full- time equivalent of paid employees and total annual turnover. Gross asset value has been removed as the third proxy.

Figure 1: Classification of MSMEs in South Africa

**SCHEDULE 1**  
The new National Small Enterprise Act thresholds for defining enterprise size classes by sector, using two proxies

Column 1	Column 2	Column 3	Column 4
Sectors or sub-sectors in accordance with the Standard Industrial Classification	Size or class of enterprise	Total full-time equivalent of paid employees	Total annual turnover
Agriculture	Medium	51 - 250	≤ 35,0 million
	Small	11- 50	≤ 17,0 million
	Micro	0 - 10	≤ 7,0 million
Mining and Quarrying	Medium	51 - 250	≤ 210,0 million
	Small	11- 50	≤ 50,0 million
	Micro	0 - 10	≤ 15,0 million
Manufacturing	Medium	51 - 250	≤ 170,0 million
	Small	11- 50	≤ 50,0 million
	Micro	0 - 10	≤ 10,0 million
Electricity, Gas and Water	Medium	51 - 250	≤ 180,0 million
	Small	11- 50	≤ 60,0 million
	Micro	0- 10	≤ 10,0 million
Construction	Medium	51 - 250	≤ 170,0 million
	Small	11- 50	≤ 75,0 million
	Micro	0- 10	≤ 10,0 million
Retail, motor trade and repair services.	Medium	51 - 250	≤ 80,0 million
	Small	11- 50	≤ 25,0 million
	Micro	0 - 10	≤ 7,5 million
Wholesale	Medium	51 - 250	≤ 220,0 million
	Small	11- 50	≤ 80,0 million
	Micro	0 - 10	≤ 20,0 million
Catering, Accommodation and other Trade	Medium	51 - 250	≤ 40,0 million
	Small	11- 50	≤ 15,0 million
	Micro	0 - 10	≤ 5,0 million
Transport, Storage and Communications	Medium	51 - 250	≤ 140,0 million
	Small	11- 50	≤ 45,0 million
	Micro	0 - 10	≤ 7,5 million
Finance and Business Services	Medium	51 - 250	≤ 85,0 million
	Small	11- 50	≤ 35,0 million
	Micro	0- 10	≤ 7,5 million
Community, Social and Personal Services	Medium	51 - 250	≤ 70,0 million
	Small	11- 50	≤ 22,0 million
	Micro	0 - 10	≤ 5,0 million

Source: FinScope (2020)

The characteristics of MSMEs differ from country to country, with different criteria being applied based on their location and other economic conditions (Abor, 2017). The South African definition as per the National Small Enterprise Act will be applied for this study.

### 2.3. Overview of MSMEs in South Africa

According to the 2010 FinScope survey, South Africa has a total of 5,979,510 MSMEs, with 17 % of them registered with the Companies and Intellectual Property Commission (CIPC). The 2020 FinScope survey found that 85 % of businesses are classified as micro- enterprises, 14 % as small enterprises and just 1 % classified as medium businesses (FinScope, 2020) as shown in figure 2 below.

*Table 1: MSMEs size by number of employees*

**MSMEs size by number of employees**

Category	Employees	Size	No of businesses
Micro- enterprise	0 to 10	84.8%	2 219 026
Small enterprise	11 to 50	14.4%	375 809
Medium enterprise	51 to 250	0.8%	20 916

*Source: FinScope (2020)*

Another feature of the MSME landscape in South Africa is the disparity between formal and informal MSMEs, with over 66 % of MSMEs being informal (SEDA, 2021). The 2020 FinScope Survey also found that formal MSMEs contribute R2.9 trillion to the economy, while informal MSMEs contribute R147 billion. Furthermore, the survey found that the township is a substantial contributor to the economy at R1.5 trillion compared to rural economy at R139 billion (FinScope, 2020). To transform these informal businesses into formal businesses, it is necessary to expand access to finance to these MSMEs (Noumba& Karimjee, 2019). A study commissioned by the Small Enterprise Development Agency (SEDA) in 2021 also concluded on key indicators, as per table 1 below, of the MSME landscape in South Africa. The table shows a 11.1 % year on year decline in the total number of MSMEs and a worrying 6.2 % decline in MSME employment, further highlighting the high failure rate of MSMEs in South Africa (Fatoki, 2021).

*Table 2: Key indicators of MSMEs*

**Key indicators of MSMEs**

KEY INDICATORS	2020Q1	2020Q4	2021Q1	q-o-q change	y-o-y change
Number of MSMEs	2 614 063	2 382 030	2 325 203	-2.4%	-11.1%
Number of formal MSMEs	755 265	656 423	667 111	1.6%	-11.7%
Number of informal MSMEs	1 748 031	1 617 533	1 552 814	-4.0%	-11.2%
Number jobs provided	10 406 070	9 124 485	9 757 287	6.9%	-6.2%
% operating in trade & accommodation	38.0%	38.1%	37.6%	-0.5% pts	-0.4% pts
% operating in community services	14.0%	13.1%	14.8%	1.7% pts	0.8% pts
% operating in construction	14.4%	15.7%	14.7%	-0.9% pts	0.3% pts
% operating in fin. & business services	13.4%	13.5%	13.7%	0.2% pts	0.4% pts
% black owned formal MSMEs	74.8%	74.8%	72.6%	-2.2% pts -	-2.2% pts
% contribution of MSMEs* to turnover of all enterprises#	37.5%	37.5%	37.4%	0.1% pts	-0.2% pts

*Source: SEDA (2021)*

An assessment conducted by MSME South Africa in 2018 found that the majority of MSMEs are based in the Gauteng province at 56 %, followed by Western Province at 11 % and KwaZulu Natal at 9 %. The same report also suggests that majority of MSMEs are black owned (72%) and that males (52%) are the majority from a gender perspective. A prior study conducted by Seda in 2016 (Table 2) supports that most MSMEs are based in Gauteng, KwaZulu- Natal and Western Cape who boast 61.7 % of the total national number. Table 3 tells us that the total number as a %age to the total for the three provinces has increased slightly to 62.2 % in 2021. The table also clearly shows the impact of the pandemic on the number of MSMEs dropping by 11 % year on year, with the highest impact being Limpopo and Northern Cape. The Eastern Cape was the only province that had an increase of total MSMEs.

*Table 3: MSMEs by province*

MSMEs by province

MSMEs	Number (2008Q1)				Number (2015Q2)			
	Total	Formal	Informal	Other	Total	Formal	Informal	Other
	2 182 823	666 501	1 420 933	95 389	2 251 821	667 433	1 497 860	86 528
Western Cape	223 933	114 976	95 212	13 745	230 324	110 107	110 188	10 030
Eastern Cape	218 865	56 579	154 631	7 655	197 366	50 670	141 739	4 957
Northern Cape	29 894	11 450	11 768	6 676	20 611	8 534	9 058	3 019
Free State	114 949	31 040	76 127	7 783	96 846	26 224	60 816	9 806
KwaZulu-Natal	418 406	102 591	289 347	26 468	373 434	74 976	283 165	15 293
North West	109 860	25 817	76 855	7 188	112 856	27 430	79 153	6 273
Gauteng	687 556	270 093	405 180	12 283	785 321	306 231	465 100	13 989
Mpumalanga	193 259	29 760	156 814	6 685	185 399	35 208	141 129	9 063
Limpopo	186 101	24 193	155 001	6 907	249 663	28 054	207 512	14 098

*Source: Seda (2016)*

*Table 4: MSMEs by province*

MSMEs	2020Q1		2020Q4		2021Q1		Quarterly change		Yearly change	
	Number	Distrib.	Number	Distrib.	Number	Distrib	Number	Distri b.	Number	Distrib
						.				.

Western Cape	298 819	11.4%	282 080	11.8%	278 721	12.0%	-3 359	-1.2%	-20 097	-6.7%
Eastern Cape	225 298	8.6%	222 698	9.3%	232 367	10.0%	9 668	4.3%	7 068	3.1%
Northern Cape	24 275	0.9%	16 346	0.7%	20 306	0.9%	3 960	24.2%	-3 969	-16.3%
Free State	114 979	4.4%	93 148	3.9%	97 905	4.2%	4 758	5.1%	-17 074	-14.8%
KwaZulu-Natal	419 467	16.0%	394 767	16.6%	381 742	16.4%	-13 026	-3.3%	-37 725	-9.0%
North West	129 168	4.9%	93 067	3.9%	111 976	4.8%	18 909	20.3%	-17 192	-13.3%
Gauteng	885 839	33.9%	807 751	33.9%	786 027	33.8%	-21 724	-2.7%	-99 812	-11.3%
Mpumalanga	229 060	8.8%	212 301	8.9%	197 809	8.5%	-14 492	-6.8%	-31 251	-13.6%
Limpopo	287 158	11.0%	259 873	10.9%	218 351	9.4%	-41 522	16.0%	-68 808	-24.0%
<b>Total</b>	<b>2 614 063</b>	<b>100%</b>	<b>2 382 030</b>	<b>100%</b>	<b>2 325 203</b>	<b>100%</b>	<b>-56 827</b>	<b>-2.4%</b>	<b>-288 860</b>	<b>-11.1%</b>

Source: Seda (2021)

The 2020 FinScope survey finds that MSMEs in South Africa mainly operate in the service (58%) and trade (26%) sectors, followed by industrial (12%) and agriculture (4%). MSMEs in South Africa are operating in highly competitive environments, with a high number of them having challenges with accessing markets (SME South Africa, 2018).

Table 5: MSMEs by economic sector

MSMEs	Number (2008Q1)	Number (2015Q2)			Turnover (2015Q1)	GDP (2015Q2)	Turnover /MSME	
	Total	Total	Formal	Informal	Other	R million	R million	
<b>Total</b>	<b>2182823</b>	<b>2 251 821</b>	<b>667 433</b>	<b>1 497 860</b>	<b>86528</b>	<b>2 908 020</b>	<b>815 636</b>	<b>1.29</b>
Agriculture	87 820	56 774	0	0	56 774	n/a	35 213	n/a
Mining	2 696	2 199	0	2 199	0	35 256	69 421	16.03
Manufacturing	267 817	201 459	62 657	138 801	0	658 740	111 672	3.27
Electricity, gas & water	4 252	7 456	6 656	801	0	7 488	38 647	1
Construction	252 233	299 242	77 098	222 143	0	229 016	38 804	0.77
Trade & Accommodation	974 083	944 467	186 798	757 669	0	1 160 560	129 144	1.23
Transport & Communication	122 370	133 134	56 620	76 514	0	134 152	87 612	1.01
Finance & Bus. Services	236 740	271 712	172 423	99 289	0	571 384	183 430	2.1
Community	227 243	305 624	105 181	200 444	0	111 424	50 982	0.36
Other	7 569	29 754	0	0	29 754	0	70 711	0

Source: Seda (2016)

According to the IFC (2019), South Africa has a slow growth rate in MSME numbers, characterized by limited early-stage businesses with low survival rates, which ultimately results in the number of established and formal businesses being low. The Global Entrepreneurship Monitor (GEM) uses the Total Early-stage Entrepreneurial Activity (TEA) index as a key measure of entrepreneurial activity, which allows for cross-sectional and

longitudinal comparisons for countries (Harrisons et. al., 2017). According the 2016 Global Entrepreneurship Monitor (GEM) report, South Africa’s TEA ranking is considerably low at 46 out of 65 countries for the year 2016. Table 5 shows South Africa’s relative TEA rankings over a 15-year period. The data shows a worsening trend of TEA activity in South Africa. The IFC report (2019) conclude that the TEA rate should at least be three times greater, given the size of the GDP. Furthermore, low levels of youth participation in early- stage entrepreneurial activity were reported in the 2016 GEM report, with 13% of 18- to 34-year-olds in South Africa compared to an average of 37.1 % in Africa. This is really concerning for the prospects of increased entrepreneurial activity in the country.

*Table 6: South Africa’s relative TEA rankings*

<b>Year</b>	<b>SA’s TEA ranking</b>	<b>SA’s TEA rate</b>	<b>Median</b>	<b>Number of positions above/below median</b>
2002	20 <sup>th</sup> out of 37 countries	6.3	19	1 below
2003	22 <sup>nd</sup> out of 31 countries	4.3	16	6 below
2004	20 <sup>th</sup> out of 34 countries	5.4	17	3 below
2005	25 <sup>th</sup> out of 34 countries	5.2	17	8 below
2006	30 <sup>th</sup> out of 42 countries	5.3	21	9 below
2008	23 <sup>rd</sup> out of 43 countries	7.8	22	1 below
2009	35 <sup>th</sup> out of 54 countries	5.9	27	8 below
2010	27 <sup>th</sup> out of 59 countries	8.9	30	3 above
2011	29 <sup>th</sup> out of 54 countries	9.1	27	2 below
2012	22 <sup>nd</sup> out of 69 countries	7.3	35	13 above
2013	35 <sup>th</sup> out 67 countries	10.6	34	1 below
2014	53 <sup>rd</sup> out of 70 countries	7.0	35	18 below
2015	38 <sup>th</sup> out of 60 countries	9.2	30	8 below
2016	46 <sup>th</sup> out of 65 countries	6.9	33	13 below

*Source: Global Entrepreneurship Monitor South Africa (2017)*

### **2.3.1. Overview of MSME Financing in South Africa**

MSMEs in South Africa largely depend on the owner’s own capital, which is often insufficient to support the operations of a small businesses, especially ones at the start- up stage (Makina, 2015). South African MSMEs have the option of debt or equity finance, made up of various sources of finance, provided by both the private and public sector. South Africa has a developed Private Equity and Venture Capitalist market, however most of these funds go towards late-stage investments (Noumba & Karimjee, 2019; Fatoki, 2021). These funds should ideally be channelled to early- stage investments for MSMEs who cannot access bank funding and often rely on personal savings, family, and friends to borrow, save, or insure their assets (Abor, 2017).







This suggests that South Africa’s Early-stage Entrepreneurial Activity will remain low until we close the financing gap for start-ups. Bank financing favours more long-term funding and working capital requirements (Noumba & Karimjee, 2019), however access to debt financing is limited for MSMEs in South Africa (Fatoki, 2021). Access to bank financing is mostly accessible to an enterprise with an acceptable credit record and sufficient collateral to offer the bank (John & Mbohwa, 2015). Despite a well-developed, strong, and stable banking industry (PWC, 2022), the low levels of MSME access to credit and low credit penetration suggests that there is a financing gap in South Africa. The IFC report in 2017 estimates a credit gap of \$6 billion and \$24 billion for formal and informal MSMEs, respectively, while the Finfind (2020a) report estimates a credit gap of between R86bn and R346bn for MSMEs in South Africa. Makina et. al (2015) also find that a financing gap also exists from a geographic perspective, with high GDP provinces (Gauteng, Western Cape and KZN) having a larger portion of MSMEs having access to formal credit. 68.9 % of credit extended to formal MSMEs in South Africa come from commercial banks, with the following product types being utilised from a value perspective; short-term loans (overdrafts and credit cards) (26%), term loans (10%), commercial property finance (15%) and vehicle and asset finance (49%) (Noumba & Karimjee, 2019). Table 6 below gives a view of the of the financial services providers in South Africa, while Figure 3 provides an estimate of the quantum of debt and equity financing, including alternative financing options for MSMEs in South Africa.

*Table 7: Number of financial services providers Financial*

Financial service providers	2012	2013	2014	2015	2016	2017	2018
Banks	16	17	17	17	17	19	19
Mutual banks	3	3	3	3	3	3	4
Co-operative banks	2	2	2	2	2	3	4
Registered co-operative financial institutions	106	24	24	28	28	28	22
Non-life insurers	106	99	97	92	89	88	86
Life insurers	87	77	74	75	74	72	73
Credit providers	5450	5,450	5,724	4,577	4,569	5,591	6,191

*Source: National Treasury (2020)*

Figure 2: MSME financing providers

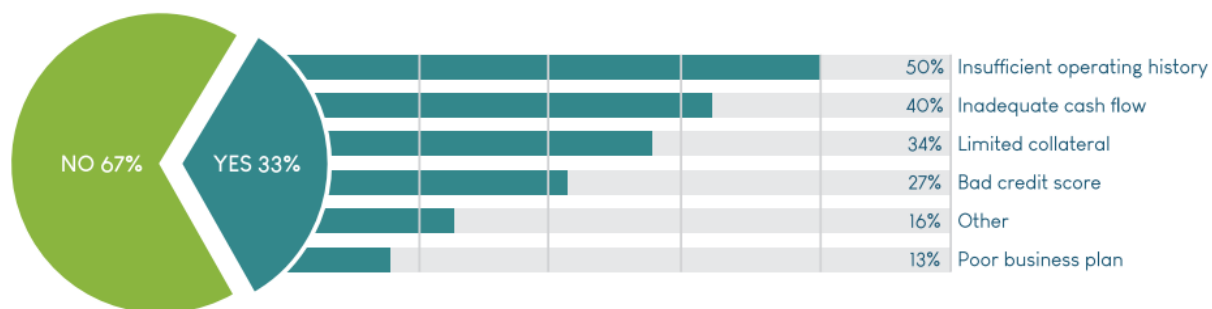
	Banks	MFI	PE/VC	AltX	Fintechs	Government
Typical segmentation						
Estimate of financing quantum	Aggregate loan portfolio of R160 billion <sup>171</sup>	Total unknown – business loan portfolio upward of R1.5 billion <sup>172</sup>	Allocation to MSMEs unknown – estimate of R36 billion for PE and R3.5 billion for VC <sup>173</sup>	Market capitalization of R12.95 billion <sup>174</sup>	Total unknown – lending upward of R500 million <sup>175</sup>	Upward of R17 billion <sup>176</sup>

Source: International Finance Corporation (2018)

Several funding programmes are available to assist MSMEs with bridging the firm- financing gap in South Africa, and they are available in both the public and private sector. The governments provide grants (including cost- sharing grants), tax incentives, equity funding and loans (SME South Africa, 2018), usually through development finance institutions. The MSME South Africa Landscape Report (2018) found that the main sources of government funding were government grants (21%), Department of Trade and Industry (DTI) (17%), National Youth Development Agency (NYDA) (16%), Small Enterprise Development Agency (SEDA) (15%), Gauteng Enterprise Propeller (GEP) (15%), Small Enterprise Finance Agency (SEFA) (2%) and the National Empowerment Fund (NEF) (1%). The same report finds that only 6 % of MSMEs managed to receive government funding, while 9 % received funding from non-government funding sourced from personal savings and/or family (50%), businesses incubators (24%) and commercial banks (20%). It was found that the main reasons for funding declines were insufficient operating history, inadequate cash flow, limited collateral, bad credit score and a poor business plan (SME South Africa, 2018). The Industrial Development Corporation (IDC) and the Development Bank of South Africa (DBSA) have also played a role to support MSMEs through their lending activities, guarantee fund and joint venture support (Noumba & Karimjee, 2019).

According to SME South Africa (2018) 88 % of MSMEs in South Africa indicate that they need support from a funding perspective, with 33 % being refused funding. The SME South Africa (2018) also found that most MSME owners are not aware of the funding requirements. The factors that contribute to the declined funding requests are illustrated on figure 4 below.

Figure 3: MSME owners who have been refused funding



Source: SME South Africa (2018)

The decline reasons include bad business plans, excessive outstanding debt and insufficient collateral or a limited track record.

## 2.4. Theoretical Framework

This sub-section discusses fundamental concepts and theories related to financing of MSMEs from both a demand and supply side. Supply and demand side issues can be the reason for the financing gap that exists for MSMEs. The demand side is believed to be a major hindrance to MSMEs' access to finance (National Treasury, undated), as most studies are found to focus more on the supply side of financing (Fatoki, 2021). A United States Agency for International Development (USAID) study conducted in 2019 identifies five theories of change for areas of intervention for MSMEs; business management, access to finance, business registration and taxation, market access and innovation. This study focuses on the theories that relate to access to finance. There is no specific theory that relates to the relationship between COVID- 19 and access to finance. The theoretical frameworks applied to this study are the institutional theory, the financial theories of static trade- off theory and the pecking order theory.

### 2.4.1. The Institutional theory

John Meyer and Brian Rowan developed the institutional theory in 1977 to explore how organisations relate to their societal, political, and global environments. They also observed that when these organisations try to act consistently against the expectations of the institutional environment, they work towards "institutional isomorphism", which can be achieved using one of three mechanisms or processes; coercive, mimetic, and normative (Di Maggio & Powell, 1983). Coercive pressures come from pressures that an organisation is dependent on, such as

customers, regulators, and suppliers. They require an organisation to comply with certain policies, rules, and regulations. Mimetic pressures arise from an organization adopting or copying other organization's practices and behaviours to compete or survive. Normative pressures arise from an organization adopting professional standards and norms from larger organisations and professional bodies to gain more legitimacy.

The theory has evolved over time, and the institutional theory has been applied in studies of MSMEs, with most of the studies focused on developed countries. Institutions foster and restrict the activities of MSMEs (Bruton et al., 2008), meaning they determine the rules of game within the environments which MSMEs will operate. It can thus be assumed that an institution which is operationally efficient fosters a thriving environment for MSMEs to prosper and even make access to finance easier, while institutional constraints lead to an increase of informal relationships and MSMEs that are not legally recognized (Klapper et al., 2006). This will make it difficult for MSMEs to access finance and therefore make it even more difficult for the same MSMEs to survive in the event of a crisis. Various studies have found that limited access to information, bureaucracy, legacy systems and infrastructure, state control of the private sector and land ownership as the some of the constraints faced in developing countries (Kuipers & Eijdenberg, 2021).

The rapid spread of COVID- 19 led to governments and public institutions introducing policies to control the impact of the pandemic. These policies can support MSMEs and ensure survival of the business and even foster performance, but they can also constrain MSMEs and result in poor performance or even closure (Slesman et al., 2021; Kabir & Abubakar, 2022). Kabir and Abubakar (2022) distinguishes between aggressive policy responses to COVID- 19, which are policies restricting local community movement, such as the national lockdown and the closure of non-essential businesses, schools and business centres, and less aggressive policy responses to COVID- 19, which relates to policies with fewer restrictions, like public awareness, social distancing, limited use of public spaces and the suspension of limited travel. It is therefore expected that the less aggressive policy responses are likely to allow MSMEs, non- essential MSMEs to continue operating and potentially foster improved performance. The aggressive policy responses are then expected to have a long– term effect on the operations of the MSMEs and even lead to business closure, loss of jobs, reduced productivity and revenues, and supply chain interruptions. The Government and related institutions have a responsibility to create an environment that protects MSMEs form the economic shocks brought by the COVID- 19. The

applicable policies include tax credits and tax cuts, subsidies, low interest rates and loans and grants to help MSMEs survive and grow (Alharbi, 2022).

#### **2.4.2. The Pecking Order Theory**

The Pecking Order Theory (POT), made popular by Myers and Majluf (1984), refers to the capital structure of a company, suggesting that managers follow a hierarchy when they consider sources of finance. The pecking order theory suggests that MSMEs prefer utilizing profits and retained earnings to finance their businesses, followed by debt, then hybrid forms of finance, with the last option being equity finance (Mole & Namusonge, 2016). The theory suggests that the cost of financing increases because of problems of asymmetric information, like adverse selection and moral risk, which can affect access to external finance (Martinez et al., 2019; Frank et al., 2020). The asymmetric information comes from the understanding that managers of MSMEs generally possess more information about the business than providers of finance. External sources of finance therefore require a higher return to mitigate the risk resulting from the asymmetric information. Therefore, using retained earnings as a source of finance is favoured because MSMEs typically want to maintain control of the business assets and operations (Mole & Namusonge, 2016). This is supported by empirical evidence in Ghana, which observed that MSMEs funding is made up of about 86% of own equity as well as loans from family and friends (Mole & Namusonge, 2016). Debt finance is the next best option should a MSME not be able to utilize their retained earnings as a source of finance. MSMEs prefer shorter- term debt before longer term debt (Yazdanfar & Öhman, 1991), which can have a negative impact on cash flows and profits of the business. External debt providers would require a lower rate of return than equity holders because of the inherent risk that comes with being an equity or shareholder of a business. As a result of COVID-19, MSMEs experienced liquidity issues and would therefore opt to utilize their own retained earnings to support the survival of the business as the first option, and then opt for cheaper debt as second option. However, the adverse selection problem leads to credit rationing due to some MSMEs being able to access finance from external debt providers while some other similar MSMEs wouldn't have the same opportunity and thereby be declined when applying for financing. The establishment of credit guarantee schemes reduce this adverse selection problem by making funds available for MSMEs at a lower cost and longer term (Corredera et al., 2021). Access to finance through the credit guarantee scheme is also expected to improve performance.

### **2.4.3. The Trade- off theory**

The trade- off theory suggests that MSMEs tend to reduce their level of debt because of the higher business risk and higher probability of bankruptcy (Swinnen et al., 2005). It assumes that the optimal capital structure is the result of balancing the benefits of leverage, mainly through tax savings, and the costs of financial difficulties (Martinez et al., 2019). This trade-off theory is seen as a competing theory to the Pecking Order theory to explain a firm's financing decision. However, Banga and Gupta (2017) observed that the theories are complementary, suggesting that the predictions of the Pecking Order theory are useful in explaining the capital structure decisions of MSMEs for short- term debt, while using the Trade-Off theory, MSMEs within greater operating risk were more inclined to reducing their leverage. MSMEs are therefore expected to use debt even if there is retained earnings available. It is also expected that the uncertainty that COVID -19 brought resulted in the reduction of existing debt and the decrease in demand for new debt from MSMEs who had a higher business risk and probability of bankruptcy.

### **2.5. Review of Empirical Literature**

This sub-section provides a review of various studies that investigated the impact of COVID-19 on the financing of MSMEs. Employment is important for the economic development of the economy, and thus outlined in the Sustainable Development Goals, as SDG 8, which aims to promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all. The unemployment rate is used to measure the utilization of the labour supply. MSMEs are widely accepted as the backbone of economic growth and contribute towards the income and job creation (Abor, 2017). Various reports, studies and surveys have widely accepted that COVID- 19 has resulted in the increase of the unemployment rate and has affected employment in ways that may have resulted in permanent changes to work patterns (Baldwin & Mauro, 2020; Reeves et al., 2020; Nair, 2022). Bartik et al. (2020) who conducted a study to assess the impact of COVID-19 on small businesses in the US over a 3-month period support this stance, as they found that the pandemic brought along large- scale retrenchments or lay- offs and business closures. The study also found that COVID- 19 resulted in 41.4 % of MSMEs being temporarily closed, while only 1.8% were permanently closed because of the pandemic. A study in Australia, supports further after it was found that 600 000 workers employed by MSMEs were retrenched (Cassells& Duncan, 2020). Changes in work patterns can certainly be observed in various industries where hybrid and remote working models have been implemented by many businesses, which one might argue could've saved many jobs from

being lost. A recent study by Blanas and Oikonomou (2022) somehow supports this notion as it found that there was a decrease in the relative demand for jobs in the food, personal care, and service industries, which are customer orientated, but found that there was an increase in the relative demand for jobs in essential service providers like healthcare and social services. Beebeejaun, (2022) also supports the narrative that not as many jobs were lost as anticipated, having found that 79% of all companies in Mauritius were able to maintain full employment because of remote working policies. However, no findings refer specifically to MSMEs in this instance, but given the high number of MSMEs in relation to the total number of companies in Mauritius, we can assume that remote- working policies have had a positive effect on staff retention. In South Africa, a study conducted by SEDA in 2021 observed that there was a reduction of 6.2% in jobs for period Q1 2020 to Q1 2021. The same report observed that for the same period there was a 11.1% reduction in the total number of MSMEs, 11.7% reduction in formal MSMEs and a 11.2% reduction in informal MSMEs. Therefore, COVID is expected to have had a negative impact on the jobs provided by MSMEs.

Improving the productivity of MSMEs will contribute towards closing the productivity gap between large companies and MSMEs within the same country or industries, which vary a factor of two or more (Albaz et al., 2020). It's important to improve the productivity of MSMEs as it will contribute positively towards the country's economic growth and reduce inequality. Productivity is expected to be reduced because of the COVID- 19 pandemic, because of the decrease in demand for goods and services, reduction in sales and profits (Alexander & Karger, 2020; Nair, 2022). Alexander and Karger (2020) further justify this point based on the finding that customer visits to non- essential business reduced by 51% and revenue at restaurants and other MSMEs dropping 37%. Blanas and Oikonomou (2022) however suggest that productivity is expected to increase in essential service providers like healthcare and social services. Fazio and Piacentino (2010) also suggest that businesses located in social decay experienced low productivity. Based on this logic, it would therefore be expected that MSMEs in developing countries or resource constrained environments would experience even lower productivity because of the pandemic. Given that 32 % of MSMEs in South Africa are classified as essential service providers (FinScope, 2020), we assume that a large portion of MSMEs will experience lower productivity because of the pandemic.

Several studies have found that about 50 % of MSMEs had temporarily stopped trading during the lockdown, with about 60 % MSMEs at risk of running out of their cash reserves (Brown et

al., 2020; Bartik et al., 2020; Cowling et al., 2020). A study by Bartik et al. (2020) supports with these studies after they conducted a study to assess the impact of COVID-19 on small businesses in the US over a 3-month period and the found that the pandemic brought about a reduction in cash flows to meet ongoing expenses. They also found that medium businesses in the US were left with only 2 weeks cash in reserves to support their operations. Apedo-Amah et al. (2020) also agrees after finding that 50% of MSMEs in the US have less than 15 days in cash reserves, inclusive of healthy MSMEs have less than two months of cash reserves. From an emerging markets perspective, Beebeejaun, A. (2022) observed that MSMEs in Mauritius experienced a 52% reduction of cashflow. However, not all research agrees with this conclusion, with Hurley et al. (2021) concluding that COVID- 19 had no effect on cash flows for MSMEs in the United Kingdom. The South African government also established a relief program through the Department of Small Business Development to assist MSMEs during the crisis. The funds and aid were made available to MSMEs to assist with acquisition of input, labour, and operational costs, and to provide much needed relief on existing debt obligations. These funds and facilities would be limited to the impact resulting from COVID and match the patterns of the MSME's cash flows. Therefore, it is expected that COVID- 19 had a negative impact on the cashflow position of MSMEs in South Africa.

The policy responses across the world resulted in a decline in global trade, thus having a negative effect of imports and exports. Developing countries experienced a steeper drop in exports, thus impacting the MSMEs in those countries (Nair, 2022). COVID- 19 has had a negative impact on the logistics of MSMEs from a hub and delivery path perspective (Reid et al., 2021). In India, Shafi et al. (2020) found that MSMEs in Pakistan were heavily impacted and “experienced financial issues, supply chain disruptions, decrease in demand, sales, and profit, with over 80 % of them ill- prepared to absorb the shock.” In Mauritius, there was a study conducted by Beebeejaun, A. (2022) which observed that 37% of MSMEs experienced disruption in their supply chains. This would obviously result in goods and services being available to service the market. It is expected that even the less aggressive policies would have a negative impact on the supply chains.

Less aggressive policy responses like social distancing have affected various business sectors, including MSMEs, and thus requiring businesses to be innovative and adopt technology to survive and improve performance. Kumar et al. (2024) found that ICT adoption has helped MSMEs survive the effects of COVID- 19 and can thus be used as a business strategy to support

MSME's resilience and sustainability efforts. However, Apedo-Amah et al. (2020) observes that MSMEs in response to the less aggressive policy responses globally, about 34% of MSMEs had started using digital platforms, internet, social media and invest in new IT equipment, software, and other solutions. Therefore, it is assumed that from a South African perspective, COVID- 19 policy responses will result in many MSMEs not adopting technology.

Brown et al. (2020) found that seed financing was the type of MSME financing mostly affected by the outbreak of the pandemic in the United Kingdom, with early-stage start-ups being the most affected type of MSMEs in the market. The impact of the pandemic appears to have had a similar major impact on MSMEs across the developed countries, with developing countries like China and Pakistan showing a significantly higher impact than that of the developed countries (Brown & Rocha, 2020; Shafi et al., 2020). MSMEs in South Africa largely depend on the owner's own capital, which is often insufficient to support the operations of a small business, especially one at the start- up stage (Makina et al., 2015). South African MSMEs have the option of debt or equity finance, made up of various sources of finance, provided by both the private and public sector. South Africa has a developed Private Equity and Venture Capitalist market, however most of these funds go towards late- stage investments (Noumba & Karimjee, 2019; Fatoki, 2021).

To support MSME finances during the pandemic, the United Kingdom and other OECD countries opted for debt finance in the form of loan guarantees and direct subsidised loans (OECD, 2020). It would be expected that most governments opted for debt finance as the preferred tool for their COVID- 19 policy response to support MSMEs. Further to their efforts to support the financing of MSMEs, the UK government established a Future Fund which aimed to provide matched funding for equity funded MSMEs (Brown et al., 2020). Other interventions in the UK included tax incentives like the Enterprise Investment Scheme (EIS) and Seed Enterprise Investment Scheme (SEIS). In the US, there was also an increase in debt finance by MSMEs, facilitated by commercial banks (Beauregard et al., 2020). The tools utilized by the US government were the Paycheck Protection Program (PPP) and the use of the PPP Liquidity Facility by commercial banks also assisted in the supporting MSME finances.

African countries experienced shock in the form of declined trade and investment activity, with fiscal and monetary measures as a suggested response to channel liquidity to MSMEs (OECD, 2020). A lot of the countries reduced interest rates to provide liquidity into their economies

(Albaz et al., 2020). The OECD (2020) also strongly recommends that progress be made to effectively implement the African Continental Free Trade Area (AfCFTA) and the African Union's productive transformation agenda to improve regional value chains, reduce vulnerability to external shocks, advance the digital transition, and build economic resilience against future crises. The decrease in interest rates encouraged for MSMEs to take on more debt.

In the South African context, the relieve provided by the Government and the commercial banks was also focused on debt finance to support MSMEs. This is approach was taken despite a high number (74%) of existing MSMEs who had taken out debt prior to the pandemic, unable to service their debt (Finfind, 2020a). The approach is somehow justified given that only 19.6 % of MSMEs were able to receive some sort of relief from formal debt providers (Finfind, 2020a). It is therefore expected that debt finance would be their preferred tool to support government policy responses to support MSMEs in South Africa, with some hope that there would also be an increase in the number of MSMEs that had previously not had access to finance before the pandemic.

The National Treasury (2001) reports that the many MSMEs are unable to access finance because their under- skilled and lack business experience. It's found that they also lack the financial planning and management skills, along with financial literacy required to raise funding (Finfind, 2020a). Finfind (2020a) also found that many MSMEs lacked finance readiness, which is their ability to produce and provide the required financial documents for funders to assess bankability and affordability.

## **2.6. Summary**

This section presents a detailed explanation of the impact of COVID- 19 on the MSMEs from a developed country and developing country perspective. The literature concluded that the aggressive institutional policy responses resulted in both temporary and permanent closure of MSMEs, job losses, reduced productivity and reduced cash flow and revenue. Less aggressive institutional policy responses to COVID-19 would have a negative impact on MSME supply chains. It is expected that credit guarantees provided relief options for MSMEs that required access to finance. Tax cuts and tax reliefs improved the cash flow pressures of MSMEs.

Payment holidays for MSMEs from commercial banks improved the cash flow pressures for MSMEs who were at the risk of default. It is expected that there would be an increase in the number of MSMEs who had previously not had access to finance before COVID. ICT adoption was accelerated by the social distancing policies and therefore increases the ability for MSMEs to survive and perform. MSMEs that were at risk of bankruptcy opted not to apply for more funding, while MSMEs who applied required funds for short- term needs.

## Chapter 3

### Methodology

#### 3.1. Introduction

This chapter discusses the research tools used to investigate the research problem. The chapter justifies the research methodology chosen for this study. The chapter starts by discussing the research approach and design, and then follows on to discuss the data collection and data analysis methods that were used to explore the research questions.

#### 3.2. Research Approach

This study aims to investigate how the financing of MSMEs in resource constrained environments like South Africa have been impacted by COVID- 19. The identified research objectives are exploratory as they seek to understand the impact of COVID- 19 policy responses on the financing of MSMEs. The inductive approach and qualitative research method were the preferred approach for this study. This study assumed the interpretive paradigm which allowed the researcher form findings based on the views and feedback, about the phenomenon being studied, received from the survey participants (Creswell & Creswell, 2008). The subjective points of view from the participants leaves some room for bias, but convey multiple perspectives which allowed for in- depth understanding of how the pandemic has impacted the financing of MSMEs. Saunders et al. (2012) support the use of an inductive study to obtain a deep understanding of the research problem. The study endeavours to obtain a deep understanding of the type of financing options available to MSMEs during the pandemic, and how some of the policy responses to the pandemic have impacted MSMEs through engagements with the participants.

#### 3.3. Research Design

Research design is defined as the specific procedures involved in the research process, which include data collection methods and data analysis (Creswell & Creswell, 2008), thus providing a framework for the research process. Creswell & Creswell (2008) also discusses the three different types of research designs; exploratory, explanatory, and descriptive. Exploratory research involves a flexible research approach aimed at generating new insights and ensuring comprehension (Alhassan, 2021). Explanatory research seeks to explain observed phenomenon, problems, or behaviour (Bhattacharjee, 2012). Descriptive research describes the characteristics

of situations, events processes, or other entities (Alhassan, 2021). This study uses the exploratory research design because of the aim to find new insights and gain an in- depth understanding of the impact of COVID 19 policy responses on the financing of MSMEs to ensure sustainability of these MSMEs. This design also allows for the exploration of challenges encountered by MSMEs in adapting to the new ways of work and the increased digitisation of world.

The study follows a case study methodological approach, which allows research findings to emerge from the themes inherent in the data (Obeng, 2015). Exploratory research design usually involves the review of existing literature, use of a small sample research in the form of in- depth interviews, focus group analysis and case study analysis (Alhassan, 2021). This study makes use of primary data collected from participants through interviews with MSMEs in Johannesburg, South Africa.

### **3.4 Population and Sample**

The target population in this study are MSMEs based in South Africa. It would've been unrealistic and time consuming to study the whole population of MSMEs in the country, and therefore, aligned with the principles of research, this study employed a purposive sampling technique to select the MSMEs who contributed towards this study. To control the scope of the study, the study was limited to purposive or selective sampling to focus on MSMEs based in the Gauteng province, specifically in Johannesburg. Gauteng is the smallest province by land yet houses more than a quarter of the country's population of 60 million. The province contributes 34 % to the national economy, with finance, real estate and business services being the sectors contributing the most, along with the manufacturing and trade. These sectors were all considered and represented in the sample selected for this study. Johannesburg is the economic hub of the province. Gauteng has the highest number of MSMEs at 33.9%, followed by Kwa- Zulu Natal at 16% (Seda, 2021). These numbers illustrate that the Gauteng Province gives us a good number of MSMEs from different sectors to choose from.

Qualitative studies generally have fewer participants than quantitative studies, and the sample size is based on saturation, which is the point at which point there's no new information (Creswell & Creswell, 2008). Therefore, the data collection for this study was set at a minimum of 5 participants or until the point of saturation. A purposive sampling approach was applied

for this study, as it allows the researcher to select participants based on their ability to provide in- depth and detailed information about the phenomenon under investigation (Creswell & Creswell, 2008). The study required the researcher to select participants who have the necessary knowledge and experience of running or operating MSMEs. The units of analysis for this study was 9 Gauteng based formal MSMEs in South Africa. The sample size is supported by Creswell & Creswell (2008), who suggests that semi- structured interviews require a sample size between 5 and 25. The interviewees were owners or directors of MSMEs who were operating business during the pandemic.

### **3.4.1. Data collection instrument**

To understand respondents' experiences, interviews can be used to provide the researcher with required detailed and quality data (Creswell & Creswell, 2008). Castillo-Montoya (2016) find that the Interview Protocol Refinement Framework (IPR) is an effective method to enhance the reliability and quality of interview protocols used for qualitative research and therefore assist with improving the quality of the data collected for research interviews. The Interview Protocol Refinement Framework of Castillo-Montoya (2016) is a four- phase process which starts with ensuring that interview questions are aligned with the research objectives, followed by the development of an inquiry- based conversation. The third phase relates to the receiving of feedback on the developed interview protocol, to enhance its reliability as a preferred instrument. The last phase relates to piloting or testing the interview protocol prior to launching the research interviews.

The research used in-depth interviews with entrepreneurs/directors of small businesses based in Johannesburg. Ethical clearance was granted by the University of Cape Town Ethical Clearance Committee on the 27<sup>th</sup> of November 2023. Once the approval was provided, the data collection started on the 7<sup>th</sup> of December 2023 and concluded on the 9<sup>th</sup> of January 2024. Administered surveys were used in the data collection process, meaning that respondents provided feedback directly to the interviewer. The respondents were not at the same place at the same time. The questions in the interviews were semi – structured to obtain a personalised and wider insight into the area of research. Semi – structured interviews are used gather information from participants relating to their personal experiences, attitudes, and beliefs (Creswell & Creswell, 2008). To avoid bias and maintain objectivity, the questions were not

repetitive and leading in nature. The questions were therefore open-ended to allow respondents to use their own words and expressions when providing responses.

### **3.4.2. Data Analysis**

Thematic analysis is used to identify recurring themes in data. It's a useful and flexible method for qualitative research (Braun & Clarke, 2006). The process follows an approach which is iterative and thus involves cyclical process of refining, tweaking, or correcting. Five phases can be applied to figure out the data collected from interviews (Braun & Clarke, 2006). The interviews were transcribed in verbatim and translated to allow for decontextualization or coding to take place. Coding is the first step of organizing data. This involves indexing key sections or items of the interview responses (Creswell & Creswell, 2008). The second stage relates to decontextualization, which involves the cross-checking of the codes with research questions and leads to reducing the number of codes into a more manageable number. The third stage involves categorizing codes based on how they relate to each other, and thus grouping them accordingly. Content analysis is then applied to establish key themes linked to the categories identified. The last stage involves the compilation of these themes to draw conclusions. This process is also iterative and thus requires constant refining, tweaking, and recoding of data. The outcome of this process results in inferences being made about the themes and relationships identified from analysing the data.

### **3.4.3. Trustworthiness**

According to Connelly (2016), trustworthiness refers to the degree of confidence one has in methods applied to interpret data to ensure the quality of a study. Qualitative content analysis is characterised by the following terms; credibility, dependability, conformability, transferability, and authenticity (Elo et al., 2014). The credibility of the qualitative data can be assured through appropriate identification and accurate descriptions of participants. Thick description of participants and their experiences were obtained, along with data triangulation to strengthen credibility. Dependability of the data refers to the stability or steadiness of the responses from participants. Reflection and reflexivity were applied to ensure that the interviewers own biases and assumptions are deliberately set aside. Conformability refers to the objectivity of the data collected from participants, where confidence can be placed on the research findings being based on participants' own words, without any bias from the researcher. To ensure conformability, all interview notes and audio recordings were transcribed to ensure demonstrate the basis of the analysis. Transferability refers to the level of applicability of the

findings to other similar settings or situations. Thick description of participants also supported transferability. Authenticity refers to the genuineness of the research process and its applicability to the field of study.

## Chapter 4

### Discussion of Findings

#### 4.1. Introduction

This chapter presents the research findings of the study from the data obtained through interviews that were conducted with MSMEs in Johannesburg. The interviews were conducted with MSMEs to try and understand the impact of COVID 19 policy responses on the financing of MSMEs. The semi- structured interviews allowed the researcher to collect qualitative results from the MSMEs. The questions also focused on understanding how access to finance was experienced from the MSME's perspective. This chapter consists of 3 main sections, starting with a description of the respondents who participated in the study, followed by a discussion of the thematic findings resulting from the analysis of data collected from the interviews. Lastly, a summary of the chapter is provided.

#### 4.2. Description of Respondents

A total of nine qualitative interviews were conducted with MSMEs to understand the impact of COVID-19 on the financing of MSMEs from a demand side perspective. Consent was obtained from all nine participants after it was explained to them that they will not be identified by name in any reports using information obtained from the interview and that their confidentiality as a participant in the study will remain secure.

The MSMEs were all Johannesburg based businesses in the Gauteng province, across different sectors and industries. All the MSMEs were registered companies with the Companies and Intellectual Property Commission (CIPC). The industries covered by the MSMEs are Transport, Manufacturing, Finance and Accounting services, Legal services, Business services (Procurement and maintenance) and Hospitality (Food, beverage, and entertainment).

All respondents were owners or directors of their businesses, with some of the respondents having more than one business operation. This is the case for two of the respondents who each had a legal practice and a different business, while another respondent owned a business consultancy business along with a retail franchise, craft brewery and restaurant. All the respondents had a business pre and post COVID- 19, with eight participants indicating a need for funding during the lockdown period. This information was useful in evaluating themes and trends resulting from the implementation of COVID- 19 policy responses and how these

benefited or challenged the operations and financing of MSMEs. Four of the MSMEs were able to secure funding or obtain some sort of debt relief during the lockdown period, with one receiving financing through a commercial bank, and others from government or development agencies like the Small Enterprise Finance Agency (SEFA).

*Table 8: Characteristics of respondents*

<b>Interviewee</b>	<b>Nature of Business</b>	<b>Position</b>	<b>Years in operation</b>	<b>Date of Interview</b>	<b>Duration of Interview</b>
<b>Respondent 1</b>	Pub, Butchery, Salon, Carwash	Owner and Director	6	07/12/2023	50 minutes
<b>Respondent 2</b>	Procurement and logistics in Health Sector	Director	4	07/12/2023	30 minutes
<b>Respondent 3</b>	Legal services	Managing Director	8	07/12/2023	66 minutes
<b>Respondent 4</b>	Supplies, facility management and Maintenance	Owner/ Director and Project Manager	17	07/12/2023	26 minutes
<b>Respondent 5</b>	Accounting services, incl. tax, payroll, and audit	Managing director	5	08/12/2023	44 minutes
<b>Respondent 6</b>	Transport	Owner and Director	15	11/12/2023	39 minutes
<b>Respondent 7</b>	Craft brewery and restaurant	Owner and Director	7	11/12/2023	41 minutes
<b>Respondent 8</b>	Manufacturing personal care products	CEO and Managing Director	7	15/12/2023	51 minutes
<b>Respondent 9</b>	Franchises, catering and tuck shops	Managing Director	8	09/01/2024	67 minutes

*Source: Researcher's study data*

### **4.3. Discussion of Thematic Findings**

The section discusses the themes extracted up from the thematic analysis of the interview responses, which were coded and aggregated into second order themes and aggregate dimensions. Annexure B provides a detail on how the responses were coded based on the data obtained from the interviews. The resultant themes came from the aggregation of the codes into second order themes and aggregate dimensions. This sub-section discusses the thematic findings from the analysis of the qualitative interviews on the two research questions.

#### **4.3.1 COVID-19 policy responses on MSMEs financing**

To understand the effect of the implementation of COVID -19 policy response on the demand side of MSME financing, the thematic analysis of the interview responses identified the following themes: financing options to support employee relief and retention; financing options to support the decrease in productivity; financing options to support cash flow and supply chain issues; financing options to support information and communications technology (ICT) adoption.

##### **4.3.1.1 Financing options to support employee relief and retention**

This theme discusses the responses of the respondents regarding the impact job losses have on the financing of MSMEs because of COVID- 19. This section also discusses whether there was a financing need for MSMEs and whether there was access to the finance they required to support employee retention.

###### **a) Job losses**

The respondents were asked how many employees they had pre and post COVID- 19 and whether there was a need to let go of any of them during the lockdown period in particular. They were also asked to distinguish between permanent and part- time employees. Six of the nine respondents confirmed to have retrenched some of their employees, although they confirmed not to have done so at the inception of the lockdown period. Temporary lay- offs of employees were implemented throughout the hard lockdown periods due to restrictions on trade for all six of the respondents.

There was broad consensus amongst the respondents that jobs provided by MSMEs were at risk due to the temporary closures of business from lockdown restrictions. Respondents confirmed to have experienced difficulties with paying salaries and wages during the lockdown period. Respondents highlighted the need to have skilled employees to survive the uncertainty that came with COVID- 19.

*“I eventually had to let go of my permanent employees due to cost pressures. No one was paying on time, and I’d therefore go months without getting paid for work that was done.”*

- Respondent 3

*“All my employees were part- timers, who would only be utilized when there’s projects to work on, however there were no projects allocated for months and had let go of them.”*

- Respondent 4

#### **b) Employee relief and retention**

There’s also consensus that the COVID-19 Temporary Employee/Employer Relief Scheme (TERS) was an appropriate policy response in order to provide relief to employees of MSMEs. This policy intervention by the government was relevant as it would target the relief of MSMEs and their employees. This meant that employees could keep their jobs during the disruption of business operations and thereby assist MSMEs to survive a bit longer.

*“The TERS fund presented SMEs with an opportunity to continue paying staff and relief pressure on business costs.”*

- Respondent 1

*“I was excited about TERS because it meant that I could help my employees claim from UIF. They were also excited about the fund when I told them about it.”*

- Respondent 8

*“The ability to retain all employees during this period played a pivotal role in fostering heightened motivation and performance. Consequently, when pandemic-related restrictions were lifted, the enhanced team morale contributed towards a noticeable increase in sales. The business witnessed a notable expansion in its workforce, progressing from 6 employees pre-*

*COVID to 30 as of the end of 2023. This all thanks to the loans and grants made available to SMEs by the government.”*

- Respondent 9

#### **4.3.1.2 Financing options to support decrease in productivity**

This theme discusses the decrease in productivity as a result the COVID- 19. Productivity is affected by a change in the demand for goods and services, and the change in sales and profits. The general feedback amongst the respondents is that there was a decrease in productivity during the lockdown period, with most of the respondents experiencing a decline in productivity because of lockdown restrictions. This created a need for financial assistance to cover the gap resulting from the decline in productivity. However, there were challenges in businesses trying to apply or access finance.

##### **a) Decrease in demand for goods and services**

The respondents were asked questions related to the relative demand for the goods and services they provided and whether there was an impact on their turnover, costs and profits. Seven of the respondents indicated that there was a significant decrease in the demand for the goods and services they were providing.

*“Demand for my goods and services dramatically decreased, but there were still costs like liquor license and Point of Sale system fees that were still payable.”*

- Respondent 1

*“I experienced difficulties in trying to collect or receive payments from customers, but I also understood that were delays in payments from their own customers. I was reluctant to seek further financing because I wasn’t confident that I would be able to service the debt on a monthly basis.”*

- Respondent 3

*“There was a huge reduction in fuel costs and car maintenance because people were no longer going into offices and those that were still required to do so were subjected to travel restrictions. There was no consideration to replace vehicles.*

- Respondent 6

Behavioural changes like limited time spent at shopping centres and malls, discovery of cooking recipes and home remedies resulted in a decrease in demand for certain goods and services, and this is certainly the case for 3 of the respondents whose businesses provide retail products.

It was also noted that those MSMEs that were providing essential services experienced an increase in demand for their goods and services. However, respondent 2 highlighted that as the restrictions were lifted, so did the demand for the goods and services they were providing. A few of the respondents indicated that there was increased need for accounting services for MSMEs. The increased demand was triggered by the need for MSMEs to be compliant in order to participate in any of the government relief programmes launched by the South African government.

*“I was supplying hospitals and clinics with goods during the lockdown period, which necessitated additional capital to fund operations, but I was unable to secure financing from both commercial banks and Purchase Order finance providers because the government purchase orders were seen as risky contracts.”*

- Respondent 2

#### **b) Decline in turnover and profits**

Majority of the respondents experienced temporary decrease in turnover as a result of a decrease in demand for goods and services, and limited operating hours. The consensus was that there was also an increase in operating costs, thus diminishing profits because of the requirement to have COVID personal protective equipment (PPE), COVID disinfecting services and other related guidelines. Four respondents also stated that they experienced an increase in operating costs as restrictions were lifted and trading activities normalized. Respondents who were running business that offered credit experienced an increase in bad debts as debtors were either closing shop or unable to pay debts. MSMEs therefore had a need for working capital financing to support their short-term operating activities.

*“Sales dropped instantly during the lockdown period. I had to adjust to selling my products through Takealot but found the fees to be too high and negatively impacting my expenses.”*

- Respondent 8

#### **4.3.1.3 Financing options to support cash flow and supply chain issues**

This theme discusses the responses of the respondents on cash flow and supply chain issues caused by COVID- 19. Respondents found that there was a reduction in cash flow to support operating expenses, and there was a decrease in import and export activities, creating a need to access finance.

##### **a) Reduction in cash flow to support operating expenses**

The respondents highlighted that there was a reduction in cash flow to support short-term commitments and operating expenses. This notion supports the need for most of the respondents to obtain some sort of debt relief or access to finance.

Five of the respondents confirmed the receipt of moratoriums or favorable payment terms on both rent and credit obligations from their landlords and creditors, respectively. This financial flexibility played a crucial role in enhancing their cash flow management, prolonging the viability of their businesses.

*“I received a 6-month moratorium from my landlord, which really helped release the cash flow pressures.”*

- Respondent 3

*“I started using white- label fuel stations instead of the popular retailers to service my fleet. This enabled me to obtain discounts.”*

- Respondent 6

In contrast, two respondents opted to use personal savings as a means of supporting their businesses. They emphasized their capacity to do so owing to the combination of sufficient savings and the absence of any pre-existing business debt.

*“I saw an opportunity to scale up, and therefore used my savings to do so. I am now in a position to grow further and would like to apply for financing.”*

- Respondent 5

##### **b) Decrease in import and export activities**

There was consensus amongst respondents that COVID- 19 created supply shortages and they were not able to import goods for their production activities. Respondents were asked whether their business does any imports and exports, and asked to elaborate whether those trading activities impacted their ability to supply and meet their customer demands. Three of the respondents confirmed that they were importing material inputs in order to produce their products. This created a working capital gap for MSMEs in order to cover their short-term needs.

*"Yes, I import goods through a third party, which were negatively impacted by the lockdown restrictions. It resulted in delays and an inability to deliver to clients on time. My customers are government departments, and they were very understanding."*

- Respondent 2

*"I was no longer able to import grain for the brewery, and then decided to use local alternatives, which I have stuck with post COVID."*

- Respondent 7

*"I was unable to import certain pigments which are only available abroad. It meant that I stop manufacturing certain products until I was able to import those pigments again. This had a negative impact on the demand for those products, as consumers started using alternatives."*

- Respondent 8

#### **4.3.1.4 Financing options to support information and communications technology (ICT) adoption**

This theme discusses the responses of the respondents regarding the impact of information and communications technology (ICT) adoption during COVID- 19 lockdown periods. The increase in ICT adoption as a result of COVID- 19 is discussed in detail. This resulted in a need for MSMEs to seek funding or access finance to invest in ICT to remain competent and survive the crisis.

##### **a) Increase in ICT adoption**

All the respondents highlighted that there was an increase in ICT adoption during the COVID-19 lockdown period. In particular, there was a need to urgently understand and use video conferencing tools like Microsoft Teams and Zoom. The respondents further highlighted that

the quick adoption of this online capability enabled businesses to be more efficient. Two of the respondents also stated the need to invest in accounting software, which contributed towards better preparation of their annual financial statements, therefore assisting their businesses to meet the requirements to obtain finance.

Respondent 3 articulated an increased reliance on online subscriptions to acquire information and self-educate. Conversely, Respondent 8 underscored the pivotal role of online platforms in sustaining their business, marking a strategic shift toward e-commerce. Presently, 40% of their business's sales are conducted online. However, they noted that engaging the online platform incurs higher costs, primarily attributed to advertising expenditures as the predominant contributing factor.

*“Using the online platform helped to sustain the business, but I find it expensive to run an online business because of the expensive marketing costs related to running ads.”*

- Respondent 8

#### **4.3.2 Benefits and challenges that MSMEs experienced in attempting to access debt relief or finance**

To explore the benefits and challenges that MSMEs experienced in their attempt to obtain debt relief or access to finance, the thematic analysis identified resilience and diversification as the benefits MSMEs experienced in accessing debt relief, while inability to access employee relief schemes and to access funding due to poor administration of funds as the challenges experienced by MSMEs in accessing debt relief. The themes are discussed below.

##### **4.3.2.1 Benefits**

The thematic analysis identified two key benefits that MSMEs experienced in their attempt to obtain debt relief or access finance during the pandemic. These included the increased resilience and diversification of MSMEs.

##### **a) Resilience**

The respondents all recognised the importance of setting up a resilient business to survive black swan events like COVID 19. The respondents noted the need to respond and adapt quickly to change, restructure your operations where required, introduce innovative solutions, diversify

your revenue channels, well- defined and documented processes and procedures, and appropriate insurance cover.

Four of the respondents highlighted the need to adapt quickly between the different restrictions applied during the lockdown period. This resulted in all four of them restructuring their operations in a way that will minimize their costs and maximize returns.

*“I closed the butchery and the pub but retained the bottle store as there was less costs associated with a bottle store. It also meant that I was operating at about 25% capacity.”*

- Respondent 1

Similar feedback was received from respondent 7, who stated that they rented out some of the space available on their premises.

#### **b) Diversification**

Diversification was highlighted as an important factor for resilience by all respondents. Not only diversification of revenue streams through different client types or profiles, but also seeking opportunities in different industries and sectors. Two respondents stated that providing goods and services that have more than one touch point in a value chain helped diversify businesses. Three of the respondents mentioned the need to continuously negotiate discounted rates and alternative suppliers to free up cash flow.

#### **4.3.2.2 Challenges**

The thematic analysis identified two key challenges that MSMEs experienced in their attempt to obtain debt relief or access finance. These include the inability to access employee relief schemes and access finance.

##### **a) Inability to access employee relief schemes**

Most of the respondents found the implementation of the scheme to be ineffective due to the unresponsiveness of administrators. They also found the process to be punitive to MSMEs that were not consistently making unemployment insurance contributions on a monthly basis.

Four of the respondents indicated that they had applied for or shown interest in the COVID-19 Temporary Employee/Employer Relief Scheme (TERS) in order to assist their employees during the lay-off period.

*“I applied for the Temporary Employer/Employee Relief Scheme (TERS) to assist with staff salaries. We only got two payouts and received no response after numerous submissions. I eventually had to retrench 4 employees.”*

- Respondent 1

*“We didn’t meet the requirements for the Temporary Employer/Employee Relief Scheme (TERS) because we had more than 10 employees, and therefore opted to go through SEFA and applied for relief funding to mainly fund staff costs. We were not happy with the loan terms because they were prescriptive on how we should use funds. Overtime, we let go of staff because we restructured business operations and closed the restaurant.”*

- Respondent 7

*“I didn’t qualify for the Temporary Employer/Employee Relief Scheme (TERS) because I was behind on Unemployment Insurance Fund (UIF) contributions to SARS. As sales were declining, I had to let go of two of my staff.”*

- Respondent 8

*“I successfully applied for to participate in the Temporary Employer/Employee Relief Scheme (TERS), which took care of salaries for 12 months. Being an accountant, by profession, made it easier to understand the requirements and ensure that my company is compliant. I understand that for most SMMEs, it’s cheaper to call out an accountant once a year, which may result in penalties being imposed on the company.”*

- Respondent 9

## **B) Inability to access to finance**

All respondents agreed that the decrease in interest rates during COVID made debt finance cheaper and therefore more attractive. They also agreed that access to finance remained a challenge, despite government interventions to make it accessible to MSMEs during COVID. Respondents had a unanimous consensus that all government related COVID relief and loan

programmes for MSMEs were clearly communicated and well drafted but were poorly executed. There was also consensus that access to finance enabled business to survive and grow.

All respondents were asked whether they applied to the Department of Trade Industry and Competition (DTIC) for any of the relief measures in support of MSMEs in distress, debt relief finance scheme or the business growth/resilience scheme. They were also asked whether they had requested or offered moratoriums on existing debt. Lastly, they were asked to share their experience regarding the application process and the terms of conditions on loans or relief granted.

*“I didn’t apply for any relief measures because professional services were not favoured and were excluded”*

- Respondent 5

Seven of the nine respondents were interested and applied for relief finance. As discussed earlier, TERS was one such programme that was available to assist with employee salaries. Respondents 2, 3 and 6 started the application process, but didn’t proceed due to the minimum criteria not being met. Respondent 3 was interested in the Legal practitioners’ benevolent scheme grant but did not meet the qualifying criteria.

*“The Benevolent Scheme grants were made available to practising legal practitioners. I was certainly interested in applying for the grant, but found it be exclusionary to senior practitioners. I didn’t meet the net income requirement of less than R30 000 per month.”*

- Respondent 3

Respondent 8 stated that they went through the Gauteng Enterprise Propeller (GEP) in order to get assistance through the Gauteng Rebuilding fund, which was aimed at supporting businesses affected by COVID 19 and looting/unrest. They eventually got funding after going through the Absa COVID 19 Term Loan scheme and was happy with the low lending rate offered by the scheme.

*“The application process wasn’t tedious, but the unresponsiveness of employees at the GEP led me to give up and seek assistance at my commercial bank.”*

- Respondent 8

Respondent 7 stated that they'd received funding from the Small Enterprise Finance Agency (SEFA), but was not happy with the terms provided, while respondent 9 participated in two other COVID relief programmes; the Township and Rural Enterprise Programme (TREP) and the Tourism Equity Fund.

*“The loans received from the different programmes helped the business retain key employees and grow further.”*

- Respondent 9

#### **4.4 Discussion of Findings**

This section discusses the themes that came out from the responses obtained from the nine semi-structured interviews held with MSMEs. The responses reveal that COVID-19 policy responses to MSMEs financing had an impact on jobs provided by MSMEs, productivity, cash flow, supply chain, information and communications technology adoption, access to finance and tested the resilience of MSMEs in South Africa. These findings are supported by Aftab et al. (2021) who found that MSMEs encountered similar unfavourable implications as a result of COVID-19.

MSMEs in developing countries are vulnerable to public policy responses imposed by government to counter COVID-19 (Kabir & Abubakar, 2022). Smart lockdown policies are therefore required to support MSMEs with the financing options to adequately address operational issues they faced as a result of COVID-19. Effective debt relief programmes play an important role in providing much needed access to finance and contribute towards the sustainability of MSMEs. Debt relief programmes also assisted MSMEs to transform themselves and their businesses, and contributed towards the growth of their businesses.

It was found that the lack of adequate financial literacy and financial management skills excluded some MSMEs from participating in the debt relief programmes, resulting in job losses and business closures. To provide the right support to MSMEs, the government must introduce smart policies to counter lockdowns, expand their programme content to include financial literacy and financial management concepts, and ensure that their implementation partners are not just broad, but are capacitated and skilled enough.

#### **4.4.1 COVID-19 policy responses on MSMEs financing**

Some of the fiscal measures implemented by the South African government to support businesses facing distress through the Unemployment Insurance Fund (UIF) and special programmes from the Industrial Development Corporation (OECD, 2020). The results indicate that the Covid-19 Response Programme as a policy intervention from government to support MSMEs during COVID was relevant and attractive to most MSMEs. Information regarding the different funds available was easily accessible, with the qualifying criteria clearly stated and documented.

SMEs need to apply various types of strategies to respond to crises. These include adopting flexible HR policies, product diversification, explore new markets and have a formal crisis plan (Alves et al., 2020). These topics were all discussed with the respondents, and they largely accepted by all. A debt policy also has an influence on the survival of a business, and therefore SMEs need to focus on finding satisfactory debt levels (Yazdanfar & Öhman, 2014). Some respondents confirmed the importance of ensuring debt levels are well- managed to help survive COVID- 19 lockdown periods.

#### **4.4.2 Benefits and challenges that MSMEs experienced in attempting to access debt relief or finance**

Financial education and literacy are key to improving access to financial markets and services (Sukumaran, 2015). It's therefore key to focus on these areas in order to counter the challenges faced by MSMEs in their attempt to access finance. Funding under the banking structure and tax regulation are seen to lower the risk of poor credit choices (Liu et al., 2022). Following engagements with respondents on access to financial markets and services, it was found that MSMEs struggled with compliance issues from a SARS perspective, poor account conduct and credit record. In order to work around some of these challenges, some MSMEs opted to go to development finance institutions before considering a commercial bank for debt finance.

The implementation of smart policies by the government to support MSMEs with more and accessible financing options will assist with creating more resilient business with diverse income streams. The implementation of these smart policies requires the right partners, including both development finance institutions and commercial banks. The application processes and requirements should not be too laborious, with the employees of the

implementation partners provided with adequate training and support to ensure competency and responsiveness.

## Chapter 5

### Conclusions and Recommendations

#### 5.1 Introduction

This chapter provides a summary of the research findings and conclusions, then follows to provide policy recommendations to policymakers and MSMEs. Lastly, the chapter provides suggestions to students and researchers on avenues for future research relating to the financing of MSMEs.

#### 5.2 Summary and conclusions

The main aim of this paper was to understand the impact of the COVID-19 outbreak on small businesses, with specifically emphasizing its effects on the financing landscape of MSMEs, using South Africa as a case study. This study has largely achieved this objective. In answering the first research question of how MSMEs have been impacted by COVID-19 policy responses, it's concluded that they were affected by the lockdown restrictions, social distancing and limited travel and use of public spaces. There were closures of non-essential businesses, albeit on a temporary basis for the majority. These findings are consistent with the findings of Kabir and Abubakar (2022). Loss of jobs, reduced productivity and revenues, liquidity and cashflow shortages, and supply chain interruptions were the result of all these policy responses to deal with the global crisis.

The second research question was to establish how MSMEs were able to gain access to relief and obtain financing to survive the recession and potentially grow. The investigation concludes that the COVID-19 response program devised an extensive array of relief and loan initiatives aimed at providing support to MSMEs. MSMEs still encountered difficulties in trying to access finance, despite the credit guarantee schemes made available to them. This finding is not aligned with that of Corredera-Catalán et al. (2021) who suggest that the establishment of credit guarantee schemes reduce this adverse selection problem by making funds available for MSMEs at a lower cost and longer term.

One of the objectives of the study was to understand the effect of the implementation of COVID-19 policy response on the demand side of MSME financing, and it's been concluded that there is a willingness from the South African government to put guarantees in place and support the growth of MSMEs. The utilization of these credit guarantees remains limited, with both

commercial and development banks significantly underutilizing their allocated portions of the funds. Consistent with the findings presented in the FinFind (2020b) report, demand-side challenges persist, emphasizing the need for MSMEs to be educated on bank process and requirements, business management and financial planning.

The other objective was to explore the benefits and challenges that MSMEs experienced in their attempt to obtain debt relief or access to finance. In their endeavour to engage in the COVID relief program, MSMEs encountered difficulties associated with interacting with inadequately skilled individuals while seeking access to financial resources. Therefore, a sentiment emerged that banks and government agencies exhibited a reluctance to attentively address the distinctive challenges faced by these enterprises, consequently constraining their ability to effectively communicate and navigate their specific circumstances. An advantageous outcome arising from this experience was the recognition among numerous MSMEs of the imperative need to register and ensure full compliance with the stipulations of the Companies Act. This realization underscored the fundamental nature of such compliance as a prerequisite for accessing financial resources. An additional revelation pertained to the imperative of cultivating business resilience as a strategic imperative for enduring comparable crises should they transpire.

## **5.3 Policy recommendations**

### **5.3.1 Governance**

MSMEs need to ensure that they understand the requirements be registered entities and educate themselves on the different options to them. They also need to ensure that they are fully tax compliant and have the discipline to make those monthly UIF contributions to the South Africa Reserve Service (SARS). This will ensure that your employees are covered in the short- term should they be unemployed or unable to work. The need to ensure that they monitor, track and follow up on the work that their accountants do on their behalf relating to compliance matters. This will go a long in proving to a bank that you are running a compliant business.

### **5.3.2 Financial and business management**

MSMEs need to educate themselves on basic financial literacy and financial management skills. This starts with ensuring that accounting records and bookkeeping is done accurately, as this informs the business financial statements. Interpretation of financial statements and key ratios is key because it will help them understand how to maximise returns and understand credit affordability metrics.

Banks take into account individual risk profiles during the finance application process. Consequently, having a comprehensive understanding of one's risk grading, strategies to enhance the risk profile, and maintaining favourable account conduct significantly enhances the likelihood of securing credit from financial institutions. This necessitates MSMEs to adopt a proactive approach, regularly monitoring their credit scores through credit bureaus.

It's imperative that each entity is responsible for its own profits and losses, and therefore important for MSMEs with more than one business entity organize themselves in such a way that each business expense relates to the correct business entity. Likewise, the separation of business and personal expenses. This will help the MSME to illustrate the profitability of their business more accurately and provides an opportunity to find efficiencies in their business operations.

### **5.3.3 Alternative sources of finance**

MSMEs have access to various alternative sources of financing, potentially more tailored to their specific requirements. Numerous financial institutions offer specialized products designed for the unique needs of MSMEs, including offerings such as invoice discounting, purchase order financing, and trade finance. It becomes the responsibility of MSMEs to proactively educate themselves about these financial products and the corresponding service providers. Moreover, providers of alternative financial products should intensify their efforts in marketing and outreach to MSMEs. Furthermore, considering the low market penetration, there exists potential for the venture capitalist (VC) market to expand in South Africa. Participants in the VC sector have an opportunity to enhance their outreach by further articulating and promoting the VC model and its value proposition within the market.

### **5.3.4 Government agencies/Development banks**

MSMEs are presented with the prospect of engagement in diverse programs facilitated by institutions such as the National Youth Development Agency (NYDA), Small Enterprise Development Agency (SEDA), Gauteng Enterprise Propeller (GEP), and Small Enterprise Finance Agency (SEFA). These entities offer a range of financial literacy, finance, and business management training initiatives designed to provide substantive support to MSMEs. It's therefore encouraged that MSMEs attend these free training sessions instead of only going to these institutions for grants and loans.

These institutions are recommended to establish training interventions for their personnel, ensuring they are well-equipped to effectively assist MSMEs with their financing requirements. Along with the commercial banks, there's a need to for financial institutions to make better use of the credit guarantee schemes and improve take- up on the schemes.

#### 5.4 Avenues for future research

This study has shown that that there's aspects of both the access to finance for MSMEs and the impact on COVID 19 policy responses on MSMEs that can be further investigated. It's important do so in the South African context given that access to finance for MSMEs remains an issue that stifles growth and job creation. Therefore, there's future research opportunities to explore.

This focused mainly on the demand side of access to finance, therefore, there's an opportunity to investigate the experience of other regions of the country and other developing countries. There's also an opportunity to investigate the supply side of access to finance, so as to understand the impact of COVID 19 on the financing of MSMEs from a supply- side perspective. This would give the researcher an opportunity to understand the viewpoint of mainly the banks, government agencies and DFIs.

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# Appendices

## Appendix A: Interview Consent form

### Master of Commerce in Development Finance INTERVIEW CONSENT FORM

**Participant name:**

I volunteer to participate in a research project conducted by Kgaogelo Tshehla as partial fulfilment of the requirements for the **Master of Commerce in Development Finance Degree** at the UCT Graduate School of Business. I understand that the research is designed to gather information about **COVID-19 and post COVID-19 financing of MSMEs** and that I will be one of approximately 15 of people being interviewed for this research.

**Objective(s) of the research**

The objective of the study is to understand the impact of COVID- 19 on the financing of MSMEs in developing countries with evidence from South Africa. Therefore, the study aims to achieve the following:

- To understand the effect of the implementation of COVID -19 policy response on the demand side of MSME financing.
- To explore the benefits and challenges that MSMEs experienced in their attempt to obtain debt relief or access to finance.

**Ethics approval**

The ethical clearance for this study was approved by the UCT GSB Research and Ethics Committee on 27/11/2023

**Participation and confidentiality**

I understand that my participation in this research is voluntary, that I will not be compensated and that I may withdraw at any time. The interview will take approximately 45 - 60 minutes to complete and will be audio recorded.

I understand that I will not be identified by name in any reports using information obtained from this interview and that my confidentiality as a participant in this study will remain secure. Subsequent uses of records and data will be subject to standard data use policies which protect the anonymity of individuals and institutions.

Should you have any questions or concerns please contact me on [TSHKGA004@myuct.ac.za](mailto:TSHKGA004@myuct.ac.za) or my supervisor ([latif.alhassan@uct.ac.za](mailto:latif.alhassan@uct.ac.za))

**Consent**

I consent to participate in this interview, based on the terms outlined above.

-----  
**Signed by interviewee**  
.....

-----  
**Date**  
.....

**Signed by Student**

**Date**

## **Appendix B: Interview questions**

### **Section 1: Demographic information**

1. Gender of respondent:
2. Age of respondent
3. Nature of business
4. Years of experience
5. Current role in business

### **Section 2: Interview questions**

1. What is your current role in the business?
  - Owner/CEO/MD?
  - FD/FM?
  - Other?
2. What is your industry?
3. Is your business currently operational?
  - If yes, are you fully on site, remote working or partially operational?
4. How long has your business been operational?
5. Were you able to operate your business during the lockdown?
  - Did you have to apply through the Department of Trade Industry and Competition (DTIC)? (Relief measures, support for MSMEs in distress, Debt relief finance scheme, Business growth/resilience facility)
  - How did you find the process?
6. How many employees did you have before COVID – 19 (Permanent, temporary or part-time)?
7. How many employees did you have after COVID – 19 (Permanent, temporary or part-time)?
  - How many employees were let go during the pandemic?

8. Did you experience a decrease or increase in demand for goods and services?
9. Does your business do any imports and exports?
  - How has that impacted your supplies and meeting your customer demands?
10. Please provide your estimated annual sales turnover for the last financial year.
11. What was your annual sales revenue before COVID?
12. Did you require any relief? If so, what type (moratorium on existing debt)?
  - Did you make use of any credit guarantee scheme?
  - Were you happy with the terms?
13. Have your current operating costs changed relative to the beginning of COVID?
  - Which cost contributed the most? Electricity?
14. Did your costs increase or decrease during the lockdown periods?
15. Did you experience cash flow problems as a result of the pandemic?
16. Did you benefit from any tax cuts and tax reliefs?
17. Were you required to restructure your operations?
18. Was the business able to respond swiftly to unexpected challenges during the lockdowns?
19. What innovative solutions were introduced to assist with managing the crisis?
20. Does your business rely on information systems or manual systems?
21. Did you have to invest in new IT equipment and software? If so, how did you fund it?
22. Were you able to make use of your resources efficiently to help manage challenges?
23. What were the learnings of operating the business during COVID- 19? Did it help you prepare for future challenges and crises?
24. What valuable knowledge and experience have you gained from the impact of COVID relating to managing a similar crisis?
25. Does your business have well- defined and documented processes and procedures to help respond to crisis events, incl. business continuity plans?
26. Do you have insurance to cover for some of the emerging or newer risks?

## Appendix C: Respondent profiles and findings

### Summary of Thematic Findings – Impact of COVID policies on MSMEs

<p><b>Employee relief and retention</b></p>	<p><b>Job losses</b>            Temporary lay- off of employees during hard lockdown.            Retrenchment of staff due to cost pressures.            Part- time employees were able to regain employment post lockdown.</p> <p><b>Changes in working patterns</b>            Increased efficiency by allocating more tasks to an individual.            Introduction of hybrid and remote- working for professional service.            Increased demand for jobs in industries providing essential services.</p> <p><b>Effective policy intervention</b>            The COVID-19 Temporary Employee/Employer Relief Scheme (TERS) provided support to businesses that are in distress.            Successful applicants of TERS resulted in businesses retaining their employees.            Unsuccessful applicants of TERS resulted in businesses retrenching their employees.</p>
<p><b>Decrease in Productivity</b></p>	<p><b>Demand for goods and services</b>            Substantial decrease in demand for goods and services because of uncertainty and lockdown restrictions.            Increase in demand for the essential service providers, with subsequent decrease post the lockdown period.            Increase in demand for accounting services to assist MSMEs comply and thereby assist them to apply for COVID related grants and/or funding.</p> <p><b>Decline in turnover and profits</b>            Increase in bad debts due to customers closing shop or unable pay debts.            Decrease in sales as a result of a decrease in demand for goods and services, and reduced operating hours.            Increase in costs because of PPE, sanitisation, deep cleaning and packaging requirements.            Increase in costs as restrictions were lifted and operation activities improved.</p>
<p><b>Cash flow issues</b></p>	<p><b>Reduction in cash flow to support operating expenses</b>            Inability to collect from debtors on time.            Moratoriums and favourable payments terms from creditors assisted with managing cash flow.            Businesses with less debt were able to manage their cash flow better.</p>
<p><b>Supply Chain issues</b></p>	<p><b>Decrease in import and export activities</b>            Restrictions caused delays and inability to deliver goods to customers.            Businesses resorted to use local alternatives when they were unable to import goods.            Some product items could no longer be produced as a result of restrictions on imports.</p>
<p><b>Information and communications technology (ICT) adoption</b></p>	<p><b>Increase in ICT adoption</b>            Investment in video conferencing tools like MS Teams and Zoom.            Investment in accounting software like QuickBooks.            Increase in online subscriptions as a source of information.</p>
<p><b>Access to finance</b></p>	<p><b>Decrease in interest rates made borrowing cheaper and attractive</b>            Successful applicants of COVID related funding were able to use it in order to increase sales and profits.</p>

	Businesses preferred to go through government agencies instead of commercial banks to access finance
<b>Resilience</b>	<p>Respond and adapt quickly to change.</p> <p>Restructure operations.</p> <p>Introduce innovative solutions.</p> <p>Document processes and procedures, including business continuity plans.</p> <p>Appropriate insurance cover.</p>