

UNIVERSITY OF CAPE TOWN



MASTER OF COMMERCE IN DEVELOPMENT FINANCE



# Exploring the role of DFI's in developing township economies

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Date: .....

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## ABSTRACT

Townships are hubs of entrepreneurship with many micro and small businesses which provide opportunities for employment and poverty alleviation. The township economy, by virtue of our past, is often overlooked and underserved regarding economic development. The government has over the past few decades introduced initiatives to promote SMME development, particularly for township enterprises. Development Finance Institutions (“DFIs”) have emerged as significant facilitators in utilising their resources and financial know-how for direct investment into the township economy. DFIs have emerged as valuable institutions in supporting the township economy, bridging the gap between financial exclusion, and needed economic development. The research explores the role and effectiveness of DFIs in supporting the township economy. The study employed a qualitative research approach covering a sample of 3 representatives of the DFIs and 10 township entrepreneurs operating in Gauteng province from four townships of Tembisa, Soweto, Katlehong and Mamelodi using a semi-structured questionnaire for in-depth interviews.

The study found that DFIs have a mandate to promote economic growth by providing financial and non-financial support where the market has failed to invest adequately. DFIs face a challenge as business support depends on the strict bankability factors resulting in a high failure rate for township businesses. In the absence of grants their performance is limited by their limited capacity and available capital. These factors limit penetration thus affecting the ability to materially transform the township economy. While there is evidence of considerable investments, job creation and value add administered into the townships because of DFI participation. SMMEs experience challenges in working with the DFIs which poses a risk to their overall effectiveness. SMMEs want to be part of the solutions and not to have the solutions presented to them.

Based on the findings, it is recommended that to unlock the full potential of DFIs, they must adopt an integrated and inclusive approach, which focuses on the needs of the SMMEs being served. Policy reforms, legislation, and programs to create a favourable environment for local township SMMEs must be designed with their full participation. The government needs to invest in more innovative ways to improve bankability for the township entrepreneur. Given the low penetration rate, the focus should rather be on bankability incorporating special programs to incubate businesses. The government should make an allocation in its budget for grants towards DFIs as this will enable these institutions to make more advances at risk-free rates to boost economic growth.

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## **GLOSSARY OF ACRONYMS AND ABBREVIATIONS**

Stats SA	Statistics South Africa
GDP	Gross Domestic Product
OECD	Organisation for Economic Co-operation and Development
SMME	Small Medium and Micro Enterprise
SMMEs	Small Medium and Micro Enterprises
DFI	Development Finance Institution
DFIs	Development Finance Institutions
GEM SA	Global Entrepreneurship Monitor South Africa
NECI	National Entrepreneurship Context Index
DED	Department of Economic Development
GDED	The Gauteng Department of Economic Development
NGP	New Growth Plan
NDP	National Development Plan
NSB	National Small Business
KHULA	Khula Enterprise Finance
SEDA	Small Enterprise Development Agency
SEFA	Small Enterprise Finance Agency
SAMAF	South African Micro Apex Fund
NEF	National Empowerment Fund
DTI	Department of Trade and Industry
NEF	National Empowerment Fund
GEP	Gauteng Enterprise Propeller
FDI	Foreign Direct Investment
EDFI	European Development Finance Institution.
DSBS	Department of Small Business Development
USA	United States of America
GEP	Gauteng Enterprise Propeller
ICLS	The international Conference of Labour Statisticians
WIEGO	Women in Informal employment: Globalizing and Organizing
IPF	Interview Protocol Refinement
SIBs	State Investment Banks
MFT	Market Failure Theory

FFT	First Fundamental Theorem
LLR	Loan Loss Rate
NPLs	Non-Performing loans
ROA	Return on Assets
ROI	Return on Investments
GPG	Gauteng Provincial Government
TREP	Township and Rural Empowerment Programmes
GBV	Gender Based Violence
IPAP	Industrial Policy Action Plan
NYDA	National Youth Development Agency
BEE	Black Economic Empowerment
BRICS	Brazil, Russia, India, and China
DHA	Department of Home Affairs

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# **Chapter 1**

## **Introduction**

### **1.1 Background of the study**

The South African economic growth agenda remains a challenge in dealing with poverty and structural inequalities. In 2020, the country reached the deepest contraction since the 1940s due to the impacts of the lockdown because of the global COVID-19 pandemic. According to Fitch the real Gross Domestic Product “GDP” fell 7.1 percent year on year in 2020 (Fitchsolutions, 2021). The recovery of which is estimated to have grown to 4.8 percent in 2021, against the contraction (Fitchsolutions, 2022). In 2022, Fitch forecasts that the ongoing impact of COVID-19, fading base effect and persistent structural problems will see economic growth slow to 2.1%. The rand is also weakened during this time with concerns over vaccines programme rollout and the increasing GDP deficit. However, there are still opportunities with the trends that the GDP is expected to grow post the crisis, and this growth will in turn alleviate poverty in the long term. The government has taken a firm view on the micro-economic reforms which includes improved skills training and support for the SMMEs.

According to Statistics South Africa “Stats SA,” the unemployment rates in South Africa continues to increase from 32.5% in quarter four of 2020 to 34.9% in the third quarter of 2021 and now reported to be 35.3% in the fourth quarter of 2021. This is the highest unemployment rates since the beginning of the Quarterly Labour Force Survey in 2008. According to Stats SA, the youth unemployment in South Africa, stands at 65.5%. This comes in the wake of the world bank report (Sulla et al. 2022) that South Africa is the world’s most unequal country. Even thirty-three years after the abolishment of apartheid, race plays a key role in how wealth is distributed according to the world bank report (Sulla et al. 2022).

Unemployment in South Africa remains extremely high and requires structural reforms in the economy with systemic changes required. Van Scheers (2016) Unemployment has been researched to be a major factor that impedes economic growth and hampering sustainable economic development in South Africa. One of the ways to solve for the unemployment crisis is to support entrepreneurship businesses which create a catalyst for economic growth and development. Entrepreneurship has always played an important role in economies of the world, inclusive economic growth and job creation are key ingredients to tackle poverty (Van Scheers,

2016). <sup>1</sup>In these countries, SMMEs are the main drivers of job creation as the main form of business. Entrepreneurship has been identified as a key contributor of employment, innovation and sustained economic growth and development. A strong realisation has emerged that economies should no longer rely on large companies to drive GDP, but rather SMMEs are making a considerable contribution to GDP of economies (Brock & Evans, 1989). SMMEs have been the foundation of economies in driving industrial development, due to their pure number, size and nature of business operations. Aris (2007) confirms that even in developed countries such as Japan, Korea, Taiwan and many others, economic growth in these countries was generated by activities by the SMMEs.

According to Global Entrepreneurship Monitor South Africa “GEM SA” (Bowmaker-Falconer & Herrington, 2020), South Africa ranked 49<sup>th</sup> out of 54 economies in terms of the National Entrepreneurship Context Index “NECI”, ahead of Croatia, Guatemala, Paraguay, Puerto Rico and Iran. The world bank study relating to ‘ease of doing business’ scored South Africa 67<sup>th</sup> out of 200 (World Bank, 2020). Notwithstanding the important role SMMEs have on the economy. South Africa is still facing challenges towards developing entrepreneurship as highlighted by the ‘ease of doing business’ study (World Bank, 2020). There are several challenges which are inhabitants and create barriers that limits the true growth potential. Some of the constraints that make “the ease of doing business” a challenge for SMMEs includes but are not limited to (i) access to funding and capital, (ii) lack of basic entrepreneurial training and/or financial literacy (iii) high data costs in a digital economy (Fourth industrial revolution) and (iv) over-regulations of small businesses leading to unnecessary red tape and (v) adverse macro-economic factors experienced (inflations, interest rates, exchange rates).

The government has over the past few decades introduced initiatives to promote SMME development. The Minister of the Department of Small Business Development “DSBD” announced new measures in pursuit of economic transformation and job creation in 2019, these programmes were aimed at the development of small businesses and cooperatives (Department of Small Business Development, 2019). These measures include, amongst others, (i) making funding available through all of the relevant departments, with commitments to improving funding turnaround times; (ii) introducing standard templates for funding applications across

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<sup>1</sup> The OECD is an international organisation that works to build better policies for better lives, it consists of 36 countries from the Americas, Europe, and Asia-Pacific. SMME enterprises account for 99% of all business in the OECD (Bowmaker-Falconer & Herrington 2020)

all DFIs; (iii) introducing the Small Business Innovation Fund, which will use a blended finance model to lower financial costs for entrepreneurs through means of loans and grants; and (iv) making provision to fund partner organisations such as incubators under certain conditions. Former president Jacob Zuma declared 2011 as the year for job creation and government pushing the economic growth through the New Growth Plan “NGP”. The NGP required more leverage of key government institutions and agencies of the state including but not limited to DFIs in the country (Baloyi et al., 2011). This was a way to channel funds to reach communities. (Rwigema & Karungu, 1999) highlights six forms of assistance available to SMMEs in South Africa. These include financial assistance, training and development, technical assistance, availability of information, industrial clustering and government and private sector support. The latter is observed by government setting up institutions such as Gauteng Enterprise Propeller “GEP”, Small Enterprise Development Agency “SEDA”, Khula Enterprises Finance Ltd, Umsobomvu, Gender and Women Empowerment Units and other DFIs to promote small business development which would include township enterprises. DFI roles and mandates are to promote sustainable development. Given their core mandates, DFIs are set to take centre stage in contributing to this agenda. They play an important role in supporting economic growth through the mobilisation of private investment in developing countries through their financing, risk-sharing, and supporting activities (Attridge, 2019).

### **History of South African Townships and the Township economy**

The history of South African townships is rooted in the apartheid system (Mahajan Sandeep 2014). Apartheid was a political and social system that was designed to keep different races separate giving massive power and advantage to white South Africans (Klemz et al., 2006). Almost three decades after the end of the apartheid regime, social and spatial structures in South Africa seem to have changed, particularly in the urban area. However, the continued use of ethnic association particularly on the part of policy-makers to aid the formerly disadvantaged groups through affirmative action programmes and discrimination against immigrants based on the country they are from, have made it all clear that some of the social reflexes learnt in the apartheid era still exist even today (Jürgens et al., 2013). The most obvious remnants of apartheid doctrine particularly relating to spatial organisation, is the so called ‘townships’ which is a term that emerged to identify ‘non-white’ neighbourhoods alone and was thus a core spatial concept of the apartheid era that still exists. South African townships are as a result of forced geographical marginalisation from mainstream economic hubs found in the European

urban areas where major economic activities occurs (Jürgens et al., 2013). These areas are where the majority of black South African still reside today, the areas are characterised by limited access to services and substandard infrastructure.

A disproportionately large portion of South Africa's unemployed population reside in the black townships due to the legacy of exclusionary policies and structural challenges that has hindered growth and development. Many of the residents in township still survive below subsistence level. This unemployed population in the township can benefit immensely from the creation of sustainable jobs through township-based enterprises.

Gauteng Provincial Legislature (2021) defines a township-based enterprise as an small enterprise, small enterprise organisations and co-operatives which is based or situated in a township designated in terms of section 6, and includes a small enterprise organisation. (Maphalla, S.T, Nieuwenhuizen, C. and Roberts, 2013) defines townships as specific areas outside major cities where the apartheid system forced black Africans to reside, separated from other races". (Gauteng Provincial Legislature 2021) refers to townships as "urban, peri-urban or rural living area which— (a) at any time from the late 19th century until 27 April 1994, was reserved for Black people; or (b) has been developed for historically disadvantaged persons after 27 April 1994".

Townships are known for extreme poverty rates and high crimes rates which one could argue is due to high employment rates. In a paper by (Scheba & Turok, 2020) titled the strengthening township economics in South Africa, it confirms that the informal sector in township economy is attracting a great deal of policy interest in South Africa, partly because of this persistence of concentrated poverty and the lack of economic transformation since democracy (The Citizen, 2018; Gauteng Province, 2014). "Township economy" refer to enterprises and markets based in what we refer to as townships. The businesses are operated by township SMME/entrepreneurs to meet primarily the needs within and often beyond the townships themselves (Department of Economic Development, 2014). These economies are diverse in nature and highly informal to meet the need of the community. The Gauteng province in February 2022 released a draft Township development bill which aims to provide a legal and regulatory framework for the promotion and development of townships economy. The bill aims to establish the Gauteng Township Economic Development Fund to support the development of these enterprises. The Fund is intended to (a) provide affordable and accessible credit or loans to township-based enterprises; (b) guarantee the repayment of or provide loan insurance

or credit insurance of financial obligations undertaken by township-based (c) enterprises; finance— (i) capacity building of township-based enterprises; or (ii) finance research, development, innovation, and transfer of technology. The township economy has the potential to support economic growth and job creation together with the formal business sector. Policy changes and support for small business could see this sector playing a more meaningful role in the recovery of the country.

## **1.2 Definition of Research Problem and Research Questions**

### **1.2.1 Research Problem**

From a South African context, there has not been a great deal of empirical literature written on the true impact of government support towards township economies. Township revitalisation is new concept which has recently been included in the National Development Plan “NDP” as late as 2014, 10 years post the apartheid regime. Premier David Makhura in his state of the province address in 2014, mentioned that “The significant participation and meaningful inclusion of the people of the township into mainstream economy of Gauteng through their own township enterprises that are supported by the government and big business will be one of the key game changers”. He went on to say that “Townships must be self-sufficient and vibrant economic centres” (Department of Economic Development, 2014).

There is a considerable amount of research on DFIs support for SMME in general however there is a need for location-specific research to take place considering the uniqueness of the township economy. Townships are politically and economically significant in South Africa. In their significance, they lurk behind their neighbouring urban core economies (Rakabe, 2017). In response, there is an increased focus by government to support township SMMEs in South Africa through mandated DFIs.

The research is focused on understanding the role and effectiveness of government support in the stimulation and development of the township economy considering the importance of SMMEs in general. The case study investigates the tools and mechanisms used as intervention for sustainable development in the township economy. There is a big drive by government to support SMMEs and particularly township SMMEs given South Africa’s history, however it is still evident that there is still a lag even with government led business development services. There is a need to investigate whether township enterprises do benefit from the intervention from DFIs. What benefits and challenges are associated with DFI support and how effective is this support to the small businesses on the ground. The question to consider is whether the DFIs

are in fact facilitating the economic growth and identify any potential hindrances toward such growth to fully reap the reward in this sector and contribute positively to the country's GDP.

The biggest challenge South Africans continues to face, is the inability to increase employment rates and reduce poverty. There is a disproportionately high both poverty and unemployment in what is deemed the 'Black townships' compared to the rest of the country. This is a legacy of the apartheid regime which we still live with in South Africa today, as evidenced by economic and social inequalities. Supporting small business and promoting entrepreneurship in the township, is one of the ways to eliminate these challenges because it has become clear that SMME are catalyst to economic growth which will in the long term alleviate poverty and reduce unemployment (Brock & Evans, 1989). The government has a firm believe that supporting township enterprises has a distinct and especially key role in creating a socially inclusive, labour absorbing and growing economy. According to the Gauteng Township Economy Strategy sets out by the Department of Economic Development "DED," the government is committed to ensure that the township economy contributes at least 30 percent of the province's GDP by 2030 in line with the NDP. The strategic partners in this strategy include government (national, provincial, and local) and its support agencies (DFIs) together with corporate sector. The support is in a form of financial and non-financial support to address barriers common to all SMMEs. Township enterprises struggle to grow their businesses and survive due to socio-economic challenges they face. These challenges hinder their success and participation in the formal economy and consequently the need for government intervention. There is a necessity to create an enabling environment for sustainable development and allow for infrastructure support via government intervention and playing a supportive role (Kubone, 2018).

### **1.3 Research Questions**

The motive of this study is to understand the role of DFIs in SMME development particularly relating to township economies. In exploring this role, the study looks to understand which government institutions are specifically tasked with SMME development and testing whether these DFI and government agencies are and have been effective. The study seeks to answer the following research question:

- a. What is the role of DFIs and government agencies in supporting township enterprises?
- b. What tools and mechanisms are used to develop township economies?
- c. How effective is the government role in developing township economies?

- d. What are the challenges of the entrepreneur's own experience when using government led development services?

#### **1.4 Research Objectives**

The overall aim of the study is to examine and analyse the research questions above. The following are the objectives of the study:

- a. To understand the role of DFIs in developing township SMME.
- b. To investigate the tools and mechanisms used by DFIs in promoting sustainable economic growth on township economies.
- c. To investigate the effectiveness of DFI programmes in developing township economies through the lived experience of township entrepreneurs.
- d. To understand the challenges of the entrepreneur's own experience when using government led development services?

#### **1.5 Limitations**

The type of research method (qualitative) has its own limitations. O. P. Atieno (2009) findings in a qualitative study cannot be expended to wider populations with the same degree of certainty than in a quantitative research study. This is because the research is not aimed to discover if statistically the results are significant or not. The other limitation could be bias from the interviewee to drive a certain agenda or narrative. The interviewee can deliberately provide misleading information which may not be true. Saunders and Lewis (2012) argue that qualitative, exploratory research is by its nature preliminary and therefore needs to be followed up with more detailed research to provide more dependable results. With face-to-face interviews, there is also the element of time pressure due participants not having enough time to engage in a meaningful manner to the study. There could also be knowledge gaps, so it is critical that in the DFIs or government agencies, the right level of seniority is important.

#### **1.6 Scope and Justification of the study**

There is growing literature on the importance of the development of SMMEs and how government support is crucial to their success. However, there is limited literature on the effectiveness of government support to SMME and to an even lesser extent with a keen focus on the development of township entrepreneurs and township economies at large. This research paper aims to fill this gap.

The study aims unpacks.

- Understanding the roles of DFIs and government institutions tasked with SMME development in general however with particular focus on township economies.
- Evaluate the effectively on these DFI and government agencies in developing SMME.

The scope of the research study is limited to SMMEs, (with particular focus on township SMMEs), DFIs which are mandated to support SMMEs through legislation as well as government agencies tasked with a similar role.

South African is handicapped with low economic growth, high levels of unemployment, and declining investors' confidence which have been exacerbated by political uncertainty together with political risks that have engulfed the country in recent times (Mopeli, 2018). The development of SMME is a fundamental way to address some of South Africa's socio-economics issues. SMMEs globally and in SA have come to play an increasingly important role in reaching desirable economic growth. (Chimucheka, 2013) mentions that the government has therefore targeted the SMME sector as an economic empowerment vehicle for previously disadvantaged people. Studies do however show that even with government support, business still face challenges which make the business environment unfriendly and difficult to navigate. Literature points out to the need for government support to aid the development of SMME (Chimucheka, 2013; Rwigema & Karungu, 1999) however the current literature does not necessarily speak to the effectiveness of the government initiatives and programmes and how they aid the development of the township economies. The study shall provide recommendations on measures and policies that the government through DFIs should adopt and implement to accelerate and realise sustained economic growth.

### **1.7 Organization of the study**

The final mini dissertation will be organised into 5 (five) chapters. Chapter 1 (one) will outline the background information relating to the study followed by the research problem statement and questions. Within chapter One, the problem statement is superseded by the research objectives. In chapter 2 (two), the research study identifies and focuses on the extensive review of relevant academic literature that aligns to the research topic. Chapter 3 (three) demonstrates the method followed in acquiring the data. This section unpacks the research approach and the research design. Chapter 4 (four) derives conclusions from the data analysis and provides

interpretation of the results. The findings of the research are discussed and interpreted in terms of the research questions. Chapter 5 (five) summarises the research study and provide recommendations for future research.

## **Chapter 2**

### **Literature Review**

#### **2.1 Introduction**

In this section, the focus is on the review of related literature from previous studies on the subject matter. The section starts by introducing definitions and key concepts around of SMMEs, Informal economy, and DFIs and their impacts on economic growth. We will then review relevant empirical literature underlining the research problem pertaining to the role of DFIs and government agencies and their effectiveness in developing SMMEs including township economies. The chapter concludes with an overview of discussions of the literature review, gaps identified, the findings of the literature review and the purpose of the study.

#### **2.2 Definitions of Concepts**

##### **2.2.1 SMMEs**

It has become clear that the success of SMMEs in South Africa has a notably positive effect on the sustainable growth on the economy of the country. The research conducted by (Van Scheers, 2016) concludes that there is a link between the economic growth of the country and the success of SMMEs in South Africa. Over the past decades, government has also realised that the economic growth of the country will no longer come from big businesses and corporates but rather from the developing and supporting of SMMEs through intentional policies that encourage development in this sector. The success of SMME in South Africa gives hope to the unemployment issues and economic problems faced. According to Bowler, Dawood, and Page (2013), 80% of all new jobs are created by SMMEs and 70% of all South Africans are employed by the small business sector. In previous studies (Abor & Quartey, 2010), it has been noted that the global impact of development programmes designed by governments and their agencies has been less than satisfactory with noted successes in other countries such as Estonia. (Smallbone, David; Welter, 1987). Agupusi, (2007) recognises that since the rule of the democratic regime, South Africa has been promoting SMME as a catalyst to economic growth and socio-economic integration. In a study (Agupusi, 2007) on small business development and poverty alleviation in Alexandra South Africa, the findings reveal a positive interaction between development agencies, and small businesses in Alexandra (a township in North Gauteng). It was noted that there are mainly informal and semi-formal SMMEs in Alexandra, and they could not only alleviate poverty but could also contribute to the general transformation

process. Research does confirm that SMME can contribute to the development of South Africa in many areas such as job creating, poverty alleviation, economic growth, and community development. Through job creation, they can assist in raising the standard of living of people residing in previously disadvantaged areas thus positively contributing to the economic growth agenda which is so much needed. (Aris (2007) further adds that the economic crisis in 1997 to 1998 has taught us that countries cannot be overly dependent on FDI to stimulate economic development. At the time of the crisis many investors withdrew their funds or investments and opted to rather re-allocate them to other destination which are far more profitable. This trend was also observed with the health crisis in 2019/2020. SMME participation in the economy is a way to generate more stable, less fickle, domestic led investments.

SMMEs are diverse in nature and operate in different industries, including retail, wholesale, tourism, mining, farming, manufacturing, construction and service (Chimucheka, 2013). Globally, the idea of small business has many varieties and interpretations, the definition largely depends on the level of each country's economic development. The lack of a clear and comparable definition of small business can affect research findings and the understanding of its contribution to socio-economic development (Agupusi, 2007). As a result of that, what defines the size of a small entity in one country varies extensively compared to another. In developed countries such as the USA, businesses with fewer than 500 employees are considered small businesses, so it is all relative. According to the National Small Business "NSB", SMMEs in a South African perspective are classified into five groups: 1) survivalist enterprises, 2) micro enterprises, 3) very small enterprises, d) small enterprises and 5) medium enterprises. The survivalist is generally providing income below the poverty line. The NSB Act 102 of 1996 defines small business as a separate entity that can be within any sector or sub-sector of the economy and which can be classified as a micro-enterprise, a very small enterprise, a small enterprise, or a medium enterprise. The NSB Amendment Acts of 2003 and 2004 further define an SMME as a distinct business entity managed by one or more persons which must meet certain specified criteria (National Small Business Act, 1996). The NSB is a regulatory and support framework for SMMEs. Table 1 displays definitions of SMMEs as per the NSB Act of South Africa.

Table 1 Schedule of definitions of SMMEs

**SCHEDULE**

(See definition of "small business" in section 1)

Column 1	Column 2	Column 3	Column 4	Column 5
Sector or sub-sectors in accordance with the Standard Industrial Classification	Size or class	Total full-time equivalent of paid employees	Total annual turnover	Total gross asset value (fixed property excluded)
		Less than	Less than	Less than
Agriculture	Medium	100	R 4.00 m	R 4.00 m
	Small	50	R 2.00 m	R 2.00 m
	Very small	10	R 0.40 m	R 0.40 m
	Micro	5	R 0.15 m	R 0.10 m
Mining and Quarrying	Medium	200	R30.00 m	R18.00 m
	Small	50	R 7.50 m	R 4.50 m
	Very small	20	R 3.00 m	R 1.80 m
	Micro	5	R 0.15 m	R 0.10 m
Manufacturing	Medium	200	R40.00 m	R15.00 m
	Small	50	R10.00 m	R 3.75 m
	Very small	20	R 4.00 m	R 1.50 m
	Micro	5	R 0.15 m	R 0.10 m
Electricity, Gas and Water	Medium	200	R40.00 m	R15.00 m
	Small	50	R10.00 m	R 3.75 m
	Very small	20	R 4.00 m	R 1.50 m
	Micro	5	R 0.15 m	R 0.10 m
Construction	Medium	200	R20.00 m	R 4.00 m
	Small	50	R 5.00 m	R 1.00 m
	Very small	20	R 2.00 m	R 0.40 m
	Micro	5	R 0.15 m	R 0.10 m
Retail and Motor Trade and Repair Services	Medium	100	R30.00 m	R 5.00 m
	Small	50	R15.00 m	R 2.50 m
	Very small	10	R 3.00 m	R 0.50 m
	Micro	5	R 0.15 m	R 0.10 m
Wholesale Trade, Commercial Agents and Allied Services	Medium	100	R50.00 m	R 8.00 m
	Small	50	R25.00 m	R 4.00 m
	Very small	10	R 5.00 m	R 0.50 m
	Micro	5	R 0.15 m	R 0.10 m
Catering, Accommodation and other Trade	Medium	100	R10.00 m	R 2.00 m
	Small	50	R 5.00 m	R 1.00 m
	Very small	10	R 1.00 m	R 0.20 m
	Micro	5	R 0.15 m	R 0.10 m
Transport, Storage and Communications	Medium	100	R20.00 m	R 5.00 m
	Small	50	R10.00 m	R 2.50 m
	Very small	10	R 2.00 m	R 0.50 m
	Micro	5	R 0.15 m	R 0.10 m
Finance and Business Services	Medium	100	R20.00 m	R 4.00 m
	Small	50	R10.00 m	R 2.00 m
	Very small	10	R 2.00 m	R 0.40 m
	Micro	5	R 0.15 m	R 0.10 m
Community, Social and Personal Services	Medium	100	R10.00 m	R 5.00 m
	Small	50	R 5.00 m	R 2.50 m
	Very small	10	R 1.00 m	R 0.50 m
	Micro	5	R 0.15 m	R 0.10 m

Source: Government Gazette, 15 March 2019

### **2.2.2 Informal economy**

There have been various terms and definitions given to the informal economy. Ferman & Ferman (1973), it is referred to as an irregular economy. There is still confusion in what is considered an informal economy or sector however the International Conference of Labour Statisticians “ICLS” approved two distinct definitions which are enterprise based and worker based. The enterprise based definitions defines of an informal sector as production and employment that takes place in an un-incorporated, small and unregistered enterprises (Pillay et al., 2018). The worker-based definition refers to three kinds of workers according to the ICLS (i) workers that are not covered or are insufficiently covered by formal arrangement thought their work, including own account workers and employers in informal sector enterprises (ii) Employees who do not have labour rights such as not receiving social insurance through their job or the right to vacation or sick leave whether they work in informal or formal enterprises or households and (iii) Unpaid workers including family workers, own use producers, volunteers and trainees. The Women in Informal employment: Globalizing and Organizing “WIEGO” defines the informal economy as a diversified set of activities, jobs, enterprises, and workers that are not regulated or protected by the state. According to Investec in an article titled “the thriving township economy vital to South Africa’s economic revival”, an estimated 17% of total employment in South Africa is through the informal economy or so called ‘township economy’. In a country which classifies 35.3% of its population as unemployed, the informal sector creates a lifeline for those who lack formal employment. According to Stats SA, while the informal economy does not contribute to the fiscus directly through tax collection, it provides employment and income to approximately 2.5mil workers which excludes the agricultural sector, which presents 17% employment. 6% of the informal economy does however contribute to GDP.

Informal economies operate within several industries and mostly offer good and services that meet social and economic need of people living in the township. The retail sector dominates in the informal economy with spaza shops, fast food outlets, shebeens/shisanyamas, bakeries and hawkers. There are other businesses such as backroom rentals, taxi operators, mechanics, creches and hair salons amongst others.

### **2.2.3 DFIs**

The OECD defines the national and international development finance institutions (DFIs) as specialised development banks or subsidiaries created to support private sector development in developing countries. They are usually majority-owned by national governments and source their capital from national or international development funds or benefit from government guarantees. DFIs in South Africa are not a new concept, they have been an integral part of the apartheid racially based industrialisation. During apartheid, the impact of international isolation and sanctions forced the state to aggressively intervene in the economy of the country through DFIs (Khadiagala, 2015). Post-apartheid, the DFI have repurposed and have become a “niche” for financing development objectives to correct inequities caused by the apartheid regimes and mandates surpassing correcting market failures. DFIs have come to characterize their ability to address more broadly the national development failure and their potential to promote SMME development. The ability to direct financial as well as non-financial technical support towards catalysing business creation proves to be important drivers for economic revitalization and employment creation which is key to the South Africa growth agenda (de Jongh et al., 2020).

DFI mandated are based on three principles (i) where DFIs are active in sectors and activities that are difficult for private sectors capital sources to address (ii) as catalysts for accelerated industrialising, job creation, economic growth, and human capital development and (iii) being anchors of sustainability for bridging investment gap (Pere, 2021). In total there are sixteen DFIs equally split between national and provincial levels and they serve the disadvantaged and economically marginal sections of the population by improving access to financial services, supporting job creating, small business development and industrial and infrastructure development (Pere, 2021). Majority of individuals in the country has no credit access from commercial banks with only very few privileged individuals having access to formal financial institutions. There is a disproportional gap between the rich and poor in which relates to access to capital, educational opportunities, access to healthcare, and infrastructure gabs such as transportation, energy, and access to clean water.

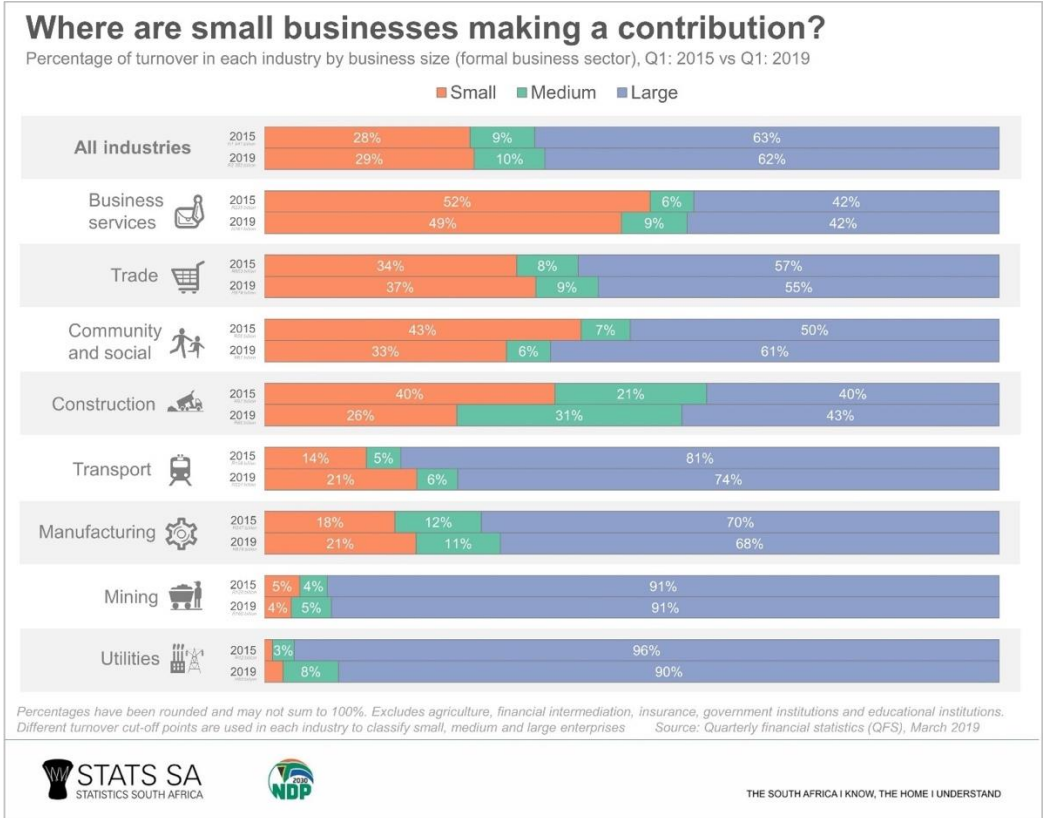
## **2.3 Overview of context stylized facts**

### **2.3.1 Overview of township economies (include SMEs) in South Africa**

According to Statistic SA, the formal business sector which includes private businesses and public companies however excludes agriculture, financial intermediation, insurance companies, government departments and educational institution generated R2,39 trillion in revenue in quarter 1: 2019. Out of this amount, large businesses contributed 62%, followed by small (29%)

and medium sized businesses (10%). It is quite clear that small businesses which are characterised by large numbers of small players have far greater potential to the growth agenda of the country. (Bowmaker-Falconer & Herrington, 2020) in the GEM SA report for 2019, agrees that the government critically and progressively acknowledges the importance of SMMEs in achieving sustainable and inclusive economic growth. The government realises the need to support this goal through setting up development institutions and policy reforms.

Figure 1 Small Business Contribution



Source : <https://www.statssa.gov.za/?p=12264>

2.3.2 The role of township SMMEs in the economy

Unemployment is seen to be the root of all crimes, poverty and the biggest impediment to the economic growth that is so needed. The fact that there is high unemployment in the townships, begs for us to understand what the true potential of the SMME investment is in these locations. And, whether government support is aiding the development which will ultimately make progress in the economic growth as measured by impact to GDP. The township SMME economy before 1994 was not included in any government policies because the townships were

disregarded by the then apartheid government. According to (Bvuma & Marnewick, 2020) many of the South African's township areas are below the basic standard of living and remain in poverty due to lack of basic infrastructure and lagging economic growth and development. The apartheid system left South African with a spatial divergence between the economic centres of the country. Before 1994, the government intentionally suppressed and marginalised black businessmen and businesswomen. At the core of the NGP is a solid growth plan for the investment in infrastructure and the identification of viable and sustainable opportunities specifically earmarked for historically disadvantaged areas (NGP, 2009).

Townships economies have great potential to contribute positively to the South African economy at the back of support given by the government and its agencies. (Bvuma & Marnewick, 2020) in Gauteng province alone, the SMME segment has created about 150,000 jobs in a single year, and this was as a direct result of government's support. It is therefore clear that the township economies must receive necessary interventions and support by DFIs and government agencies to address many of the challenges faced. This has been the prerogative of the movement for the past few decades, as the economy depends on the success of township businesses.

Township enterprises have very important economic and social importance to the communities in which they serve (Department of Economic Development, 2014). The below example demonstrates the self-serving nature of these economies:

- a) Minibus taxis, in the absence of the adequate public transport system as part of the inadequate infrastructure development of the country, the taxi business plays a very critical role in daily commuting of millions of townships working class to and from work, to visit family members and general shopping routines at cheap rates and employing more than 70,000 people in Gauteng alone.
- b) Spaza shops - This is a R7 billion business that has played a role of a micro convenient grocery store providing necessities to township residents within a walking distance from where they live. In the last decade or so, these businesses have been threatened by an influx of large retailers in the townships (e.g., Pick in Pay and Shoprite).
- c) In response to the need for decent and dignified funeral, thousands of burial societies were born to provide an informal funeral insurance cover at affordable rate - to an estimated 12.5 million members and their dependents. This economic activity is valued at R25 billion; and

d) Stokvels – These are traditional rotating schemes that have played a role in funding education of black children and providing credit to township entrepreneurs.

Table 2 Different clusters in township business

Sectors	Clusters				
<b>Retail</b>	Butcheries	Spaza shops	Fish and Chips	Fruit & vegetable stalls	General dealers
<b>Service Industry</b>	Hair Salons	Shebeens	Shisanyama	Security companies	Gym
	Sewing and Tailoring, including shoemakers	Sanitation (plumbers)	Mobile toilets	Car wash	Burial society
<b>Construction and real estate</b>	Brick Laying/manufacturing	Construction business	Property development	Renting	
<b>Tourism</b>	Tourism guide and logistics	Bed and Breakfast	Restaurants	Catering and events	Shisanyama
	Water sports and recreation parks	Heritage tourism	conferencing	Sports Tourism	Tour operators
<b>Manufacturing</b>	Clothing and textile	Auto body repairs and maintenance Auto mechanics	Furniture manufacturing	Steel production	Tar and Oil production
<b>Transport</b>	Automotive cooperatives	Minibus taxi ownership	Logistics companies	Taxi Associations and opening new lines to Johannesburg	Tour operator
<b>Agriculture and agro procession</b>	Olive oil for fuel	Biofuel	Milling	Poultry retail	Vegetable production
<b>Finance</b>	Stokvels	Mashonisa money/lending schemes	Burial societies		
<b>Creative Industry</b>	Arts and craft Cinemas	Music and entertainment	Fashion design Bead making	Music and video production	Coordination of cultural events
	Jewelry design and manufacturing				
<b>Government and community services</b>	Childcare and early development centers Care for elderly Feeding schemes (supply bread for schools' hospitals)	Clothes for school and police uniforms Furniture for office space	Facilitation of social grants agents	War on drugs	HIV/AIRDS and other chronic
<b>ICTS</b>	Internet solutions in townships	Multimedia service centers	Technology application design	Electronic Repairs	ICT Recycling
<b>Green Economy</b>	Waste Management	Recycling	Coal and wood making		

Source: (Department of Economic Development, 2014)

According to the (Department of Economic Development, 2014), the Township Economy Revitalisation Strategy builds on existing government support programmes and responds to the challenges faced by township enterprises both common and specific issues. The strategic goal is to remove these barriers to achieve three key outcomes as outlined: (1) Create an enabling and supporting environment based on the strategic focus areas (below) for township economy revitalisation, (2) the establishment of social and economic value of township economy, and (3) to ensure that the township enterprises/businesses become major players in the Gauteng economy.

*Table 3: Summarised Township Economic Revitalisation Strategy by GPG*

<b>Key Focus Areas</b>	<b>Brief Definition</b>
Making sure that there is appropriate regulatory and legal framework.	The government seeks to review and revise the regulatory and legal framework so not to hinder the development and growth. This focuses on provincial and municipal regulations which place both a time and monetary burden on small businesses and may therefore potentially discourage informal businesses from growing and registering as formal businesses.
Advancing manufacturing and productive activities.	This focus area provides training, project support and technical assistance businesses to businesses in the township who play a role manufacturing sector, as a result will increase the level of local content in the market and thus decreasing the dominant position of larger and established suppliers.
Supporting the Infrastructure in enterprise development.	The strategy is for the provision of various specialized economic infrastructure for the township economy. This will reduce the cost of doing business and promotes linkages and co-operation between township businesses.
Promoting development of entrepreneurs in the township.	Focuses on the expansion of training and workplace programs in townships, this will increase the total number of entrepreneurs and employment opportunities in the township economy
Ensuring Access to Financial Markets.	The use of government procurement as a mechanism to promote the growth or establishment of township firms, as well as the possible role of community marketplaces and clusters in fortifying relationships between producers and sellers both inside and outside the township economy.
Promoting entrepreneurship development in the township.	Addresses the challenges experienced by township businesses in accessing external finance and the need to bring additional and new forms of finance into the Township Economy. Specifically, the strategy identifies the need to re-capitalize and strengthen the Gauteng Enterprise Propeller (GEP); possible investigations in the

	establishment of a state-owned bank; Township Economy Bond or Solidarity Fund; and develop and formalise co-operative banks and insurance enterprises.
Promotion of Innovation and Knowledge Systems.	This is to facilitate innovation, protect knowledge and improve the commercialization of products under development will result in more successful enterprises in townships.
Understanding the Economic and Social Value chains of the Township Economy	The focus will be on building research, data, and information systems to understand the township economy better and to increase the scale of interventions and to make sure the economic actors in the township are recognized.

**Source:** TER Strategy: Mid-Term Implementation Evaluation report (2016:3)

### 2.3.3 Overview of DFIs in South African and their role

Giordano & Ruiters (2016) in their study further notes that DFIs play a crucial role in overcoming and fixing market failures by bridging the gap between private and public finance. An example of a market failure could be the issue of access to funding which is a key barrier or constraint to entrepreneurs. Giordano & Ruiters (2016) further support that DFI are better placed to support SMMEs due to their lack of and/or poor ratings and their inability to collateralise their exposures which is a prerequisite for lending in the formal sector. Bongomin et al., (2017) supports that access to finance and growth of SMME have a positive relationship. They add that there is a positive and significant moderating effect of financial literacy between access to finance and SMME growth particular in developing economies. This support that financial and non-financial support as suggested by government are both important however their effectiveness remains questionable. Smallbone, David; Welter, (1987) suggest that there are many small businesses that are set up, survive, and grow without the support of government. This is solely due to the individual running the business who reflects their own creativity in mobilising resources. The problem with these situations is that the businesses remain small and their contribution to economic development in terms of creating employment is rather limited. A summary of their evidence suggests that priorities for governments vary according to the stage of market reform reached. In countries that are still in the early stages, the priority need is for a recognition of the part of the state of the important roles SMMEs play in developing the economy. The steps include reviewing basic reforms such as reviewing the registration process, the tax systems etc but is also includes a step to eliminate corruption. From this study of (Smallbone, David; Welter, 1987), we can see that South Africa is still in a transition stage and

in its early stages of development as evidenced by the same objectives of the NGP. Agupusi, (2007) purports that the government through the DTI established two agencies specifically mandated for the development of SMME which are SEDA and Khula. The agencies have a range of programmes for start-ups and existing businesses. There was however a large gap identified in the micro-SME space, and in responds to that, SAMAF was brought about in 2004. SAMAF sits within Khula, and its mandate is to provide financial support for micro businesses. SAMAF focus mainly on micro business owners in the rural areas and township communities. Other DFI and government agencies that support SMME are NEF, IDC and the GEP.

*Table 4: Government DFIs supporting small business.*

<b>Institutions</b>	<b>Activities</b>
<b>SEFA</b>	Through a combination of direct and wholesale financing channels, SEFA offers financial services and products to cooperatives and SMMEs that meet the eligibility requirements. SEFA works to reduce poverty, create jobs, and stimulate the economy by supporting the founding, expansion, and success of SMMEs and cooperatives.
<b>SEDA</b>	SEDA offers a range of business development services. It provides non-financial services through integrated support agencies across the nation with more than 284 Enterprise Information Centres in the municipalities across the nation.
<b>KHULA Enterprises</b>	Khula facilitates access to finance for small businesses. It has various financing products and works with major commercial banks and private organisations such as Business Partners. Khula’s operations involve loans and credit guarantees through commercial banks. It also offers a mentorship programme.
<b>National Empowerment fund (NEF)</b>	NEF provides various start-ups for small businesses and rural and community transformation. Its financing capacity ranges from R250,000 to R10m. NEF focuses specifically on disadvantaged individuals
<b>Industrial Development Corporation (IDC)</b>	IDC generates its funds independently of the government. It provides various sector-focused financing products ranging from R1m, with specific focus on SMEs and empowerment.
<b>South Africa Micro Finance Apex Fund (SAMAF)</b>	SAMAF is modelled on the Grameen Bank in Bangladesh. It provides loans of up to R10,000 to micro and survivalist enterprises in poor areas. Its focus is poverty alleviation.
<b>Gauteng Enterprise Propeller (GEP)</b>	The GEP is a Gauteng Provincial Government (GPG) agency established under the auspices of the Department for Economic Development to provide non-financial and financial support and to co-ordinate stakeholders for the benefit of SMMEs in Gauteng.

Source: (Agupusi, 2007)

The NGP framework has “Ten programmes to control inflationary pressures and inefficiencies combined with more proactive strategies to support an inclusive economy, social equity and

regional development” (NGP, 2009). Programme five of the NGP, involves promoting small business and entrepreneurship with the aim of abolishing unnecessary red tape. One of the core elements of this programme is to design what is called a “one-stop shop” and single funding agency for SMMEs through the consolidation of Khula, SAMAF and IDC funding amongst others. The plan is to improve access to funding and reduce the overhead costs to make more resources available to the SMMEs (NGP, 2009). Additionally, programme five aims to strengthen access to micro-finance for SMME to bring more South Africans into economic activities thus widening the pool and promoting growth.

*Table 5: Other South African DFIs Establishment*

<b>Name</b>	<b>Abbreviation</b>	<b>Year established</b>
Development Bank of South Africa	DBSA	1983
Land and Agricultural Development Bank of South Africa	LADBSA/Land bank	1912
National Housing Finance Corporation	NHFC	1996
Independent Development Trust	IDT	
National Youth Development Agency	NYDA	
National Urban Reconstruction and Housing Agency	Nurcha	1996
Rural Housing Loan Fund	RHLF	2006
Micro Agriculture Finance Scheme of South Africa	Mafisa	2004

Source: [www.gcis.gov.za](http://www.gcis.gov.za)

These DFI hold varying mandates and they have increased their scope over time to invest not only in South Africa but have become regional players on the continent while mainly capital distributors in mainly in South Africa.

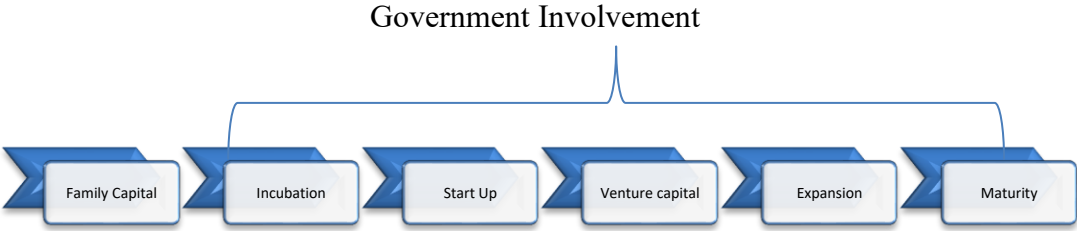
**2.4 Conceptual framework: DFIs, economic growth and township economies**

Mazzucato & Penna (2016) developed a typological framework for the roles of SIBs in the economy. We will refer to State Investment Banks “SIBs” as DFIs interchangeably. The paper identifies four different roles of DFIs in the typology namely: Venture capitalist (New venture support role), Countercyclical, Capital development and Challenge-led roles. While DFIs are not a new phenomenon, they have diversified their roles beyond traditional activities of yester years. Mazzucato & Penna (2016) argue that the roles of DFIs is not to fix market failure as

economist put it in the Market Failure Theory “MFT”. SBIs are not just market failure fixers, they are policy and political tools used to direct resources to strategic and priority areas to drive economic growth and development. The MFT uses the First Fundamental Theorem “FFT” of welfare economics as a starting point (Arrow 1951; Debreu 1959). The FFT states that markets are most efficient allocators of resources under three conditions which are (1) there is a market with supply and demand of goods and services that is traded at publicly known prices (2) consumers and producers behave competitively and (3) there is equilibrium in the market. With this condition, the market allocates resources, and no other allocation will be better off without making another worse off. MFT though occurs when condition (1) and or (2) are violated, this is also referred to as an inefficient market. Market failure is not the only condition for government intervention but is a necessary one.

Out of the four roles (Challenge-led role, Venture capital, Developmental and Countercyclical roles of development banks by Mazzucato and Penna (2016)), the one relevant to this study is the new venture support developmental role of DFIs, the “Venture capitalist” in the typology. New venture investment such as SMMEs have been the focus of DFIs since the 1950s however these activities have been intensified recently especially around innovation (Griffith-Jones and Tyson 2013; Mazzucato and Penna 2015). It is well known that SMMEs face unique challenges which include the constraint to find external funding due to lack of security or collateral required by the traditional financiers, poor record keeping, lack of information, to mention just a few. In industrialised economies, the DFI are critical to assist SMMEs in closing the funding gap. The MFT justification of the new venture support or venture capitalist role is therefore in this instance related to market inefficiencies at the micro level. According to (Mazzucato & Penna, 2016) these information failures arising from incomplete markets with high transaction costs and information asymmetries, in a form of unavailability of public information to determine who is a bad borrower versus who is a good one which leads to issues such as adverse selection or moral hazard behaviours. Such market failures create inefficiencies associated with non-equilibrium situations that result from the interaction between agents (microeconomic exchanges). For example, microeconomic Pareto inefficiencies may be caused by information asymmetries that lead to adverse selection of potentially good borrowers (Stiglitz and Weiss 1981); or they may be the result of high costs to carry out a transaction through markets (Coase 1960). The classic example is the lack of finance/funding for small enterprises and start-ups, which usually lack a track record of good borrowing behaviour and are unable to offer guarantees for debt contracts.

Figure 2 Venture Capital Life Cycle



Another notion that is required to better understand the past and present dynamics of South Africa’s segmented, multi-layered economy and the place where the township economy fall within this arena. The basis for such a concept lies in two closely related ideas (Mahajan Sandeep, 2014): First, theoretical, and empirical analyses show that accelerated growth in the urban informal economy (in South Africa this would be the ‘the township economy’,) is fully consistent with growth in the urban formal sector. There is nothing inevitable about the prospect, as some have advanced, that the township economy could wither away under the shadows of the formal advanced economy (Mahajan Sandeep, 2014).

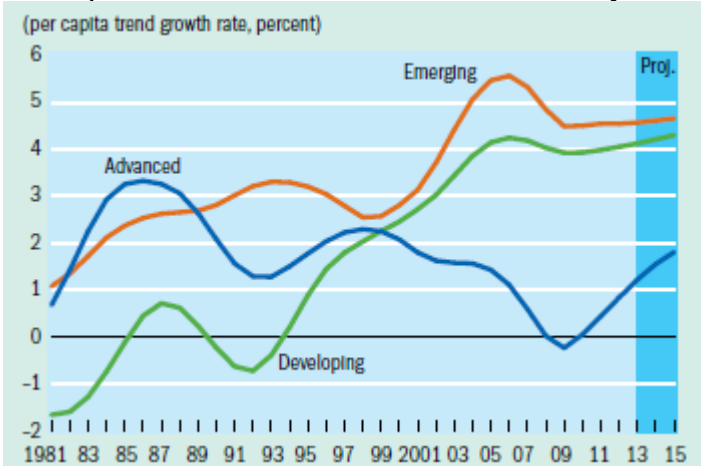
Second, developed economies don’t grow fast; it is the lagging underdeveloped economies that do. Therefore, the township economy not only can play very much alongside the urban formal economy but also can potentially become an important driver of economic growth given the lag.

Idea 1: Role of the ‘informal economy’ township economy in relation the urban formal economy. A viable and strong township economy ‘informal economy’ is no longer just a theoretical dream, but it has become an empirical reality. The relative size of the informal economy is persistency even during GDP growth. A 2009 OECD study concludes that the ideal of Informality is increasingly becoming normal, not only in middle and high-income countries but similar patterns in the development in Southeast Asia and Latin America: over the last 30 years, growth in these countries was followed by growth in the informal economy (Jütting and Laiglesia 2009).

Idea 2: the phenomena that by starting from a low base of income and production is an advance of its economic growth potential is called economic convergences. Empirically it has been found to be valid in the experience of well-integrated economies in Europe. South Africa’s economic growth potential could be significantly enhanced if it able to create its own version of a convergence machine within—one that would enable rapid growth of the township economy by releasing its own internal economic dynamics and by integrating it in meaningful ways with the modern urban economy. (Mahajan Sandeep, 2014). The so-called catch-up strategy would involve budding on the comparative advantages of township economy being unskilled labour, land space that is far more affordable that the city and a market of clients currently untapped.

Figure 3 Sustained Difference

Emerging and developing economies enjoying faster and long run trend growth versus developed countries since the turn of the century



Source: Author’s calculation based on data from the IMF’s April 2012 World Economic Outlook

**2.4.2 Instruments used by DFIs in supporting SMMEs.**

There are many theories identified by researchers that attempt to explore the topic on the development of entrepreneurship. Simpeh (2011) examines six entrepreneurship theories that underline the studies. The six theories relate to (i) Economic theory, (ii) Psychological theory (iii) Sociological theory (iv) Anthropological theory, (v) Opportunity-based theory and (vi) the resource-based entrepreneurship theory. The resource-based theory of entrepreneurship relates to the ability of an entrepreneur to access resources as being the driving force for opportunities and the growth of new endeavours (Alvarez, Sharon A; Busenitz, 2001) This supports the

notion that resources enable entrepreneurs to exploit opportunities. Simpoh (2011) financial capital/liquidity, social capital or human capital are theories entered under the resources-based entrepreneurship theories. These theories underline the concept of DFIs. This has fuelled academic researchers' interest in establishing the relationship between firm-based resources and the performance of businesses in entrepreneurship. Entrepreneurial opportunities exist in most instances because different agents have different beliefs about the relative value of resources when they are converted from inputs into outputs (Schumpeter, 1934; Kirzner, 1979; Shane & Venkataraman, 2000).

The market failures mentioned in the theories as well the challenges faced by MSMEs which include access to funding which has a bias to larger, more established firms creates a role for DFI's. DFI play a critical role in financing small enterprises (Khadiagala, 2015). The big part of DFI is actually a policy tool in the hands of government to foster developmental objection and addressing imperfection in the market for finance, investment capital, economic growth and contribution to public goods (Khadiagala, 2015). Micro financing institution play a key role in financing small enterprises. Micro finance is defined as providing financial services to a market that is generally excluded from the traditional financial system due to their low economic status. Their services include small loans, savings, and micro services (Akinadewo, 2020).

DFIs fall within four categories which include (i) Financial intermediation (2) Social intermediation (3) Enterprise development and (4) Social services (Abor, 2016).

Financial intermediation is deemed to be the primary focus of DFI's; as indicated previously the products and services that mainly include micro-savings, credit, payment systems and insurance (Abor, 2016).

Social intermediation is important to be able to achieve the first which is sustainable financial intermediation. Generally subsidized by donor agencies, this intermediary includes building human and social capital of the DFI's employees to ensure effective supply-side service delivery. This includes services such as group formation and leadership training (Abor, 2016). Enterprise development services is the non-financial services that exist to support the clientele in skills development, business planning, technology, and the likes (Abor, 2016). These training resources are usually dependant on the client's willingness to fund – or ability to gain funding for these additional services. Similarly, social services are non-financial services that promote MSME training (Abor, 2016), the difference being that these services focus on promoting the

welfare of the poorer spectrum of clientele and micro-enterprises. Examples of such training include education, health, and literacy training. Like social intermediation, this type of service usually requires continuous government subsidies and/or donor-supporting NGO assistance (Abor, 2016).

There would be instances when the micro-finance institutions (MFIs) given non-financial services in addition to their standard mandated products and services, this is commonly referred to or known as an integrated lending model (Orbuch, 2011). Another model which is used by DFIs is what is called the group-lending model. This requires customers and clients to apply for facilities whether credit or otherwise in voluntarily formed groups (Kodongo & Kendi, 2013). Regarding what is known as social collateral, the members are required to elect the co-debtors they want to be in their group (Abor, 2016). This approach increases risk appetite for lending and improves creditworthiness according to lenders. The two issues that get mitigated included information asymmetry and the adverse selection problem (Armendariz and Morduch, 2010). At the same time, it uses peer pressure to ensure repayments and obligations are upheld, due to joint liability (Madajewicz, 2011).

Other products and services that protect DFIs from the inherent risk associated with their clients include graduated loan schemes, frequent collection of loan instalments, compulsory savings, and use of guarantors (Abor, 2016). With varying opinions on the usefulness of these tools, it is imperative to investigate which specific DFI funding mechanisms lead to positive outcomes in a township context.

## **2.5 Empirical Literature**

There is a plethora of literature that is dedicated to exploring development and support of SMMEs in developed and developing countries. This section will also explore literatures pertaining to economic and developmental impacts that DFIs have on projects and how this has a knock-on effect on the broader communities. We also explore related studies done linking DFIs and economic growth in other countries as well as literature on the relationship of development initiatives on growth on SMMEs.

### **2.5.1 Development and Growth of SMMEs**

A case study of the IFC on how Development Finance Institution support SMMEs reveals that through the provision of funds, advisory services and capital raising, DFIs contribute significantly to growth of SMMEs (Gyimah & Agyeman, 2019). However, even with efforts by government globally to improve and strengthen the contribution of SMMEs in economies

of the world, they still face many challenges especially in Africa. According to the African Development bank, more than 70% of SMMEs don't have access to medium to long term financing which results in a funding gap of USD140bn in Africa alone (Gyimah & Agyeman, 2019). The study by (Gyimah & Agyeman, 2019) reveals that DFIs contribute significantly to the growth of SMMEs though they face systemic and non-systemic challenges. Emanating from this study are findings of the kind of assistance DFIs offer. They offer fund management, advisory project management, on lending services and leasing to governments, financial institutions, and businesses amongst others. DFIs also impact SME growth through the indirect influencing of policies and legislature. In this study it was found that DFIs must aim to tailor global products to suit the local market needs as much as possible. They must also caution the danger to crowd out other private players in their endeavours to create the much-needed economic growth.

By supporting SMMEs, there is better economic growth, increased employment opportunities, increase in taxes (government revenue), technological advancement which are some of the benefits that come with a solid and successful SMMEs sector around the world today (Adewale & Olalekan, 2016). Access to finance (due to credit risk appetite) or the lack thereof, has been identified as one of the major constraints to SMEs development (Nichter & Goldmark, 2009), this is where DFIs have taken some of the perceived risk on SMMEs from lending institutions and aided growth opportunities.

In a study on Development Financial Institution and Small Medium Enterprises Development on Osun State in Nigeria, (Adewale & Olalekan, 2016), identified that the ability to access to finance is one of the key factors that are associated with low growth amongst small business particularly in developing countries in Africa. The challenges as discussed in the paper to adhere to formal financial institution risk appetite standards has hampered position expansion opportunities and development opportunities for SMMEs. SMME are left with no other choice but to borrow funds from friends, family members and associates to aid the financing gap. The study concludes with the fact that from a Nigerian SMMEs perspective, they have not been able to drive the economy mainly due to this funding conundrum. In the research, it was found that unemployment issues persist in the economy mainly due to their poor performance due to their inability to grow and expand their business operations. The Nigerian state remained underdeveloped, the DFIs seem to be inactive as entrepreneurs are not aware of their existence

and those that did thought the interest rates offered by DFIs are high and as a result have not met their needs.

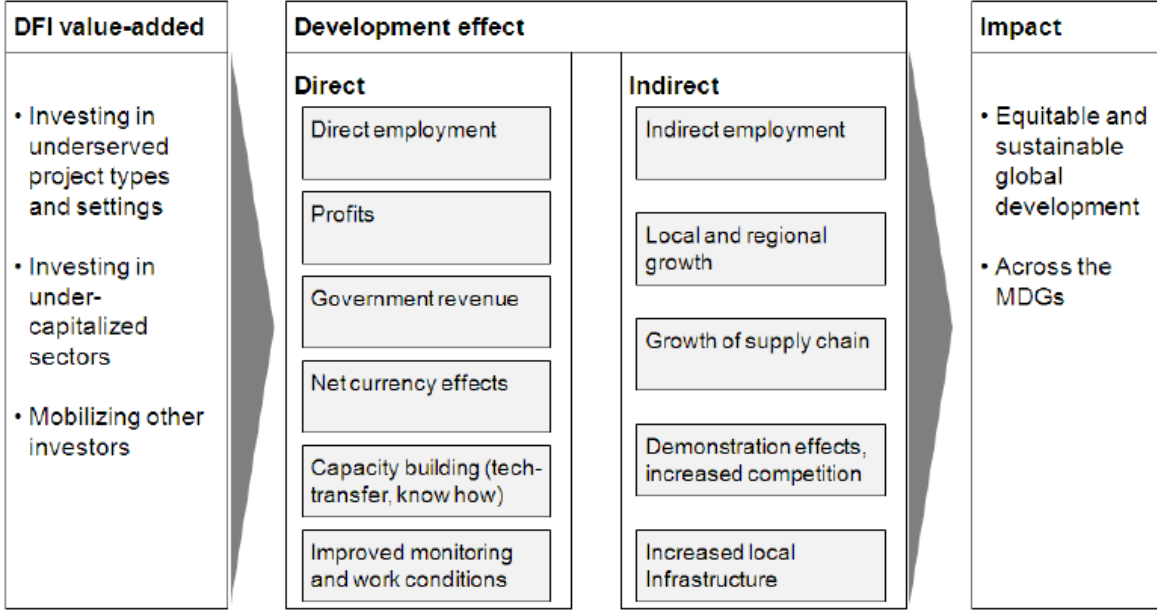
R. Atieno (2001) in his empirical study on the, role of institutional lending policies among formal and informal credit financial institutions in determining the access of small-scale enterprises to credit, used structured questionnaire and primary data was collected via a field survey where a total of 334 enterprises were interviewed. The results and finding indicated that there was rationing behaviour demonstrated by financial institution both formal and informal as demonstrated by the limited use of credit (low supply of credit). The study concludes that established financial institutions can improve lending terms and conditional to favour SMME's and this can form an avenue for credit lending in this space.

Akingunola (2011) in the study of the assessment of Financing Options for the growth of SMEs in Nigeria used the Spearman's Rho correlation test to determine the relationship between SMMEs, and investment level, which outlined a significant Rho value of 0.643 at 10%. The findings show that there is materially positive relationship between SMEs economic growth and financing in Nigeria. The research conducted also suggests that availability of relatively lower interest rates should be provided to SMEs in Nigeria to boost economic growth.

### **2.5.2 Economic and development impacts of DFIs**

Dalberg (2009) DFIs have a direct effect on the project but also indirectly in the communities they serve particularly in developing countries. Key impacts as depicted in table 5 includes job creation, the profits from the project itself, revenue for governments. The broader community also benefits from the impact because of improved working conditions and environment standards.

Table 6 DFIs direct and indirect development effect



Source: Swedifund (2008) “New thinking new markets – Sustainable report 2008”; Norfund (2008) “Creates value combats poverty – Contribution to development 2008”; Dalberg analysis

According to the EDFI (2009) the impact from their projects was measured based on indicators such as how much employment has the initiative created, how much profits were made by the projects, what are the government revenues and net currency effect were. The measurable impact from EDFI in 2008 was reported to be: 56,000 new direct jobs and 300,000 employed on EDFI projects. Indirect jobs of 1.4m through value chain (related to supplier and sub-contractors). Profits of Eur145m and about Eur2bn of government revenue generated with Net currency effect of Eur4.3bn. The research also confirmed non-financial impacts of EDFI. Direct effect was noted to be capacity building in a form of transfer of technology and know-how (Dalberg, 2009). This takes the form of training of staff and build skills amongst vulnerable groups such as women. There is also improved governance as DFI projects would adhere to strict governance and monitoring standards which most SMMEs lack.

**2.5.3 DFIs and Economic growth**

Economic growth is defined as an increase in the productive capacity of an economy by which the economy is capable of producing additional quantities of goods and services (Noel T Palmer, 2012). The standard of living is normally measured by the quantity of goods and services available to us so that economic growth is synonymous with an increase in the general

standard of living. Therefore, from wide literature researched on the best measure of economic growth is through GDP because it considers all economic output of a country whether sold domestically or internationally.

DFI through their mandated instruments which include debt, equity and quasi equity, de-risking mechanisms and grants are known to be catalysts of economic growth in developing countries. Massa (2011) sets on a task to contribute to current literature by analysing the extent of the impact of multilateral development finance institutions on economic growth. The paper considered different income categories of countries and grouped them in either “lower-income” or “higher-income” to measure if the growth levels with DFI inflows is consistent in these countries. The study used Generalized Method of Moments (GMM) for panel data analyses, to determine relationship between the investments of a selected sample of multilateral DFIs and economic growth. The study found that investment by multilateral DFIs plays a positive and significant role in fostering economic growth in recipient countries, and that their impact is stronger in lower-income countries than in higher-income countries. From the observations presented, the authors found that growth rate is experienced in low-income countries was 0.4% higher at 1.3% than that in high-income countries. Despite result not being uniform in most countries, depending on the stage of economic development, the econometric results confirm the role of DFIs fostering economic growth in countries. Furthermore, the author stretched their analysis to gain understanding into which economic sectors proved more relevant in for growth. In order of highest growth impact, the econometric results presented show that if DFIs direct their investments into infrastructure, the industrial sector, agriculture sector, respectively. With DFIs investment commitment to financial sector leading to negative economic growth

## **2.6 Understanding effectiveness of financial and non-financial support.**

To assess and understand effectiveness, one must define it and recognise what success looks like. McLeod and Atwell (1992) as cited in the research in (Murphy, (2013 p.322)) defined institutional effectiveness “as the condition of achieving the set goals by an institution and being able to verify the attainment of these goals with specific data that show the degree or quality of their attainment”. There are key factors that need to be unpacked by the statement above. From this literature we note that to measure “effectiveness”, one would need to have set a goal. In our case the goal of DFIs, and development agencies is that of development. The other factor (Murphy, 2013), it is crucial to know how attaining the set goal with be verified and what data points will indicate the degree or quality. The difficulty comes in that each DFI or government

institution would have its own way of verifying the set goal effectiveness. Some DFIs and government agencies are mandated to assist with only financial support, some give non-financial support to SMME and some a combination of both financial and non-financial support. (Klonowski, 2010) in his study of the effectiveness of government programmes in Poland had three conclusions relating to programmes, specifically in Poland. The first is the government programmes are poorly structured, fragmented, and untargeted. The second conclusion on the effectiveness of government programmes was that they do not meet the needs of the SMME sector and thus poorly used. Thirdly, he concludes that there appears to be a liquidity gap in financing the SMME sector. (Hallberg, 2000) in understanding the success of government interventions, the results have frequently been limited to measuring of program input or program output. The attempts to measure the impact are infrequently done and are full of problems relating to how to measure and methodology. (Hallberg, 2000) concludes that evaluating the impact of interventions on SMME performance against the backdrop of government support can benefit from using a logical framework that defines the programs objectives and links activities and inputs to outcomes and impacts. Figure 2 is a framework (Hallberg, 2000) using as an example a training program designed to help SMMEs adopt and use quality management systems.

Figure 4: Framework for training program measuring impact.



Source: the framework development by Oldsman (1998) to evaluate DDS programs in Mexico

(Alfred, 2011) on the future of institutional effectiveness confirms that “effectiveness is a complex, multifaceted construct with a myriad of meanings and interpretations”. Alfred (2011) mentions two basic constructs that usually serve as a foundation to effectiveness which are constituted by a numerator (growth and resources) and a denominator (outputs). Growth, is defined in the oxford dictionary as the process of increasing in size. Alfred (2011) uses the example of rising enrolments, increasing revenue and anything that can be counted to illustrate growth. This can be used to gauge effectiveness if one is looking for simple evidence of success. Outputs on the contrarily are more complicated, they are results and are not easily calculated nor are the numbers measuring them easily understood. Alfred (2011) mentions that while effectiveness models in colleges today focus primarily on outputs, leaders and staff working in a world of enrolments and resources focus on growth. What this suggests is that for leaders, the bigger return on investment may come from working with the numerator rather than measuring the denominator.

## **2.7 Summary of Literature**

This chapter reviewed literature on SMMEs by providing definitions from various literatures and particularly from a South African perspective. The literature review section also discussed the role of DFIs and government agencies in the development of SMMEs. The chapter then discussed effectiveness theories from the literature review. Although the literature is not necessarily similar or identical particularly referencing to “townships”. The literature does help to see how reforms and government interventions do support SMME in general. There seems to be very little evidence from research which supports the effectiveness of DFIs and government agencies in support and development of SMME in the townships.

## **Chapter 3**

### **Methodology**

#### **3.1 Introduction**

This chapter defines the research method and research approach used in the final mini dissertation. It also gives an idea of the target population of the study, the unit of analysis, the sampling methodology and size, the tools, and instruments to be used in the data gathering process. It is also important to point out possible limitation of the study and ways to mitigate.

#### **3.2 Research Approach**

The nature of this study is exploratory to gain familiarity into the role and effectiveness of DFIs in developing SMMEs in the township. Saunders, M., Lewis, P. and Thornhill, A. (2012) in their paper define exploratory research as one that aims to seek new insights, ask new questions and to access topics in a new light. Lack of comprehensive data on SMMEs particularly in township enterprises is a significant challenge when researching and studying small businesses in South Africa. Over the last few years, there has been an improvement in terms of collecting data from the formal sectors perspective, however not so much on the informal sector where poverty and structural inequalities persist. The exploration element of the study then is followed by a qualitative approach. This study will aid in understanding the contexts to address the problem or issue (Creswell, 2007: p40).

#### **3.3 Research design**

##### **3.3.1 Target population**

Saunders, M., Lewis, P. and Thornhill, A. (2012 p.597) in their paper define the population as “the complete set of research participants available to the researcher. To maximise information, it will involve multiple data sources”. Most of the information will be from the DFIs. These institutions have been identified to include IDC, NEF, and SEFA who have a mandate specifically for SMME development. In addition to the DFIs, we have sampled SMMEs in the townships to test effectiveness.

The study was conducted in South Africa, Gauteng province. It is mainly focused on various townships in Gauteng for geographic diversification. The SMMEs are important as they would be the “to be” beneficiaries of the DFIs and government agencies. Qualitative research was used to provide the researcher with the opportunity to conduct interviews with SMME and senior managers of the DFIs to gain an in-depth understanding.

### **3.3.2 Units of analysis**

Saunders, M., Lewis, P. and Thornhill, A. (2012 p.77) explain the unit of analysis in research to be “the major entity that you are analysing in the study”. Your unit of analysis is the ‘who’ or the ‘what’ that you are analysing. In this case it is the applicable DFIs as well as the individual business owners (SMMEs). The interviews from an SMME perspective are aimed at beneficiaries of DFI support who would be able to unpack the effectiveness of the interventions and those that have not been able to understand the reasons for not using the support available to them.

### **3.3.3 Sampling technique and size**

Saunders, M., Lewis, P. and Thornhill, A. (2012) narrate a sample to be a subgroup of the whole population. In the townships, we do not really know how many SMME there are and with that in mind we used a sample methodology. This study specifically used purposive sampling within non-probability sampling. Saunders, M., Lewis, P. and Thornhill, A. (2012) define purposive sampling as a type of non-probability sampling in which the researcher’s judgement is used to select the sample members based on a range of reasons and premises (non-probability). We sampled ten (10) SMMEs operating in the townships and interviewed three (3) representatives from the government agencies/DFIs (Heads of departments or senior individuals). Structured interviews were held via Microsoft teams (5), WhatsApp call (1), face to face sitting (2) and questionnaires (2) with the township entrepreneurs given some limited access to technology. There were instances where SMMEs could not sit for an interview, we used questionnaires in those instances. In those instances, the approved questionnaire was shared with the participated and returned completed. All participant requested accepted to be involved in the study. Structured interviewed where held electronically via Microsoft teams for (2) representatives and 1 by a completed questionnaire of the DFIs. Several requests were sent out to the GEP who never responded to the call for an interview.

There is sufficient geographical diversification for DFIs and SMMEs. The sampled entrepreneurs run business operations (owner managed) in various townships such as Tembisa, Katlehong, Soweto, and Mamelodi. The population was diverse in sector, years in business, gender, and demographics. The sectors in which the entrepreneurs operate are also diverse as it includes, Taxis, Stokvel, Business consulting, logistics etc. On the DFI side both regional and national DFIs were represented.

### **3.3.4 Data collection instrument**

Interviews provide researchers with detailed qualitative data for a rich understanding the participants' experiences, how they describe those experiences, and the meaning they make of those experiences (Rubin & Rubin, 2012). Semi-structured interviews and questionnaires were conducted as a method of collecting data. In certain instances where face to face interviews was not possible, questionnaires (sent via email) were sent to the SMME and the DFIs. Saunders, M., Lewis, P. and Thornhill, A (2012), researchers using semi-structured interviews prepares a list of topics to be covered (not necessarily strictly formal) and questions to be asked. Semi structured have more open-ended questions rather than closed straight forward question.

The questions in the interviews (Appendix B) were designed to be semi structured to get a more personalised as well as broader insights from the area of the research. When questions are more open-ended questions, they allow the interviewee freedom from being pushed into constrained alternatives (Koboekae, 2012). Furthermore, there is also avoidance of leading-questions, bias, indiscretion and repetition in the questions and the interviewer's delivery was avoided for the investigation to remain as objective as possible.

The Interview Protocol Refinement "IPF" framework was followed which helped to strengthen the reliability of interviews during qualitative research and thereby improve the quality of the data obtained in interviews (Castillo-Montoya, 2016). The process includes (1) making sure the interview questions align to the research questions (2) creating an inquiry-based discussion (3) receiving feedback on interview protocols and (4) piloting the protocol.

We interviewed 10 SMMEs who run their businesses in the various townships in Gauteng. Due to confidentiality and the Protection of Personal Information Act, 2013, the DFIs interviewed above could not provide the researcher with names of businesses whom they have provided funding to. This would have given the study direct appraisal to access the impact and effectively

of the lived experience of those whom they have aided. The researcher interacted with Facebook (Brown sense group, Kasi Economy group), Twitter (Kasi Economy page) and word of mouth to sample businesses to interview. All the 10 entrepreneurs are owners and founders of their businesses.

### **3.4 Data gathering process.**

As this research is more exploratory in nature, which requires an in-depth analysis of the study. It is thus more appropriate to use a semi structured interview as the best method to collect the data. Semi-structured interviews allow the researcher to follow questions and topics that he or she thinks needs to be covered. These were the same standard set of questions for each of the participants which will be researched in advanced and must be designed in a manner that addresses the objectives of the study. In O.P.Atieno (2009), qualitative researchers are more interested in the meaning how people make sense of their lives and their structures of the world. It is the process rather than the outcomes or process that they are concerned with. As these will be a standard set for each separate population sets, this ensures consistency. The interviews are planned to be completed face to face, should the respondents not be available face to face then an email with a link to the questionnaire that was compiled using Survey and telephone approach was accommodated.

Permission was requested and any ethical concerns to be addressed prior to the interviews. The study was anonymous and on a voluntary participation basis with clear confidentiality. The participants were be asked to be honest and not bias in their response. The information will remain confidential.

### **3.5 Data analysis**

Charmaz (2014) defines data analysis as a process in which the researcher utilises to reduce the data gathered into a story and its interpretation. There are a few different ways to analyse qualitative data. There is a combination of factors that determine the analytical approach of a researcher such as the research questions that are being asked, the theoretical basis of the study and the appropriateness of the process to make sense of the data. Framework analysis involves familiarisation of data, searching and identifying thematic framework, coding and eventually interpreting the information.

Creswell et al. (2007), explained this concept in his paper where he mentioned that they would go through the transcripts from the 10 interviews and begin highlighting significant statements, sentences or quotes that provide an understanding of the overall timing experience. Next, they would array these statements on paper and collapse them into meaning units or broader themes”.

As part of the thematic analysis process, the recordings of the interviews and questionnaires were transcribed and analysed through thematic content analysis using the five-step method developed by Rugman (2013), as follows:

- Step 1: the researcher must familiarise themselves with the data – Read and re-read the data recordings to grasp the broad and general messages that is conveyed by the data.
- Step 2: Generate initial key codes – researcher must go through transcripts noting and highlighting any statements that put forward codes that have a close similarity to the research questions.
- Step 3: Develop topics – Based on the codes, develop initial themes and topics and sub-themes under which the findings from the interviews could be presented.
- Step 4: Review themes, topics, and sub-themes – Review the initial themes by assessing if there is enough information to support each of the themes, topics, or sub-themes.
- Step 5: Define and name the themes – Prepare short definitions for each theme/topic to capture what each theme represents. Based on these short definitions, given explanations that will respond to the research questions and specific research findings.

In addition to the analysis, the researcher referred to the study findings and compared with the theories and ideas discussed in the literature review. This comparison is used as a way of validating the findings.

### **3.6 Reliability and Validity**

According to Adams et al. (2007), reliability and validity are two essential criteria that were important when evaluating the effectiveness of a measurement. This would be particularly important given the ambiguous nature of qualitative research. Validity is the representativeness and the precision of the findings relating to the data, on the other hand reliability is concerned with concerns maintaining consistency within the analytical procedures (Noble & Smith, 2015).

To maximise validity, there are three measures have been put in place for the pre-testing phase. For one, engagement with other researchers' pre-interview must be done to minimise potential research bias (Noble & Smith, 2015). Additionally, during the interview, record-keeping should be meticulous, and the interviews must be recorded and transcribed – to ensure consistent interpretation of the data. Lastly, respondent validation will be incorporated into the interview process whereby respondents will be invited to comment on the transcript and provide feedback on whether the recorded findings accurately reflect their experiences and the phenomena being tested (Noble & Smith, 2015).

In terms of reliability, there could potentially be issues at the stage of wording the questions and testing the survey. To mitigate this, then questions were sent to the research supervisor for independent verification before the sample is surveyed. After that a pre-testing phase will take place where the survey questions are asked to a group, like the sample being questioned, to identify errors or inconsistencies in the design of the survey. The piloting of the questionnaire assisted to assess the time it takes to complete the questionnaire, then clarity of the instructions and how clear the layout of the questionnaire is.

To minimise research bias, the research was conducted in different sites (different townships and different micro-enterprises) or using different methods (interviews and questionnaires).

### **3.7 Ethical considerations**

The checklist by Patton (2002)'s unpacks what constitutes good ethical conduct when one is conducting field work. The checklist addresses issues around legal risk and other risks of the method of research, reciprocity, confidentiality, informed consent, data access and ownership. Ethical clearance was applied for from the University of Cape town's ethics committee and was granted on the 3<sup>rd</sup> of October 2022 by the Departmental Ethics Representative. All interview participants were requested to sign a consent form that outlined the details of the study such as purpose and data collection process. The participants who took part in the study were SMMEs in the township who were partaking in their personal capacities and therefore organisational consent was not required. The representatives from the DFI were senior members of their respective organisations. We did not receive organisation consent except for GEP however this was based on their own understanding of their organisations and not on behalf of the organisation. GEP however did not avail themselves for an interview. Confidentiality was

maintained so the names of the interviewer and the name of the DFI was removed. Participants were assured their anonymity will be maintained. All participants agreed for their names to be published. The interviews were electronically recorded (via Microsoft teams or cell phone voice recording) and only the researcher had access to the recording.

## Chapter 4

### Findings and discussion of results

#### 4.1 Introduction

This chapter presents and analyses the findings from the semi-structured interviews/questionnaires with senior representatives of 3 DFIs and 10 SMMEs operating from the township. The chapter lays out the findings in line with the methodology as discussed in chapter 3. The aim of the study is exploratory in nature to gain familiarity and insights into the role and effectiveness of DFI in developing SMMEs in the township economy. Section A are insights and findings obtained from representatives of the DFIs while Section B is an analysis and findings from an SMMEs perspective.

#### 4.2 Sample overview

The description of the sample, as covered, in the data collection described in chapter 3 is summarised in tables below. A synopsis of participants that were interviewed is shown in the table 7 (DFIs) and table 8 (township SMMEs). The research was broken up into (1) representatives of the DFIs who's organisations are mandated to provide support to SMMEs and (2) SMMEs to unpack their lived experience of government support, if any.

*Table 7: Characteristics of respondents - Profile of the DFI representatives*

Number	Regional/National	DFI	Representative	Years of experience
DFI 1	National DFI	IDC	Senior Transactor	+15 years
DFI 2	National DFI	NEF	Senior Fund manager	+20 years
DFI 3	National DFI	SEFA	Strategy and Planning	+10 years

Note: Research data

The results indicate that all respondents interviewed had more than 10 years' experience working in financial services particulates in the DFI space. Respondents had the right level of seniority and appropriate role to engage.

The SMMEs sample consisted of 10 participants who own businesses in the various townships of Johannesburg. 8 businesses are registered with CIPC or the national regulating body for the

industry they operate in while 2 are not registered businesses. The businesses are 100% owned by South African nationals.

The businesses covered in the sample fall into 8 different industries with transport/logistics, beauty, consulting, and commercial property being sampled more than once. All businesses operate only in the Gauteng province; however, the townships expand to Tembisa, Soweto, Katlehong and Mamelodi.

The participants had varying educational level ranging from matric to master's degrees, all of them having passed Grade 12.

All SMME owners were the original founders of the businesses, and all used their own capital to fund their businesses as startups, none had purchased an already existing enterprise.

1 respondent received business development services from an incubation centre affiliated with SEDA, 2 respondents are undergoing credit assessment with SEFA, 1 respondent declined an offer for funding and the rest of the sampled population did not utilise any government assistance in their businesses.

The population sampled is diverse in sector, years in business and gender and demographics. In terms of gender 30% are females and 70% males, all African. The ages of the respondents ranged from 30 to 77 years old, with an average age of 43 years. The youngest participant was 30 years and the oldest 77 years. five participants were between the ages of 31 to 40 years, four between 40 and 50 and one older than 50

Table 8: Characteristics of respondents - Profile of the Township SMMEs

	Gender/Demographic	Participant	Township	Years in operation	Highest level of education	Type of business	Age of owner/s	Legal status
1	Male/African black	Participant 1 (F01M)	Tembisa Mamelodi	+7	Matric	Township delivery service	38	Registered
2	Male/African black	Participant 2 (A02M)	Tembisa	+25	Matric	Taxi Owner	77	Registered
3	Male/African black	Participant 3 (M03S)	Soweto	4	Diploma	Business Services (consultant, stokvel franchise)	41	Registered
4	Female/African black	Participant 4 (Y04S)	Soweto	14	Honours Degree	Commercial Property	38	Registered
5	Female/African black	Participant 5 (N05M)	Soweto	4	National Diploma	Commercial Property	43	Registered
6	Male/African black	Participant 6 (B06M)	Soweto	8	2x Masters	Commercial Property	35	Registered
7	Male/African black	Participant 7 (S07M)	Tembisa	+15	Degree	Transport	51	Not registered
8	Male/African black	Participant 8 (T08M)		8	Degree	Gaming	30	Registered
9	Female/African black	Participant 9 (N09K)	Katlehong	2	Matric	Beauty	31	Not registered
10	Male/African black	Participant 10 (N10S)	Katlehong	3	Honours	Petrol Station	43	Registered

Note: Research

### **4.3 Section A: Thematic findings from DFIs**

The thematic analysis of the responses by the DFIs to the questions relating to the tools and mechanisms used to develop the township economy and the effectiveness of the government role in developing township economies. The findings are presented according to meaningful themes that emerged from the structured interviews with the representative of the DFIs:

#### 4.3.1 DFIs mechanisms used to support the township economy.

- a) Financial and
- b) Non-financial support

#### 4.3.2 Effectiveness of DFIs

- a) Investments made to the township economy.
- b) limitations

#### **4.3.1 DFIs mechanisms used to support the township economy.**

This section answers the question: “What tools and mechanisms are used to develop township economy.”

From the research conducted, there was consensus on the kind of support being provided which was broadly in categorised into of financial and non-financial support. Provision of development finance such as grants and guarantees are mechanisms that the government uses to directly inject to the townships however using the DFIs as a conduit. This is a way to catalyse and assist in investment mobilisation thus promoting shared economic growth. These tools of support are in line with the literature by (Rwigema & Karungu, 1999).

#### a) financial support

Outside of development finance (grants), the main support was found to be more financial in nature, which can be structured in many ways such as debt or equity and quasi-equity, trade finance and venture capital as examples given by DFII.

*The threshold lending is for funding needs of R1m and above. Any funding request by a prospective client that is less than R1m is deemed too immaterial and will not be considered. We do work closely with other DFIs for smaller funding needs. (DFII)*

By virtue of the nature and type of the township entrepreneur (micro in nature), this threshold of DFII disqualifies countless of businesses of their financing needs.

DFI 2 Financial support includes uses of a combination of funding instruments such as secured (senior debt) to unsecured options (equity), and/or a hybrid of the two. The DFI lending is for funding needs that are from R250,000 to R75,000,000.

*If for example the target for the year is R1.2billion of investment, the DFI must invest 30% of the target to Township and Rural businesses. The 30% will go into the specific fund for Rural and Township businesses. (DFI2)*

DFI3 provides SMMEs and cooperative throughout South Africa with access to finance through a Direct Lending channel and Wholesale lending channel. The Direct lending to SMMEs and cooperatives range from R5m to a maximum of R15m. these are in a form of Asset Finance, Bridge loans, Revolving and Term loans. The wholesale lending, they provide Debt or equity to intermediaries, joint venture, partnerships (Specialised Funds) and other collaborative relationships to extend the reach for funding small businesses across South Africa. The Loans to intermediaries can go up to R150 million while loans through intermediaries to end-users up to R5 million. *For the fiscal year 2022/23 the DFI has approved about R1,7 billion for small businesses and co-operatives. We have disbursed about R2,4 into the South African economy in support of small businesses and cooperatives. (DFI2)*

From the findings, all DFIs expect the shareholder and/or sponsors to have some “skin in the game” by providing some financial contribution (capital/equity injection). The contribution of previously disadvantaged individuals under extraordinary circumstances may be lowered, and in that case the DFI will be prepared to extend finance higher than the owner’s contribution.

DFI 1 has a minimum requirement also includes security in a form or nature which relates to the lending. However, DFI 2&3 this is not a requirement given their mandate is for transformation and entrepreneur they work with rarely have security to offer.

All DFIs highlighted in the interviews that DFIs must pay attention specifically to the township economy given the potential role it may have in creating jobs, stability and creating black social capital. The DFIs note that the township economy is a force that needs to be looked at and will play a meaningful role if we were to change the fortunes of this country.

#### **4.3.1.2 Non-Financial Support**

Non-financial support compliments the financial offerings by the DFIs. The DFIs can reach more people, provide services at a lower cost, and have access to greater knowledge and expertise through strategic partnerships. DFIs also dedicate resources to preparing projects for investments right from inception, these processes form part of business development services being offered.

##### **Strategic partnerships**

The role of the DFIs has evolved over time, to also identify opportunities for collaboration and coordination amongst other South African DFIs and private players. Currently, DFI3 and the DTIC are working together to provide funding to companies that are in rural, township, or economically undeveloped areas. This is another mechanism used by DFIs to support the township economy is by providing strategic partnerships.

Special collaboration with other DFIs and the private sectors was also mentioned as means to support the township SMMEs. Two DFIs specifically mentioned the partnerships, especially for township businesses. The partnership between NEF and DBSA called Sakhumzi was raised by one of the DFIs. Another DFI has D-labs (development lab) which focus on social infrastructure in the township aimed at providing previously inaccessible education and services. The DFI takes opportunities to the township which include aiding in skill competencies development for young people to access the mainstream economy, enables them to solve challenges.

##### **Business Development Services**

Business Development services are an important way of supporting the developing SMMEs which helps improve governance. The importance of business development service was highlighted by all DIFs participants to ensure that they support skills capacity building through these interventions. All DFIs agree that the township economy is critical and there are many programmes that are built around supporting this marginalised groups. Business development services improve an organization's performance, competitiveness, and market accessibility.

DFIs emphasised that a sizeable portion of their support mechanisms and instruments are non-financial in nature as well as financial.

DFI 2's business development services that are offered include pre-investment services. *The market that this DFI is mandated to service (Black population) has been excluded for many years due to apartheid and colonialism. Given the economic exclusion, when the clients approach the financial institution, there is a lot of hand holding. Those activities are what is called "pre investment" services. These activities are not only limited to the DFI itself, but rather can be applied to other financial institutions as an empowerment tool. (DFI1)*

The DFI has also got a financial model on their website which can be used freely, their application form is also universal in a business plan format to guide the applicant and ensure sufficient information is received. The institution also does roadshows across the country where they engage directly with entrepreneurs and communities on the ground particularly around financial literacy. The organisation provides information as wide as how individuals can access shares and provides awareness around the importance of entrepreneurship.

DFI1 has a condition for participation in TREP, the business owner must agree to follow applicable product standards, take part in the DSBD/SEDA facilitated business development process and get mentorship and training in business and financial management from the Business Services assistance programme.

Once the business is banked and invested; the organisation is also post-investment services as part of non-financial assistance. In post investment, they help the entrepreneur monetise and create value within the business as well as provide mentoring and guidance.

Lastly turn around, for businesses that are in distress to mitigate the risk of business closure they can turnaround effectively giving a lifeline to a dying business.

*There is more interest to do business with the SMME's but there is also more work in doing business with the township's entrepreneur. The issue is when township people are unhappy, they go burn the infrastructure because they do not own the asset. If we have township businesses that originated and are owned from the local environment. The people will not*

*vandalise what they own so it is important for the township economy to be owned by the people hence the need to support them from a DFI perspective. (DFI1)*

### **4.3.2 Effectiveness of the role in the township**

This section answers the questions on the “The role of DFIs in supporting township enterprises” and “How effective is the government role in developing township economies?”

#### **a) Investments made to the township economy.**

There was consensus that it is the responsibility of the DFIs to finance investments that promote development for entities in various sectors. DFI’s primary goal is to make investments in sectors with institutional shortcomings and insufficient market investment such as the townships. The DFIs affirmed that the role and impact they play in the township economy is documented and presented to parliament annually which talks to their positive contribution to economic growth of the rural and township economies given that most of these entrepreneurs would not have received support from traditional financial institutions.

By providing finance to entrepreneurs in a range of industries, including manufacturing, real estate and affordable housing, tourism, agro-processing, and energy, DFI3 has sped up economic transition. Additionally, this has helped the township and rural economies and built a network of Black industrialists with manufacturing and industrial capability. DFI3 granted R1.2 billion in investments to Black South African-owned and managed enterprises in the 2002/2003 reporting period, mostly in townships and rural regions exceeding their budget by 0.2 billion. R692 million in total was invested in the domestic economy, resulting in the creation and maintenance of 4598 jobs. To date the DFI has disbursed circa R2.4 billion in support of over 380 entities in rural and township economies. Re-capitalization of the DFI is a priority that will continue to be prioritised to make more impacts. This will not only allow the impact to be massified but also expand the reach by fostering the creation of sustainable SMMEs particularly in townships and rural areas. These SMMEs have the potential to spur economic growth in economically depressed regions, bridging the economic divide. The township economy is then able to operate, scale up and contribute to reducing unemployment. This is corroborated with part two of the research findings by SMMEs below, the level of contribution needs to be improved which would overall improve effectiveness and impact.

#### **b) Limitations**

Overall effectiveness is impacted by the claims of poor management by the entrepreneurs and mismanagement inside DFIs, along with a high percentage of businesses failing which affect the effectiveness of the role they play in developing the township economy. There were two broad themes which affect DFI effectiveness in the township economy were noted by all respondents:

**i. Bankability of township SMMEs**

DFIs are required to implement strict investment standards that protect social responsibility, transparency, and financial sustainability. The study reveals that the success of a SMME in applying for funding, depends on the quality of the business plan and the loan application. Applications get declined by the DFIs because of financial viability, market visibility, technical competency, character risk and weaker business plan among other things. These are ‘in any case’ typical constraints that a township entrepreneur ordinarily must access financial markets.

*The success rate for application received is around 2% meaning if one hundred applications are received only 2 will be banked because the rest of the applicant do not meet the criteria. The annual report for 2021-22 indicates that the DFI approves 203 transactions worth R1.3bn, with a success rate of 2%, it means they received 10 150 applications and 9 947 were rejected due to bankability. The main are issues around project viability, incomplete information and hence the need for a grant to be more accommodative. (DFI2)*

Bankability remains a key concern from a DFI perspective. The issue with DFIs and banks they have limited risk appetite towards SMMEs, particularly start-ups and lower end micro businesses. South Africa’s township economy is mostly made up of small, micro, and informal businesses in the informal sector many of them survivalist businesses however constitution to income opportunities and job creation.

DFI3’s qualifying criteria for the TREP program which is aim particularly at the township includes: (1) formal registration of the business with CIPC, (2) Business license with local municipality (3) valid business bank account (4) registration with SARS and UIF (5) employees must be 70% South African or hold work permits from DOH.

From the findings, all DFIs expect the shareholder or sponsors to have some “skin in the game” by providing some financial contribution (capital/equity injection). From the research conducted, the DFIs indicated that the contribution of equity from previously disadvantaged populations (townships) under exceptional circumstances may be lowered, and in that case the DFI would be prepared to extend finance a higher debt to equity ratio.

The lack of collateral was also a big obstacle in the tools for support. DFI1 has a minimum requirement which also includes security in a form or nature which relates to the lending. However, DFI 2&3 this is not a requirement given their mandate is for transformation and entrepreneur they work with rarely have security to offer.

The role that DFIs can play in the township becomes less effective as most applicants are excluded due to strict lending criteria.

Given the nature of the township business which is the 'informal economy' this represents a true dilemma. This does create an opportunity to redesign the bankability criteria for this group of businesses. There is a need for transformation in lending criteria so DFIs can play a more meaningful role. (Adewale & Olalekan, 2016), found that one of the main causes of the sluggish growth of small businesses, especially in developing African nations, is the inability to obtain financing.

## **ii. DFI Funding mechanisms**

South African DFIs function on a “not for profit” basis despite that their role is to facilitate a developmental objective. This is because the government lacks the funding to underwrite the losses that come with high-risk clientele. As a result, it has become difficult to distinguish between the DFIs and commercial banks because DFIs frequently fund projects or opportunities that the private sector would equally be willing to support. DFIs in this study are self-financing organisations because they must reinvest the earnings made from successful investments into new meaningful investments but also pay salaries and other expenses.

Furthermore, the DFI now compete for feasible projection the market based on their term sheets rather than making projects itself. The research shows that DFIs do not provide grant finance and therefore they do not have much room for technical help and concessional support which

would be more beneficial for high-risk funding such as township businesses. They do however make use of quasi-equity and patient capital although capped at extremely low levels. More of a challenge is that DFIs like commercial banks have a limited appetite for investing in early-stage initiatives, SMME scale project or new and innovative technologies and business models. These would increase their appetite to the township and in turn become more impactful in the township economy.

All DFI who participated in the research are self-funded. While these DFI are 100% government owned, they do not receive grants or funding from the government and therefore must raise capital to support their mandate via the capital markets. Unlike traditional banks who are deposit taking and can get cheaper source of funding, these DFIs are constrained by expensive funding in the market in the absence of government capitalisation. DFIs face challenges balancing profits and development due to the lack of additional capital resulting in them having limited opportunities for investment in high-risk investments.

The source of funding comes from a combination funds from international development agencies, commercial banks, and/or bond issuances coupled with internally generated funding. The DFIs also need to ensure their long-term sustainability through prudent financial and human capital management whilst safeguarding the natural environment and positioning as forerunners in development finance.

In the absence of government direct funding to support their developmental mandate in high-risk investments such as township. How much of a role can they play in the township given their high-risk nature. The result also mean that they must ration the credit. Is this effective? Could this be a limitation?

*Initially the DFI was given R2billion by the government as seed capital 15 years ago. That was the only capital received from the government. No other allocation has ever been received from then however through investing the money, collections and reinvesting the balance sheet has growth to R13bn. Investing in projects has grown the book. There are instances where capital is raised from private sector partners and other government entities where the DFI enters partnerships and provide fund management services managing their investments and that is how the institution recapitalises and manages liquidity. (DFI2)*

The conundrum of self-funded DFIs is that the higher cost of funding reduces their competitiveness in the market by pricing themselves out of projects/deals and thus create restrictions to fund higher risk sectors. As a result, DFIs are forced to apply strict bankability criteria which rules out the high-risk township entrepreneur. This exacerbates the funding gap, all DFIs interviewed agreed that diversification of funding sources and grant funding from the government becomes critical to reduce the overall cost of capital and increase risk appetite to high-risk sectors. The end goal should be on a blended finance regime that is to reduce the cost of financing to businesses and cooperatives.

#### **4.4 Section B: Thematic findings from an SMMEs perspective.**

In section B, discussions referred to, are in relation to themes identified during the structured interview process with township SMMEs. Thematic analysis of the responses addresses the specific research questions. Having established the role of DFIs and the tools and mechanisms to support the township economy. This section answers the question “What are the challenges of the entrepreneur’s own experience when using government led development services.”

##### **4.4.1 Challenges experienced by township SMMEs.**

- a) Lack of knowledge and understanding of the role of DFI
- b) Limited appetite for start-up funding
- c) Strict credit assessments
- d) The mismatch in how SMMEs want to be supported versus how the support received.

##### **4.4.1 Challenges experienced by township SMMEs.**

- a) Entrepreneurs’ knowledge and understanding of the role of DFIs.

Research conducted showed that all participants have a level awareness of DFIs and their role in the township communities. However, while all participants had an awareness, two respondents (taxi business) were adamant that their sector does not get supported financially to acquire their assets (taxis). There was consensus from the entire population interviewed i.e., 2 out of 2 entrepreneurs interviewed in this sector. One participant did not know what a DFI was but did understand that government does help small businesses.

*Many operators' resort to own funds, banks, and other financial institution such as SA Taxi to assist financially to purchase their taxis. These institutions charge extremely high interest rates and as a result the default rate is quite high. Our industry is not supported by the government. (A02M)*

The taxi operators only been given financial support of R5000 from the government during the COVID-19 crisis. The R5000 was not sufficient to cover vehicle instalments, or any working capital needs therefore the amount was far less than what was needed at the time of the hard lockdowns. This money was only paid out to taxi operators who were registered for tax thus only a few taxi operators/owners qualified and received the funds.

While there are well over 10 DFIs in South Africa, many of the participants mentioned SEFA and GEP specifically as having an interest in the township economy. Out of the ten, two participants have been approached by a DFI directly, who have shown an interest in their business models. They are currently going through the credit assessment process. One participant approached a particular DFI for funding but was rejected due to not meeting the qualifying criteria. All participants who had an engagement with the DFIs indicated that the government needs to relax their lending criteria.

*The DFI does not fund commercial property or commercial vehicles, so my business was excluded from the lending criteria. The feedback given by the government agency was that through their experience in these sectors, entrepreneurs end up living in the commercial properties that are meant for business and thus not able to service the debt when it becomes due. (Y04S)*

One participant approached a DFI as they had a special programme for township entrepreneurs in the sector that he operates in. He did not find them useful as they had a standard response which was not helpful.

*I have never applied to other government institutions due to the bad reputation they have generally. I did try with one of them, but they gave me a standard response and was not helpful at all. (B07M)*

Most participants talked about having workshops so that people are more informed and educated. Information and awareness were identified as a huge problem. The numbers indicated

that people who are connected get ahead. You need to know someone to connect you with people. *People are thirsty for knowledge of what DFI are and what they do. (N04M)*

b) Limited appetite for start-up funding

The research shows full consensus amongst all the participants who have dealt with DFI is that their risk appetite does not allow for funding starts up businesses. This is similar feedback received from participants which relates to other financial Institutions such as Banks.

The findings show that there is no appetite for funding “green field” projects, all participants used their own money to start up their businesses. Money from savings, overdraft and credit cards was the general theme amongst the participants.

*The business is self-funded from my consulting work, overdraft, credit cards. ((F01M))*

*As an employee in my younger days, I used his own savings to buy a small car which was used for long distance transportation to Matatiele in the Eastern Cape on weekends. Through this activity, I managed to buy my first taxi and got a formal transport license from the Department of Transport and that is how one taxi funded the fleet of taxis grew. (A02M))*

c) Strict credit assessments

For DFI and Bank funding, one needs to display a solid track record. This entails that applicants must evidence that they have several years in the business and have historical financial information/cash flows to support this. All entrepreneurs that were interviewed self-funded in the beginning. Three participants used microfinanciers to expand their businesses. One participant’s funding was from TUHF’s finance product called “Umastandi” after buying land and not being able to develop it.

While TUHF funds start-ups, one needs to have collateral. Umastandi gives financial and education support for existing township properties. Property owners who hold title deeds can approach uMaStandi who is a micro financier for finance to develop units on their property which can be used for rental income. In this model, the entrepreneur does not need to have a history of operating unlike the requirements for DFI support, but financing is based on character, the area they are operating in and the project itself. A feasibility study is however

conducted. If the project is approved, uMaStandi will help with the finance as well as training during construction, letting up and ongoing property management. UMaStandi supports solely township areas.

*I bought some stands in 2011 for R150 000 but struggled to get funding to develop any property on them. I even sold one of the stands with the hope of raising funds to develop properties others which was not enough at all. I was advised by my mentor on uMaStandi finance product. I applied for and received funding in 201. It is easier to get funding even though its more expensive. (N04M)*

*I tried banks for more than 6 years with no success due to my credit profile. It is then that I got to learn about DFIs, The Nelson Mandela foundation but ended up with UMaStandi as it was easier to get. I was even told that townships are elevated risk by the other lenders (N04M).*

Two participants are currently going through the credit assessment process for DFI funding.

*There is quite a bit of documentation and paperwork required, which is a lot of work. The conditions of funding proposed is that 10% of the funding, you do not have to pay back (grant), 90% is on concessional rates (cheaper than bank funding) however should there be a default then the DFI will get 40% equity in the business. (F01M)*

The issues raised by the two entrepreneurs being assessed for government funding is of the cumbersome documentation required and that the proposal should not be called “funding.”

*Funding should look more like a grant rather than debt. Funding should not be putting the company into debt. (F01M)*

The concerns raised by an entrepreneur who is going through government funding assessment was “it is difficult to let go of 40% of the business that one build from scratch through hard work and dedication thus the offer will be rejected. The view is banks do “funding” but DFIs should not be asking them to pay back if it is for empowerment purposes. Another frustration is that they do not fund start-ups as well, so it becomes difficult”

d) Mismatch in how SMMEs want to be supported versus How they are supported by DFIs.

The study reaches consensus that DFIs need to understand that businesses in different environments require support that addresses their unique challenges. It's important to understand the limitations that exists and be able to tailor solutions that are appropriate to this economy. There is a common theme that requires better support and more consultation with the entrepreneurs.

*One of the biggest mistakes the government makes is that they want to do things for us not with us. (M03S)*

*Often DFIs come with a program designed for the township without the consultation of the actual SMMEs. "Entrepreneurs want to be active participants in the 'support' initiative by the DFI. The model should involve active participation from the township business community. The best program would be where they are heard and building in conjunction with the SMMEs. Government should build policies in consultation as well. We don't expect the government to give us things. We want to work with the government. (M03S)*

One of the participants indicated that the government is not ready for the revolution, their drive to revitalise the township is artificial as it was imposed by COVID-19. The averages spending in the suburb has declined significantly in Sandton. People no longer have funds due to COVID-19 and the current macro-economic environment. The marketing revenue is not making sense. The government realised that work force stays in the township thus making the township the new economic hub.

One participant used the "non-financial support offered by the Youth Development program. this was through their voucher programme. This program is a business support programme aimed at assisting young entrepreneurs by providing business development support through NYDA's approved business consultancy service providers thereby enabling their participation in the mainstream economy. The vouchers range from R6 600 to R19 800. There is no contribution fee required for young entrepreneurs to participate in the programme. Each registered entity is entitled to a maximum of two (2) vouchers as per business development phase. Services offered by the NYDA include but are not limited to Business Feasibility, Bookkeeping and Financial Administration, Website development and hosting, Business Plan Development and Marketing Strategy and Plan. The quality of the services provided was found to be unsatisfactory.

*A business plan was drafted for me, but I could not vouch the suppliers. I only gave them a one pager on my business. I was expecting a consultative process. I did not identify some of the information used. It was difficult for me to talk through it as I was not involved in it. I merely gave a one page and got a full document back. I needed to be part of the process, but I was not. Those services did not work for me. (Y04S)*

#### **4.5 Summary**

The study reveals that the success of DFIs funding a business will be dependent on the quality of business plan, the loan application, and whether the business is viable. The study reveals that there are more applicants that are declined for support than those who are approved. In fact, a 2% approval rate was mentioned indicating that 98% of applications are rejected because businesses do not meet the minimum criteria and therefore are not 'bankable'. All DFI indicated that applications are declined because of financial viability, market visibility, technical competency, character risk and weaker business plan among other things.

The concern is that these are typical constraints that the township entrepreneur ordinary experiences regarding access to financial markets. SMMEs (on the contrast) indicate that government should fund their businesses as they are. That would be an indication of support.

There is a general awareness of DFIs in the township with two agencies being the most popular among the participants. DFIs have indicated they have a requirement for entrepreneurs to have skin in the game meaning entrepreneurs need to have an equity injection into their business first. Equity is a big stumbling block as many entrepreneurs do not have these funds. The research shows full consensus amongst all the participants that the DFI criteria does not allow for funding of starts up businesses.

The lack of knowledge from the township entrepreneur's perspective is one of the reasons why there is not much interest in the support. While the study found that all entrepreneurs have some varying knowledge and awareness of DFIs, only 2 were approach and are undergoing credit assessments, 1 was rejected by the DFIs as not meeting the qualifying criteria and 1 was able to get non-financial services which was found not to be effective. The rest have gotten no assistance from DFI.

All SME self-funded as startup and to expand, Microfinanciers or banks or own means. No entrepreneur received funding.

The above findings correlate with the low penetration rate as confirmed by DFI where only 2% of applicants are bankable. While DFI are effective, their reach is still very minimum. They need programs aimed at improving bankability and supporting starts up. All participants indicated the lack of appetite for startup being a huge challenge.

## Chapter 5

### Summary and recommendations

#### 5.1 Introduction

This concluding chapter presents the conclusions drawn from the results of the data that was collected and analysed, the literature reviewed and sets out the limitations and provides recommendations for future studies.

#### 5.2 Summary of the study

The research explores the role and effectiveness of DFIs in supporting the township economy. Townships are epitomised by lack of access to even the most basic of services, high unemployment rates, high crime which often results from lack of economic opportunities and activities. Townships by virtue of our past, are often overlooked and underserved with regards to economic development. DFIs have emerged as key players in addressing these challenging by providing financial support and non-financial support to entrepreneurs in the township.

This study aimed to explore:

- a. The role of DFIs and government agencies in supporting township enterprises?
- b. The tools and mechanisms are used to develop township economies?
- c. How effective is the government role in developing township economies? What are the challenges of the entrepreneur's own experience when using government led development services?

The study begins with examining the mandates of the DFIs and explores the various DFI interventions and tools used for employment creation and creating an involvement in economic development in the townships. The study also considers the challenges and limitations faced by the DFIs, such as funding. Furthermore, the research evaluates how impact is measured and effectiveness of DFI in achieving their objectives within the township economy context.

The key findings from the research

98% of businesses are not successful in their application for funding, that is where pre-investment services by government are required the most. The DFIs confirm that there are deep

structural issues characterised by our history. The combination of alcoholism and poverty also destroys mental capacity and the ability for cognitive learning which has an impact on financial literacy and the case of bankability.

Often DFIs come with programs already designed for the township without the consultation of the actual SMMEs. Entrepreneurs want to be active participants in the ‘support’ initiative by the DFI. The model should involve active participation from the township business community. The best program would be where they are heard and customised in conjunction with the SMMEs. Government should build policy in consultation with the SMMEs as well.

### 5.3 Conclusions

Based on the analysis and findings, the concept of DFIs is vital and critical in that they play an enormous role in supporting the township economy by providing financial and non-financial resources, technical expertise, and capacity building support. They have and continue to contribute to the growth and economic development of township business. These actions enable job creation, they play a role in poverty alleviation and income generation. However, the effectiveness of DFIs is dependent upon addressing key challenges that include enhanced co-ordination with the SMMEs themselves, improved penetration to those businesses that require access to finance, strengthening the awareness. Bankability and business viability are some of the biggest hurdles for closing the gap between entrepreneurs thriving and effectiveness of DFI support. Bankability often stemming from lack of skills is a key bottleneck in unlocking the true potential of DFI support.

In conclusion, DFI have emerged as valuable institutions for supporting the township economy, bridging the gap between financial exclusion, and needed economic development. By providing financial products and technical support DFIs in their form can facilitate the growth of township businesses and can contribute to empowering the local community. However, there is a lot of room for improvement in terms of collaborations with the communities, reach/low levels of penetration and addressing operational challenges.

To unlock the full potential of DFIs, it is important to adopt a comprehensive approach which is inclusive of the needs of the SMMEs being served. SMMEs want to work with government. Policy reforms and programs to support township SMMEs must be designed with their full participation right from beginning to the end. Township entrepreneurs want to be part of the

solution and not to have the solution presented to them. From the study, microfinanciers seem to be getting more reach than banks or DFIs. The risk appetite includes starts up which is more attractive to SMMES while the cost of borrowing is higher.

#### 5.4 Recommendation

Based on the conclusions of the study, the following are recommended to inform government on township development policy:

- Better collaboration with the SMMES they serve. Solutions must be made in consultation with the SMMES.
- Increased grant funding for SMMES. The funding strategy of DFIs means they must operate such as banks. The government should make allocation within its budget towards Development Finance Institutions as this will enable these institutions to make advances at risk-free rates to boost economic growth.
- Government needs to invest in innovative ways to improve bankability. Given the low penetration rate, the focus should be on bankability. Special program to incubate businesses and aid bankability.

#### 5.5 Limitations and implications of future studies

The sample of the study was limited to Gauteng townships of Tembisa, Katlehong, Soweto, and Mamelodi; this would constitute a small sample if you had to look at townships in the entire South Africa. Gauteng townships also have unique layers of awareness and sophistication therefore the findings of the study cannot be deduced to other South African townships.

Studies from other townships would yield separate set of findings especially from a DFI awareness perspective. The Gauteng township revitalization bill would create more awareness given roadshows and media coverage, but other provinces could be left behind. It is therefore recommended that studies that cover all townships and a wider range of business sectors in South Africa be conducted to get deeper insights on the role and effectiveness of government in township economy development.

Similarly, the sample of the study for DFIs is limited to 4 (four) and can be extended to cover more regional players and national players given that South Africa has over 20 DFIs.

The study sample was concentrated on micro and small businesses. Medium to Large enterprises that are at a different stage of the growth cycle experience a separate set of

challenges and experience. It is recommended therefore that future studies under roles of government at each business cycle stage should cover the entire SMME value chain.

There is a need in future studies for research to be conducted on all the themes that were found to be challenges affecting SMEs in the townships, to obtain an in-depth understanding to aid better policy reform on township SMME development.

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## Appendix A: Signed Commerce Faculty Ethics Form



UNIVERSITY OF CAPE TOWN  
**FACULTY OF COMMERCE**  
 Igniting Knowledge and Opportunity



# Commerce Faculty Ethics in Research Application Form

Any person planning to undertake research in the Faculty of Commerce at the University of Cape Town is required to obtain ethical clearance. This form is intended for undergraduate students, honours students, PD Dip students and Masters students whose research component is less than 90 credits.

Once this form is completed it should be sent via email to your departmental ethics representative. Your supervisor will be able to provide you with the contact details.

It is assumed that the researcher has read the UCT Code for Research involving Human Subjects (Available at <http://web.uct.ac.za/depts/educate/download/uctcodeforresearchinvolvinghumansubjects.pdf>) in order to be able to answer the questions in this form. Students must include a copy of the completed form with the dissertation/thesis when it is submitted for examination.

1. PROJECT DETAILS			
<b>Project title:</b>	The role and effectiveness of DFIs in supporting township economies		
<b>Principal Researcher/s:</b>	Matau Molahloe	<b>Email address(es):</b>	mlhmat004@myuct.ac.za
<b>Research Supervisor:</b>	Assoc./Prof. Abdul Latif Alhassan	<b>Email address(es):</b>	latif.alhassan@uct.ac.za
<b>Co-researcher(s):</b>	NA	<b>Email address(es):</b>	
<b>Department:</b> Development Finance: Mcom			
<b>Brief description of the project:</b>			
<p>The project is to facilitate the fulfilment of a minor dissertation component of the Mcom in Development finance research report. The nature of this study is exploratory in nature to gain familiarity and understanding of the role and effectiveness of DFI in developing SMMEs in the township. The research approach is of a qualitative form in nature which will involve collecting and analysing first-hand information. The research will be used to provide the researcher with the opportunity to conduct semi-structured interviews with SMMEs and senior managers of the DFIs to gain an in-depth understanding. In any event where face to face interviews are not possible, questionnaires (sent via email) will be sent to the SMME and the DFI/government agencies</p>			
<b>Data collection:</b> (please select)			
<input checked="" type="checkbox"/> Interviews <input checked="" type="checkbox"/> Questionnaire <input type="checkbox"/> Experiment <input type="checkbox"/> Secondary data <input type="checkbox"/> Observation			
<input type="checkbox"/> Other (please specify): _____			

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Have you attached a research proposal OR a literature review with research methodology? (please select)  Yes  No

## 2. PARTICIPANTS

2.1 Does the research discriminate against participation by individuals, or differentiate between participants, on the grounds of gender, race or ethnic group, age range, religion, income, handicap, illness or any similar classification?	YES	<input checked="" type="radio"/> NO
2.2 Does the research require the participation of socially or physically vulnerable people (children, aged, disabled, etc.) or legally restricted groups?	YES	<input checked="" type="radio"/> NO
2.3 Will you be able to secure the informed consent of all participants in the research? (In the case of children, will you be able to obtain the consent of their guardians or parents?)	<input checked="" type="radio"/> YES	NO
2.4 Will any confidential data be collected or will identifiable records of individuals be kept?	YES	<input checked="" type="radio"/> NO
2.5 In reporting on this research is there any possibility that you will not be able to keep the identities of the individuals involved anonymous?	YES	<input checked="" type="radio"/> NO
2.6 Are there any foreseeable risks of physical, psychological or social harm to participants that might occur in the course of the research?	YES	<input checked="" type="radio"/> NO
2.7 Does the research include making payments or giving gifts to any participants?	YES	<input checked="" type="radio"/> NO

If you have answered YES to any of these questions, please describe how you plan to address these issues (append to form):

I will request all participants for a signed participants form giving consent. Appendix 1 attached

**Affiliations of participants:** (please select)

- Company employees    Hospital employees    General public    Military staff    Farm workers    Students  
 Other (please specify): \_\_\_\_\_

**Race / Ethnicity:**

Are you asking a question about race/ethnicity in your questionnaire?

Yes     No

Which race categories have been used?

- African black
- White
- Indian
- Coloured
- Other
- Prefer not to answer

Have you included the option: "Prefer not to answer" as part of your race/ethnicity question?

Yes

**3. PROVISION OF SERVICES**

Does your research involve the participation of or provision of services to communities?

If your answer is YES, please complete below:

3.1 Is the community expected to make decisions for, during or based on the research?	YES	NO
3.2 At the end of the research will any economic or social process be terminated or left unsupported, or equipment or facilities used in the research be recovered from the participants or community?	YES	NO
3.3 Will any service be provided at a level below the generally accepted standards?	YES	NO

If you answered YES to any of these questions, please describe below how you plan to address these issues.

N/A

**3. ORGANISATIONAL PERMISSION**

If your research is being conducted within a specific organisation, please state how organisational permission has been/will be obtained:

Not a specific organisation. DFI will be selected as well as SMMEs who have received support.

Have you attached the letter from the organisation granting permission? (please select)

Yes     No, but this will be obtained before commencing the research     Not applicable

Are you making use of **UCT students** as respondents for your research? (please select)

Yes     No

If yes, have you contacted Executive Director: Student Affairs for permission? (please select)

Yes     No

Was approval granted? (please select)

Yes     No     Awaiting a response

Are you making use of **UCT staff** as respondents for your research? (please select)

Yes     No

If yes, have you contacted Executive Director: Human Resources for permission? (please select)

Yes     No

Was approval granted? (please select)

Yes     No     Awaiting a response

Contact Emails: Executive Director: Human Resources ([Miriam.Hoosain@uct.ac.za](mailto:Miriam.Hoosain@uct.ac.za))  
Executive Director: Student Affairs ([Moonira.Khan@uct.ac.za](mailto:Moonira.Khan@uct.ac.za))

#### 4. INFORMED CONSENT

What type of consent will be obtained from study participants?

- Oral Consent  
 Written Consent  
 Anonymous survey questionnaire (covering letter required , no consent forms needed)  
 Other (Please Specify)

How and where will consent/permission be recorded? Written signed consent

Have you attached an informed consent form to your application?  Yes     No  
(Appendix 1 of this form)

#### 5. SPONSORSHIP OF RESEARCH

**If your research is sponsored, is there any potential for conflicts of interest? No**

If your answer is YES, please complete below

4.1 Is there any existing or potential conflict of interest between a research sponsor, academic supervisor, other researchers or participants?	YES	NO
4.2 Will information that reveals the identity of participants be supplied to a research sponsor, other than with the permission of the individuals?	YES	NO
4.3 Does the proposed research potentially conflict with the research of any other individual or group within the University?	YES	NO

If you have answered YES to any of these questions, please describe how you plan to address these issues (append to form)

N/A

## 6. RISK TO PARTICIPANTS

Does the proposed research pose any physical, psychological, social, legal, economic, or other risks to study participants you can foresee, both immediate and long range? (please select)

Yes       No

If yes, answer the following questions:

1. Describe in detail the nature and extent of the risk and provide the rationale for the necessity of such risks
2. Outline any alternative approaches that were or will be considered and why alternatives may not be feasible in the study
3. Outline whether and why you feel that the value of information to be gained outweighs the risks

1. N/A

2. N/A

3. N/A

I certify that I have read the Commerce Faculty Ethics in Research policy  
(<http://www.commerce.uct.ac.za/Pages/ComFac-Downloads>)



I hereby undertake to carry out my research in such a way that

- there is no apparent legal objection to the nature or the method of research; and
- the research will not compromise staff or students or the other responsibilities of the University;
- the stated objective will be achieved, and the findings will have a high degree of validity;
- limitations and alternative interpretations will be considered;
- the findings could be subject to peer review and publicly available; and
- I will comply with the conventions of copyright and avoid any practice that would constitute plagiarism.


Signed by:

	Full name and signature	Date
Principal Researcher/Student:	Matau Molahloe	18 July 2022

This application is approved by:

Supervisor		28 <sup>th</sup> September 2022
Assoc/Prof. Latif Alhassan		
Departmental Ethics Rep		3 October 2022

Questionnaire checklist on next page

CHECKLIST	SELECT
	<input type="checkbox"/>
Interview schedules / cover letters / questionnaires / forms and other materials used in the study are attached in separate files	<input checked="" type="checkbox"/>
Organisational consent letter / UCT student or staff approval letter	NA <input type="checkbox"/>
On your cover letter to your questionnaire have you included the following?	<input type="checkbox"/>
1. The following UCT Logo 	<input type="checkbox"/>
2. A sentence explaining the aim of the research	<input type="checkbox"/>
3. Sentences of a similar nature to below must be included in the cover letter or consent form:	<input type="checkbox"/>
This research has been approved by the Commerce Faculty Ethics in Research Committee.	<input type="checkbox"/>
Your participation in this research is voluntary. You can choose to withdraw from the research at any time.	<input type="checkbox"/>
The questionnaire will take approximately X minutes to complete	<input type="checkbox"/>
You will not be requested to supply any identifiable information, ensuring anonymity of your responses.	<input type="checkbox"/>
	OR

<p>Due to the nature of the study you will need to provide the researchers with some form of identifiable information however, all responses will be confidential and used for the purposes of this research only.</p> <p>Should you have any questions regarding the research please feel free to contact the researcher (insert contact details).</p> <p>4. Have you scanned in your signature for the last section of the form?</p>	<input type="checkbox"/>  <input type="checkbox"/>  <input type="checkbox"/>
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Appendix 1:

Signed participants form giving consent



Consent form

The role and effectiveness of DFIs in developing township economies

Hello, my name is Matau Molahloe, and I am conducting research towards a master's degree in development finance at the University of Cape Town. The nature of this study is exploratory in nature to gain familiarity and understanding of the role and effectiveness of DFI in developing SMMEs in the township thus promoting township economies.

This research has been approved by the Commerce Ethics in Research Committee.

Consent to take part in research

I..... voluntarily agree to participate in this research study. The choice to participate is mine alone. If I choose not to participate, there will be no negative consequence.

I understand that even if I agree to participate now, I can withdraw at any time or refuse to answer any question without any consequences of any kind.

I understand that I can withdraw permission to use data from my interview within two weeks after the interview, in which case the material will be deleted.

I have had the purpose and nature of the study explained to me in writing and I have had the opportunity to ask questions about the study.

I understand that participation involves answering semi-structured questions by the researcher

I understand that I will not benefit directly from participating in this research.

I agree to my interview being audio-recorded or written questionnaire.

I understand that all information I provide for this study will be treated confidentially.

I understand that in any report on the results of this research my identity will remain anonymous.

I understand that disguised extracts from my interview may be quoted in the dissertation

I understand that signed consent forms and original audio recordings will be retained in secure location, security arrangements and only researcher has access until one year after approval of the dissertation.

I understand that a transcript of my interview in which all identifying information has been removed will be retained for [one year].

I understand that under freedom of information legalisation I am entitled to access the information I have provided at any time while it is in storage as specified above.

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I understand that I am free to contact any of the people involved in the research to seek further clarification and information.

-----

Signature of participant

-----

Date

I believe the participant is giving informed consent to participate in this study

-----

Signature of researcher

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Date

**Appendix B: Interview Questions**

**Interview Questions for the Representatives of a DFI**

**SECTION A:**

1. Type of organisation  
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2. What is the mandate of the DFI/organisation you work for? And is there a particular focus to SMMEs?  
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3. What forms of support does the organisations provide to its clients?  
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4. Is there a particular focus to support township SMMEs?  
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5. Which sectors received the most support in the past 2 years? and why  
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6. What tools and mechanism are used to facilitate the DFI mandate?  
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.....
7. How much funding has the institution reserved for SMMEs?  
.....
8. How much funding has been reserved for SMMEs in the townships in particular?

.....  
9. How many applications have been processed for SMMEs over the past 2 years?  
.....

10. How many of those application where for township enterprises?  
.....

11. What is the average success rate (%) of application for SME funding in your institution?  
.....

12. What would you attribute the rate above to?  
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13. Are there special programs to aid awareness particularly in the township economy?  
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**SECTION B – Impact and effectiveness of DFIs**

1. How do you measure effectiveness of the tools and mechanisms mentioned above?  
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2. Are there any consequences or corrective actions where DFI support is found to be ineffective?  
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**SECTION C – General population of SMME vs Township SMMEs**

1. Does the entity differentiate between support for the township economy versus other economies/ small businesses not based in the township?

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2. Based on the data, have beneficiaries of support been able to increase their financial performance more for general SMMEs compared to Township SMME

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3. Is there more or less appetite for township economies from a DFI perspective? And why

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4. Is there a perception that township entrepreneurs carry a higher risk than other type small business owners?

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**SECTION D**

1. What do you think DFIs can do better support the township economy?

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## **Interview Questions for SMEs operating in the townships in Gauteng**

### **SECTION A: Demographic Information**

1. Please specify your demographic

- African black
- White
- Indian
- Coloured
- Other
- Prefer not to answer

2. In which category of SMEs does your firm fit in?

- Micro Business
- Small Business
- Medium Business

(We can refer to the definitions in line with the study for clarity in the interview)

3. How long has your company been operating?

- Less than a year
- Between 1 - 2 years
- Between 3 - 5 years
- Between 6 - 10 years
- 11 years and above

4. How many permanent employees do you have?

5. What is your highest level of education?

- Lower than matric
- Matric
- Certificate
- Diploma (Technical college or University of Technology)
- University degree
- Postgraduate degree
- Other

Where other please specify

6. Age of owner/s

7. Type/Nature of the business

8. What is the legal status of your business (Registered or No registered)

9. Which township/s does your business operate in?

10. What is your annual turnover/revenue?

11. Where are your business premises? (Example, home, outlying business area, Industrial area, Agri-land other)

**SECTION B – Detailed questions**

12. Do you have knowledge of DFI and other government agencies providing support or interventions to township enterprises. If so, what do you know.

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13. How is/was your business funded? (start-up cost and working capital)

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14. Which institutions did you approach for financing your business and why?

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14a. If you have not approached a formal institution for financing, what is the reason for this?

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15. State unique challenges of your business?

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15a. Please state if these challenges are unique to township entrepreneurs only in your view?

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16. Have you received support from DFIs or any other government institution? Yes, or no?  
(Funding or other)

if, yes

Which institution provided this support?

What kind of support did you receive?

If financial, how much was provided

How much was taken out?

What was the tenor of the loan?

What was the interest rate charge?

What was the reason for the loan?

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17. Did you receive support/funding from the private sector such as banks and micro-financiers?

if, yes

Which institution provided funding?

What kind of support/funding did you receive?

How much was taken out?

What was the tenor of the loan?

What was the interest rate charge?

What was the reason for the loan?

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18. For financial assistance, what kind of obstacles did you experience in the application process?

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19. Are you aware of non-financial assistance from DFIs and other government agencies?

.....

20. Did you receive non-financial assistance from DFIs and other government agencies?

If yes on the above. What support did you receive – e.g.) technology, financial literacy training, business planning etc.

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21. What was your experience of your support of DFI intervention

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22. What was your experience of the financing received?

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23. Would you say the support was effective?

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234a. If yes, what did you deem to be effective (i.e., any potential benefits)

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23b. If no, why did you think it was not effective (i.e., any potential challenges)

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24. Based on your answers above, do you think after care support is a necessity?

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25. Do you think the government needs to do more to support the township economy and why?

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26. How would you want the government to support your business?

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