



Research Article

Strategic Preferential Procurement Policy for Localisation and Inclusive Growth for Micro Small Medium Enterprises (MSMEs) in Gauteng Province

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Abstract: The study aims to develop interventions to address the low productive capacity and competitiveness levels of township Micro Small Medium Enterprises (MSMEs) to enable meaningful participation in the mainstream economy. Most township firms continue to be informal and underdeveloped. Despite countless interventions by the development finance institutions, most township enterprises remain perpetual survivalists. The study is anchored upon the neoliberal theory, which emphasizes value for money and market efficiencies in procurement, as well as interventionist theories promoting the inclusion and participation of MSMEs in business, and advocating for the localization of products through various policy interventions. The researcher adopted a mixed-method approach to gather primary and secondary data. Secondary data was used for analysis and supported by the primary information or empirical evidence. The secondary data enriched the research content and complemented the primary data. Databases and reports on township suppliers from the Gauteng Provincial Treasury (Procurement Division) and Gauteng Department of Economic Development helped determine the extent of MSMEs' access to development and financial support opportunities. The study found that the high informality level of township businesses, low level of development, poor economic infrastructure, and lack of access to finance hinder MSMEs' participation in public procurement. Programs and products offered by government agencies do not adequately respond to public procurement challenges facing MSMEs, e.g. product testing and accreditation. The high barriers to entry due to complicated administrative processes and procedures continue to deter MSMEs from participating in the mainstream economy. The Development Finance Institutions (DFIs) were found to be a challenge due to a mismatch between the resource structure to drive economic development and the products offered. The study recommends that to increase the participation of MSMEs in public procurement, there needs to be a targeted growth continuum strategy that tracks interventions from the beginning to the end. Additionally, there needs to be a shift from a quantitative approach with minimal impact to a customised one with qualitative, tangible and tradable products and skills aimed at increasing participation of MSMEs. Furthermore, the political will is required to address the resource mismatch, repurpose resources, or develop specific products by the well-resourced Development Finance Institutions to suit the material conditions of township MSMEs with lesser stringent measures.

Keywords: MSMEs, DFIs, set-asides, enterprise supplier development, public procurement, localisation, inclusive growth

1. Introduction

Globally, public procurement continues to be a tool used to address a myriad of issues, including social inclusion, inequality, industrialization through local content production, infant industry protection, and promotion of new products, innovation, and improved economic participation. In other countries, beneficiaries are required to source and procure from local producers, thereby increasing local production (Felipe & Rhee, 2014). Corvaglia and Li (2018) concur that globally, there is an acknowledgment of public procurement being an instrument of inclusive and shared growth. While the use of public procurement to stimulate inclusive growth is acknowledged, Micro, Small, and Medium Enterprises (MSMEs) worldwide find it difficult to penetrate the supply chain and become credible suppliers. Public procurement struggles to realise its mission to create public value due to a narrow focus on the cost of procured goods and services (Malacina et al., 2022).

On the contrary, Small and Medium Enterprises (SMEs) in countries like India contribute nearly 30 percent to the Gross Domestic Product (GDP) and are responsible for over 110 million jobs (Dwivedi, 2022). In China, SMEs contribute nearly 60 percent to the country's GDP and 79 percent of total employment (OECD, 2018). This shows that creating an enabling environment for small firms can reduce unemployment, inequalities, and poverty (Naape, 2023). Conversely, there is a worldwide trend to liberalise public procurement, which allows equal market access for well-established global players and domestic businesses (Sen, 2019). The proponents of Public Procurement liberalization led by the World Trade Organization (WTO) argue that open competition in public procurement offers the government benefits such as quality, skills, and competitive prices, rather than a system that promotes corrupt practices and inefficient allocation of resources (Lember et al., 2014).

Furthermore, the liberalisation of public procurement through the Public Procurement Agreement (PPA) can potentially defeat the empowerment and inclusive initiatives aimed at closing the inequality gaps, further exacerbating the current structure of the economy that favours dominant economic powers. While most developing countries utilize public procurement to boost local production and foster economic inclusion, advocates of public procurement liberalization argue in favor of inclusive or open competition to access market opportunities. Fundamental to the WTO's big push for the liberalisation of public procurement is the concept of 'double standards'. Some members of the PPA, such as China, continue to benefit from open competition while deterring other countries from accessing their public procurement markets (Chen, 2013). This policy contradiction also finds resonance in the "Buy American goods", which violates the Global Procurement Act (GPA) principle and promotes unequal power relations. The neo-classical approach advancing the liberalisation of public procurement fails to consider catch-up programs of developing countries aimed at closing poverty gaps, inequality, and high levels of unemployment, instead, it places all countries on an equal growth path. The purpose of this paper was on leveraging public procurement for the realisation of inclusive and shared growth in Gauteng Province. The paper covers the objectives of the paper, literature review, methodology, study results, the discussion of results and the conclusion.

2. Rationale of the study

This paper is based on the study focusing on leveraging public procurement for the realisation of inclusive and shared growth in Gauteng province and South Africa at large. It is based on the premise that despite public procurement set-asides for township businesses over the past fifteen years, there is still negligible participation of MSMEs in the mainstream economy. Broadly, the paper focuses on the public procurement landscape in the Gauteng province and the limits to economic inclusion. Despite the set-aside policy tool to increase economic participation, public procurement continues to benefit well-established businesses, making it difficult to reverse the poverty, unemployment and inequalities faced by the majority of the population. While many studies highlight the high levels of informality and underdevelopment within township businesses, there seems to be a lack of specific interventions addressing these deficiencies. The study explores the challenges and potential interventions necessary to increase economic inclusion.

3. Literature review

3.1 Public procurement in the South African context

Before the dawn of democracy in South Africa in 1994, public procurement focused on well-established large companies that favoured minority white-owned businesses. The South African government faces the challenge of balancing the allocation of limited funds, and the appointment of contractors among former government beneficiaries and previously disadvantaged individuals (Ngcamphalala & Amber, 2016). Because of stringent public procurement measures, new players or companies owned by new market entrants find it difficult to participate (Amber, 2016). Post 1994, the South African government used public procurement as an instrument to address socio-economic injustices of the past by developing inclusive policies aimed at increasing participation of the previously disadvantaged groups. While the democratic government in South Africa adopted policies that promote socio-economic objectives, MSMEs still struggle for recognition in South Africa (Hlakudi, 2012). Public Procurement spending in South Africa was sitting at 15 percent of the GDP in the years 2021 and 2022 (International Monetary Fund, 2023).

Despite various interventions to increase the participation of MSMEs in public procurement, including set-asides, the uptake from township-based enterprises remains low at only 12.38%, instead of the 30% target (Gauteng Provincial Treasury, 2021). This low uptake can also be attributed to low-value goods and services, while well-established non-township businesses continue to dominate high-value end products. This can be attributed to the underdevelopment of most township businesses, compounded by the resource structure that continues to favour and support the apartheid geography due to stringent lending measures. In his State of the Province Address, Gauteng Premier Panyaza Lesufi announced a 60% set-aside for township enterprises despite the inability to meet the previous goal of 30% (Gauteng Provincial Legislatures, 2023). While the announcement bodes well for the township enterprises, the enforcement remains lacklustre because the supply chain divisions continue to rely on their traditional suppliers. Compounding the poor participation of MSMEs in public procurement is the lack of big-push support to close the development gaps of township enterprises.

3.2 Barriers to public procurement participation

Complex regulations and processes and the power relations between micro and small suppliers and buyers relegate township businesses to the economic fringes. Philip (2012) contends that the market is horizontally and vertically controlled by well-established businesses that own and control the entire value chain. There is also a pure lack of a concrete strategy to increase the productive capacity of small and micro firms, while the lack of products earmarked to increase product testing, accreditation, and provision of cutting-edge industrial instruments remains a glaring feature of township MSMEs. Development finance institutions, by design, were not intended to provide the skills and capacity to make township businesses competitive, but to remain survivalists (Guliwe, 2022). DFI's product offerings are limited to a few low-level interventions, which are less focused on enhancing the productive capacity of MSMEs through the provision of cutting-edge machinery, innovation, and product testing. Instead, they resemble a structured pipeline aimed at supporting MSMEs through a handholding process (Gauteng Enterprise Propeller, 2022).

Institutions or structures that provide product testing and accreditation services are based in metropolitan areas, which makes accessibility difficult for township-based enterprises. Compounding the low productive capacity of township micro and small firms, is the contention amongst business forums, instead of being a collective voice representing the diverse interests of township businesses (Gauteng Department of Economic Development, 2022). Organising township micro firms along the lines of industrial clusters (producing similar products) can potentially reduce the high cost of product testing and accreditation and increase the economies of scale necessary to compete for larger contracts; attract investment, and increase participation of township firms (Gauteng Provincial Legislature, 2022). This fragmentation of township business forums defeats the power of a collective voice to address the many challenges facing micro and small firms, such as access to public procurement and corporate market opportunities. Most township businesses also produce or manufacture products from their backyards, as the high cost of industrial economic infrastructure and the cumbersome government laws that promote an open market or neo-liberal paradigm hinder the realisation of inclusive economic growth (Ansari, 2016). These challenges are compounded by the crumbling energy infrastructure in South Africa and rising crime. At the same breath, the cost of living is high, which has reduced the productive capacity of MSMEs (Department of Small Business Development, 2021).

3.3 The state of resource structure to drive enterprise and industrial development

The current incentive structure in South Africa favours neo-liberal global liquidity with limited or no growth prospects for investment in the long-term industrial program (Ansari, 2016). This makes it difficult for most township firms to leapfrog from the current development state to a desired state that resonates with the material conditions of underprivileged businesses. Further compounding this is the business community's veto over policy through its ability to hold back investments. This only adds to the low participation of township businesses in public procurement, as does the current structure of DFIs, which continue to pursue a pro-market agenda with its risk-averse nature and stringent lending requirements that prevent township businesses from participating in the mainstream economy. The fact that National Development Finance Institutions (NDFIs) own about 91% of all DFI assets, compared to the Provincial Development Institutions' 1.3%, further compounds the financial challenges MSMEs face (National Treasury, 2018). The structural positioning and the stringent lending requirements of the DFIs make it difficult for township MSMEs to access funding. It is worth arguing that without repositioning and repurposing the NDFIs to consider reducing the lending requirements to MSMEs from townships or disadvantaged communities, very few enterprises from disadvantaged communities would benefit and contribute meaningfully to the mainstream economy.

3.4 Argument for and against the liberalisation of public procurement

There is an acknowledgement that public preferential procurement is a tool to stimulate the local economy, increase economic participation and drive industrialisation in developing and developed countries (OECD, 2019; Corvaglia & Li, 2018). What has become common in most countries (in terms of the application of public procurement) is the creation of a platform to increase small businesses' participation in various forms, such as setting aside or reserving certain purchase orders for small players (UNIDO, 2020). It is worth noting that most government departments still subtly protect public procurement (Fountoukidis et al., 2022). A case in point is that during COVID-19, most government departments resorted to leveraging public procurement to stimulate the domestic economy (Gereffi, 2020). Proponents of public procurement preferential treatment advocate for redressing economic injustices and inequality. While this strand of literature corroborates the inclusive nature of public procurement, the pro-market theory challenges the ring-fencing or provision of procurement set aside. They argue that public procurement should be liberalised and contested fairly and equally by local and international businesses. The main argument espoused by the pro-market proponents is that competition plays a crucial role in public procurement and enhances the efficient allocation of resources (Fountoukidis et al., 2022). The pro-market approach of public procurement is also advanced by the Global Procurement Act (GPA) which advocates for the liberalisation of public procurement.

Chang (2002) challenges this notion by arguing that rich economies use industrial policies that go against the neo-liberal orthodoxy but make it difficult for developing countries to pursue a similar approach. Further, it is argued that developed countries continue to use economic protection and subsidize their businesses while preventing developing countries from doing the same (Chang, 2002). An example is the United States of America's push to "Buy American Goods" (Cravero, 2017), whereas China has made it difficult to penetrate its public procurement market despite being a member of the World Trade Organisation (Global Public Procurement Act) (Chen, 2013). Larger businesses that circumvent preferential procurement laws while using wholly owned subsidiaries and corporate arrangements are endemic in China (Chen, 2013). Conversely, state-owned enterprises (SOE) compete for the preferential procurement earmarked for MSMEs. Similarly, the US federal government pushed for an increased purchase of domestically produced goods (CBS, 2021). In addition, the Australian government advocates for the procurement or purchasing of indigenous goods while being a member of the WTO's Agreement on Government Procurement (Cutcher et al., 2020). Although the Global Procurement Act does not penalise members contravening this act, this 'double standard' continues to hit harder on developing economies.

4. Theoretical framework

4.1 Neoliberal theory

The market-led argument is based on the idea of market efficiency, value for money, skills, and quality products

(Borvic, 2016). It assumes that preferential procurement perpetuates the sub-optimal allocation of resources and represents a welfare loss for the economy of the relevant state. The market-led policy agenda is aligned with the neo-liberal policies that advance trade openness (Górski, 2016). These policies are based on the premise that transparency and equal participation in public procurement promotes efficient resource allocation, skills, value for money and savings (OECD, 2018). The neoclassical economic theory emphasises the market is an ahistorical phenomenon that functions as a universally applicable mechanism for efficient resource allocation (Sadiqqi, 2015). It is premised on the idea that state or public sectors are inefficient and that only markets and private sectors can create employment and welfare.

This school of thought challenges the structuralists or interventionist approach to protecting and ring-fencing public procurement. It argues that the government lacks the ability to deliver and allocate resources efficiently. The market-led approach to public procurement thus advocates for equal competition for businesses. It advances less or no state intervention in the market and is premised on the trade liberalisation theory supported by the WTO (Saddiqi, 2015). The neoliberal theorists argue that public restrictions in competition are among the sources of distortion in free-market dynamics that are most pervasive and difficult to combat. It places competition at the centre of the fight against public restriction (Sanchez-Graells, 2018). The neoliberal theories thus argue that public procurement needs to take place in competitive markets (Sanchez-Graells, 2018). Keulemans and Van de Walle (2017) agree the neoclassical model of public procurement (based on cost effectiveness) is viewed by its proponents as the best means of achieving fair, transparent, and unbiased tendering processes. However, Junior (2015) claims that discrimination that favours domestic suppliers risks price-fixing, corruption and reduced investments in Research and Development (R&D).

4.2 Interventionist theory

State-led approach measures for redress always form part of procurement regulations, especially those that promote small businesses and marginalised groups. Moreover, the state-centric approach promotes MSMEs' inclusion and participation, and is known for providing set-asides for small enterprises. Central to the state-centric approach is the promotion of localisation or domestic products through various policy interventions. The traditional school of thought argues that economies' progress, specifically those of poorer countries, will not happen if left to the whims of the market (Chang, 2014). The development of globally inclusive MSME-friendly policies aimed at addressing the exclusion of small businesses is an acknowledgment of market failure (Flynn et al., 2015). They argue that state intervention is significant and can be promoted through various tools, set-asides or lots. Some newly industrialised countries like Thailand and Taiwan region placed small and medium enterprises at the centre of industrial development, supported through state intervention mechanisms (Maleka, 2017).

Public procurement is also used for the protection and advancement of human rights. Ortega (2018) challenges the notion of international public procurement's myopic focus on efficiency and value for money by protecting against anti-competitive behaviour and exclusion rather than considering other social factors. An interventionist approach to public procurement is ultimately endemic in most democratic societies and advocates that local content development be stimulated, promoting 'buy local' initiatives, fairness and transparency (McCue et al., 2015). In both the UK and the US, public procurement is also used to prevent products from being bought from countries involved in human rights violations, including child labour, human trafficking, and other forms of modern slavery (Ortega et al., 2015).

5. Methodology

The researcher conducted mixed-methods research, focusing on MSMEs benefiting from provincial preferential procurement set-asides for township businesses, and the development support offered to improve the efficiency and quality of products. The researcher also explored the perspectives of various stakeholders and experts in the field of public procurement and the enterprise development space. The study targeted business analysts, researchers, policymakers, supply chain managers and development practitioners. These respondents provided diverse views based on their experiences in their space. This approach assisted the researcher in ascertaining whether the current enterprise development model is responsive to small businesses' needs. For this study, the researcher collected primary (interviews) and secondary data. For primary data collection, a semi-structured questionnaire was developed for quantitative and interviews were utilised for qualitative data collection. The researcher also attempted to investigate variables, like small

firms' rate of accessibility, level of inclusivity and exclusion, the set-aside policy, distribution of public procurement amongst transversal groups, dominant sectors, and the level of small firms' contribution to regional economic growth. The study used the convenience sampling technique due to the researcher's proximity to the research universe.

6. Data analysis and discussion of study finding

6.1 MSMEs participation in public procurement

The findings from the survey unearthed three major themes, namely, MSMEs' level of participation, the political will, and the set-asides and measures taken to accelerate enterprise supplier development and skills.

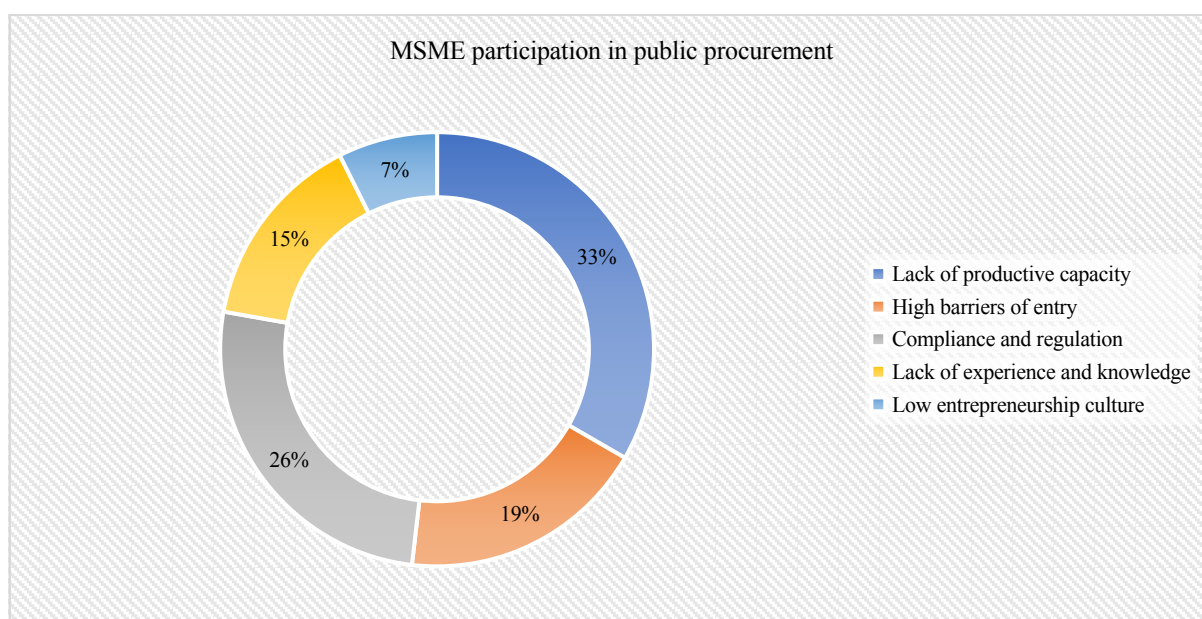


Figure 1. MSME participation in public procurement

Source: Own calculations (2022)

Figure 1 indicates that 33% of the respondents cited the lack of productive capacity as a major challenge hindering MSMEs' increased participation in public procurement. Another 26% pointed at compliance as a significant challenge prohibiting participation. Moreover, 19% of respondents cited the high barriers to entry as a primary impediment to MSMEs' participation in public procurement, while low entrepreneurial culture was mentioned by 7%. While the significant barriers to entry are acknowledged, the inability of the state to provide economic infrastructure for MSMEs to thrive was overlooked. Compounding the economic infrastructure as a critical barrier for business expansion is the pro-market approach, characterized by an open tender system, instead of the provision of industrial hubs with developmental rates for MSMEs. The neo-liberal approach to economic infrastructure allocation by municipalities favours well-resourced established businesses. Chamon et al. (2022) suggested a three-pronged approach reform agenda supported by complementary policies could be pursued to unlock product markets for new businesses. This includes reforming State-Owned Enterprises and DFIs and rethinking their business model. There is also a need to leverage innovation to allow the private sector in strategic sectors while reviewing the regulatory architecture and enforcing competition policy to enable access are key to transforming the economy.

6.2 Political will to implement

The new Spatial Planning and Land Use Management Act (SPLUMA) advocates for equal access to economic

infrastructure owned by municipalities with fewer or no prospects for MSMEs to acquire operational spaces. SPLUMA is the antithesis of the Gauteng Township Development Act, which compels municipalities to reduce red tape and assist MSMEs to unlock economic opportunities.

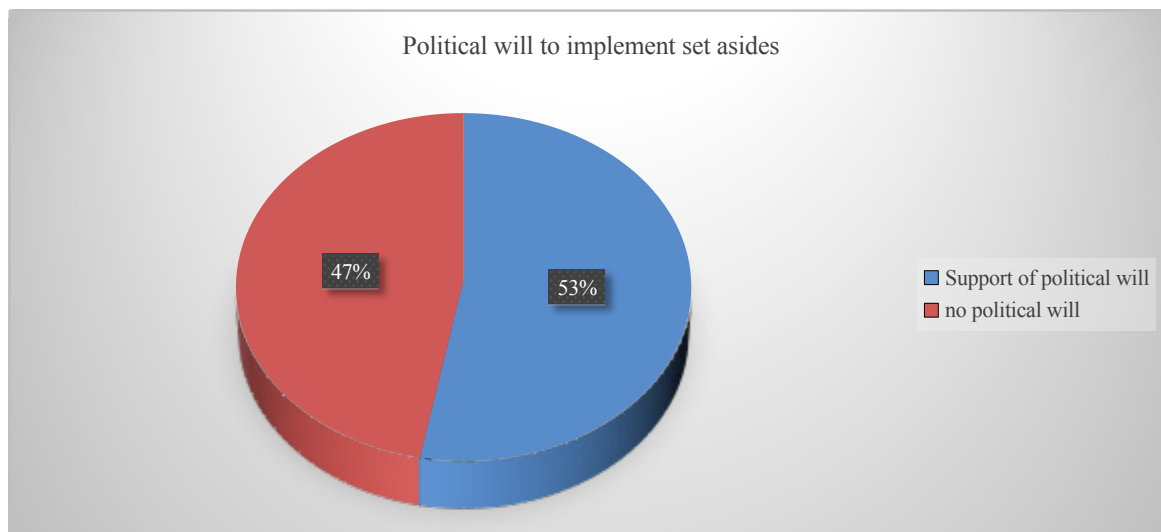


Figure 2. Political will and the implementation of set-asides

Source: Own calculations (2022)

Figure 2 indicates that 47% of respondents felt there was a lack of political will, while 53% believed that the political will existed, though the execution and enforcement of public procurement policies was the problem. Collins (2018) argues that public procurement benefits politicians and those who are connected. As such, it has been suggested that public procurement should be open and competitive to prevent corruption and inefficiencies while promoting value for money, skills transfers, job creation, and economic growth (OECD, 2015). Proponents of market-led public procurement advocate for openness, quality of products, value for money, and market efficiencies (Borvic, 2016; Górski, 2016). Some respondents felt that the passing of certain policies demonstrated the government's political will, but that there was a lack of administrative will from officials in different public institutions.

Certain goods and services targeted procurement from companies owned by designated groups. Critics of set-aside policies argue that reserving public procurement for certain target groups is discriminatory and counterproductive (Collins, 2018). McKinsey and Company (2022) argue that local content policies could limit sourcing options for products or services from more competitive markets. This view is also supported by the pro-market theorists who advocate for openness in public procurement. Conversely, those who support public procurement set-asides argue for the equitable distribution of resources, increased economic participation and industrialization, and changed ownership patterns (Brown & Girth, 2018). However, public procurement policies that promote MSMEs would not have met specified requirements without affirmative action interventions (Cravero, 2017). Over 23% of respondents cited a lack of supplier development, while 13% argued that support interventions from DFIs do not address market demands, resulting in a skills mismatch.

Moreover, the pre-qualification criteria for the advancement of designated groups are applied to tenders below R30 million, with demand management plans targeting procurement from these groups. Some respondents argue that political will exists, but that MSMEs suffer from an entitlement mentality and do not want to comply. Some believed that, compared to the previous dispensation, there seemed to be a gradual buy-in from political principals. They argued that the political will to increase MSME participation is reflected in policy, including preferential procurement regulations, but these lack enforcement and accountability in the case of non-compliance. Compounding the low level of MSME participation in public procurement is the fact that various departments continue to surrender huge budgets to the provincial treasury due to poor implementation and lack of capacity to spend. Some respondents argued that political

will be compromised by infighting within the ruling party, hence the lack of enforcement or offtake agreement across departments.

6.3 Measures to accelerate enterprise supplier development and skills

Heyn and Luke (2018) argued that suppliers are still struggling with the skills needed in the supply chain. This corroborates with the strand of literature that complex procedures and processes continue to hinder MSMEs' participation in the mainstream economy. Philip (2012) argued that vertical and horizontal structures make it difficult for MSMEs to break the barriers to entry. During the survey, respondents had mixed views on measures to accelerate supplier development. Some respondents argued there are measures, while other respondents refuted their existence. About 52% supported the existing measures and suggested improvements, while 17% were against the existing measures, and 35% chose not to respond. Most measures geared towards increasing spending on MSMEs included providing non-financial support to promote supplier development. Respondents also called for contracted banking institutions in the Gauteng provincial government to provide product development support and enterprise development, including skills development as part of the Master Service Agreement. Part of these measures is to ensure the realisation of Broad-Based Black Economic Empowerment (BBBEE) and Corporate Social Responsibility. Support interventions to accelerate supplier development tend to be minimal, generic, unfocussed and unsustainable, and do little to enhance the competitiveness of existing products from township enterprises. Instead, a shotgun approach is usually taken with MSMEs, hence the need for customised and structured solutions that consider the uniqueness of each business. There needs to be a shift from the quantitative approach that focuses on big numbers rather than the quality and impact outcomes.

Most government entities include key performance indicators (KPIs) in their performance plans, which measure the allocation of a certain percentage of the budget to supplier development, skills development, and enterprise development. It is worth noting that supplier development should focus on existing products and necessary steps aimed at improving quality and competitiveness, rather than just generic targets. This should be linked to a structured pipeline of products or enterprises with stages of development and a clear exit strategy, for example, readiness to supply and access the market. Some departments have preferential procurement strategies, and departments like the Gauteng Provincial Treasury (which plays an oversight role) assist with skills and supplier development initiatives. However, the lack of a specific and tailor-made approach to specific products and services continues to undermine and compromise the program objectives. Respondents concur that there are no clear support measures, and it appears various departments and entities find it easy to exclude MSMEs based on their inability to comply with procurement requirements. However, respondents stated that supplier development is enforced through the Department of Trade and Industry and Competition in terms of BBBEE Act 53 of 2003 (BBBEE Act), as amended, and the Codes of Good Practice on broad-based black economic empowerment. It forces all government departments to comply with the requirements as gazetted; however, departments' performance appears to be minimal.

6.4 Approach to a new product-led industrialisation path

In most cases, interventions to stimulate local production and industrialization in South Africa tend to be sporadic and piecemeal, and continually under-resourced. There is also a lack of an integrated structured approach that can create sustainable and competitive enterprises. Product-led industrialization will be premised on the idea of clustering micro-producers to ensure improved production quality and compliance through product testing, industrial machinery upgrades, and the provision of economic infrastructure and market access. Central to industrial clustering and the provision of economic infrastructure is the establishment of industrial districts. Because of these short-term interventions, enterprises continue to suffer exclusion from the mainstream economy. A model or approach to create sustainable enterprises has been developed.

The MSME Growth Diagnostic Tool below is used to address productivity gaps and an inability to transform the current economic structure. Low levels of investment in R&D, accreditation, and product certification to bridge the development and competitive gap appear to be a serious problem. Conversely, in South Korea and Brazil, a major portion of development support gets allocated to developing productive skills geared to stimulate the local production of goods and enhance export competitiveness. The weak local content and industrial policies tend to slow

the development linkages in terms of the range of suppliers sourced locally and local value addition (Fessehaie, 2012). Institutions designed to provide and stimulate productivity of small and micro enterprises appear to be inaccessible and unaffordable, hence the need for government to help in the form of discounted rates and incentives. Local content policies need to be matched by industrial and business development policies, as well as high domestic capabilities (Morris & Fessehaie, 2014).

Morris et al. (2011) observed an association between low levels of industrialization and high dependency on commodities was-to a greater extent-determined by the absence of capabilities in commodity- or mineral-resource-dependent economies. The diagnostic tool will assist MSMEs in moving from being distributors of first-economy goods and services to becoming sustainable manufacturers positioned to increase economic participation. This view resonates with the product-driven industrialisation path pursued in South Korea and Brazil. It will assist MSMEs to transcend from the production of simple to complex and high-value products and diversify products oriented toward export-led economic growth. A new product development approach for township enterprises would assist in reducing the concentration of resources and inequality since concentration increases dividends and capital gains to the wealthy (Khan & Vaheesan, 2017). The study proposed a diagnostic tool to facilitate the support for MSMEs.

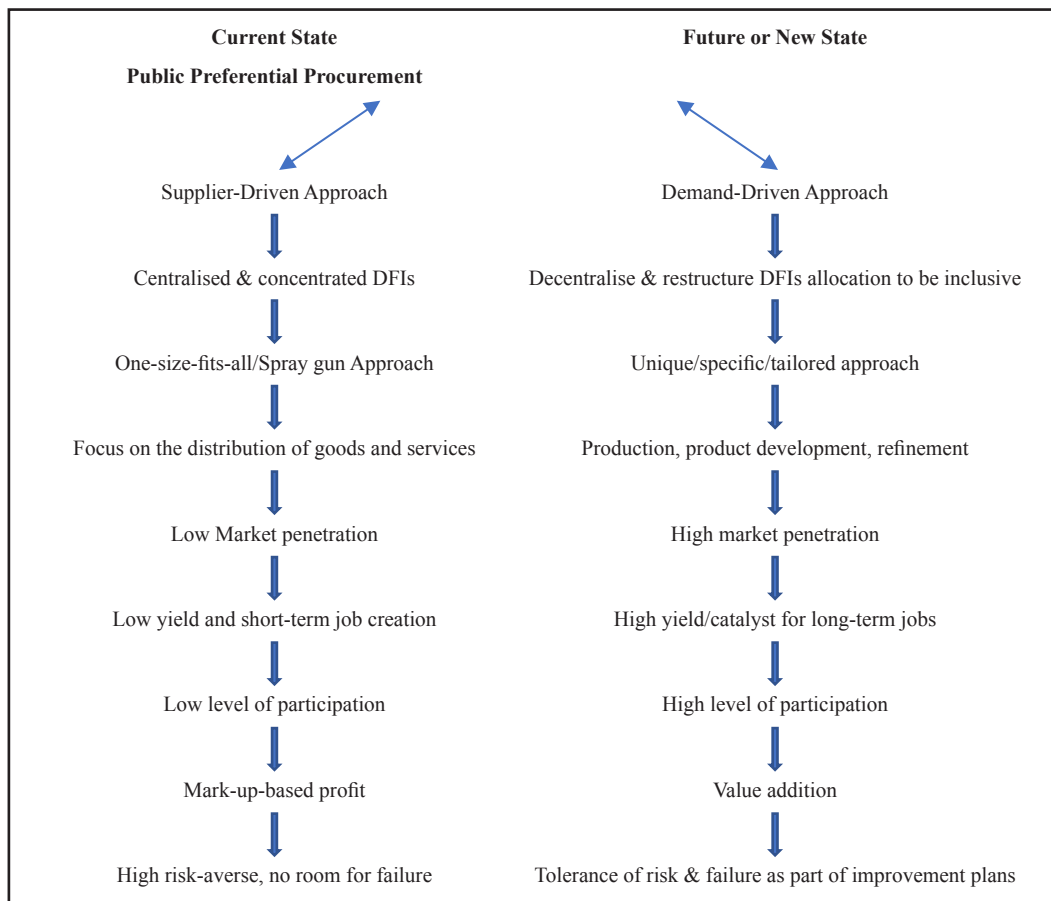


Figure 3. Proposed MSME Growth Diagnostic Tool

Source: Guliwe (2022)

The diagnostic tool (Figure 3) presents the challenges MSMEs experience and proposed sustainable solutions (future state) to ensure inclusivity and shared growth based on the above approach and the proposed industrial cluster model, which aims to bring together micro and smaller producers, assess the productive capacity of MSMEs, improve economies of scale, quality assurance and promote access to markets or larger contracts. This model has the potential

to increase the participation and competitiveness the township-based enterprises. The agglomeration approach has huge benefits, such as discounted rates of product testing, bulk buying, and an increase in the scalability of products to access markets that continue to be the domain of well-established businesses. In addition to this, MSMEs would be able to move from low-value to high-value addition.

6.5 Gauteng township procurement spending

Public procurement spending as a tool for inclusive economic growth in South Africa is supported by section 217 of the Constitution of the Republic of South Africa (108 of 1996), which provides for categories of preferences when allocating contracts to previously disadvantaged groups (Bolton, 2016). This section empowers entities or organs of the state to set up policies that provide for categories of preferences to ensure increased participation of the marginalized groups in the mainstream economy (Department of Small Business Development, 2021). The section below provides a deeper insight into the beneficiaries of public procurement in the Gauteng province. It also assists in understanding the patterns of spending and the position of township enterprises within the public procurement landscape. It gives an indication of why public procurement spending continues to benefit big businesses and the low participation of the transversal groups within the public procurement value chain.

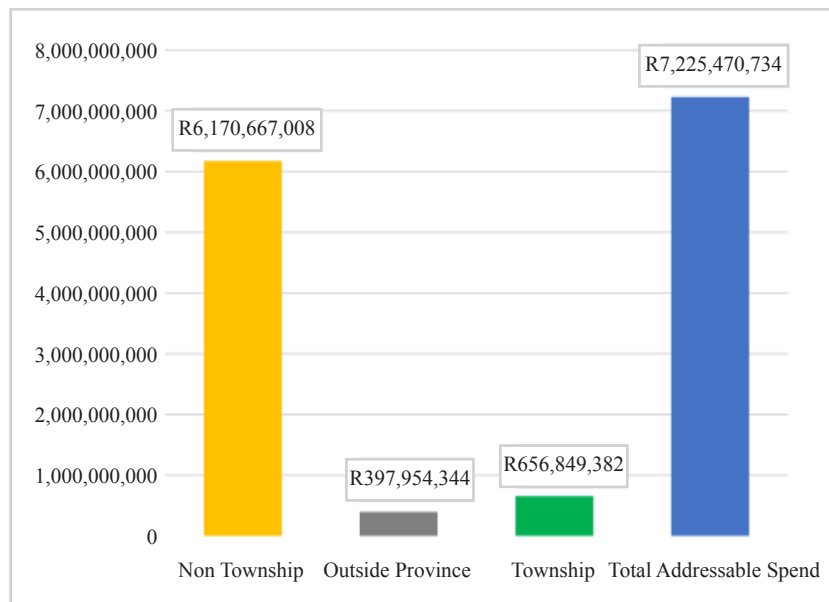


Figure 4. Procurement spending between township and non-township businesses
Source: Gauteng Provincial Treasury (2021)

Figure 4 indicates that public procurement continues to benefit mostly non-township businesses while township businesses experienced a low level of participation. This mirrors the broader societal problems of inequality between the rich and the poor, hence the need for a collective effort to invest in developing productive and tradable products (Gauteng Department of Economic Development, 2016). The literature on public procurement concurs that MSMEs are under-represented in public procurement based on their size, thresholds, and level of development (Tammi et al., 2014).

6.6 Distribution of public procurement in Gauteng province

Additionally, the researcher(s) went further to focus on the analysis and discussion of the distribution of public procurement in Gauteng Province and the results are as shown on Figure 5 below and the discussion thereafter,

Public procurement remains concentrated in the central corridor or Joburg region. Non-township businesses tend

to be the major beneficiaries of public procurement spending in Gauteng (at R6,000,000,000 compared to R646,849,382 for township businesses and R460,000,000 for those outside of the province). This procurement gap between the township and non-township enterprises confirms the low level of production from township businesses and the unequal resource allocation bias towards well-established businesses with low risk.

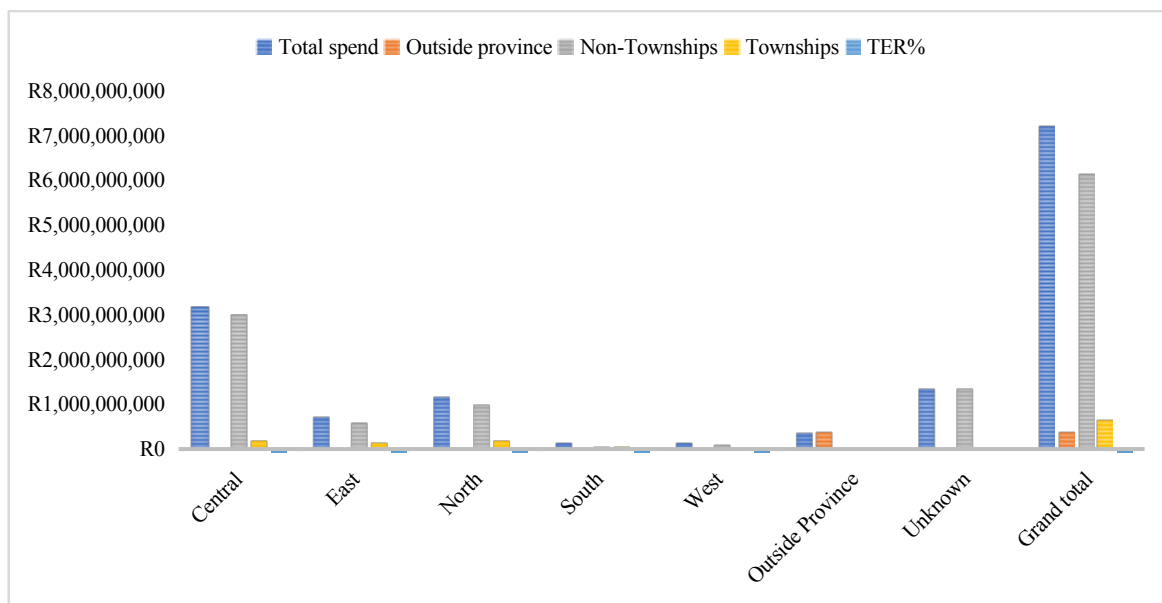


Figure 5. Regional spread of public procurement spending

Source: Gauteng Provincial Treasury (2021)

6.7 Spending per product within the Gauteng provincial government

The northern corridor (Tshwane region) is the second greatest beneficiary of township spending, followed by the eastern region (Ekurhuleni). While public procurement favours the Johannesburg region, it benefits mostly well-established non-township businesses. Township spending in the western and southern corridors appears to be high (46.13% and 30.19% respectively for the western corridor against the annual target of 12.50% for the southern corridor) though insignificant compared to the big metros (Gauteng Provincial Treasury, 2021). This also confirms the low level of participation and high unemployment in the West Rand and Sedibeng regions. Thus, despite significant procurement share in favour of metropolitan areas, public procurement spending to township enterprises remains insignificant. Below is Figure 6 which speaks to priority product spending for Gauteng Province,

Public procurement spending in the Gauteng province tends to benefit the 22 highest priority products, including transport, project management (professional consultation), and security services (Gauteng Provincial Treasury, 2021). Sectors and products with the most budget, including transport, project management, and security services, continue to be dominated by well-established businesses. The low level of township business participation, especially in priority products, mirrors the DFIs’ resource mismatch and the centralisation of regulatory bodies that are supposed to assist MSMEs in favour of well-established minority businesses that became large businesses during the apartheid years. Buthelezi et al. (2019) found that nearly 71% of South Africa’s sectors have distinct markets with dominant firms. The dominance of well-established businesses in products with high-value addition suggests that the product market structure is a major contributor to weak economic performance and inclusion (Chamon et al., 2020).

Similarly, suppliers of essential and scarce goods are able to charge excessive prices (Kaleme & Moeketsi, 2020). Recent policy research gaps show that, in many instances, procurement legislation provides general recommendations, subjecting it to individual supply chain practitioners to decide (Harazika & Jena, 2017; Kumar, 2020). While MSMEs appear to be victims of market abuse, the government, as a recipient of the scarce products, bears most of the brunt

due to higher prices determined by the sole provider of goods and services. Again, evidence points to a correlation between market concentration and lower entrepreneurship, private investment, and growth compared to South Africa’s global peers. Therefore, consumers pay higher prices for their goods and services while being excluded from jobs and entrepreneurship opportunities.

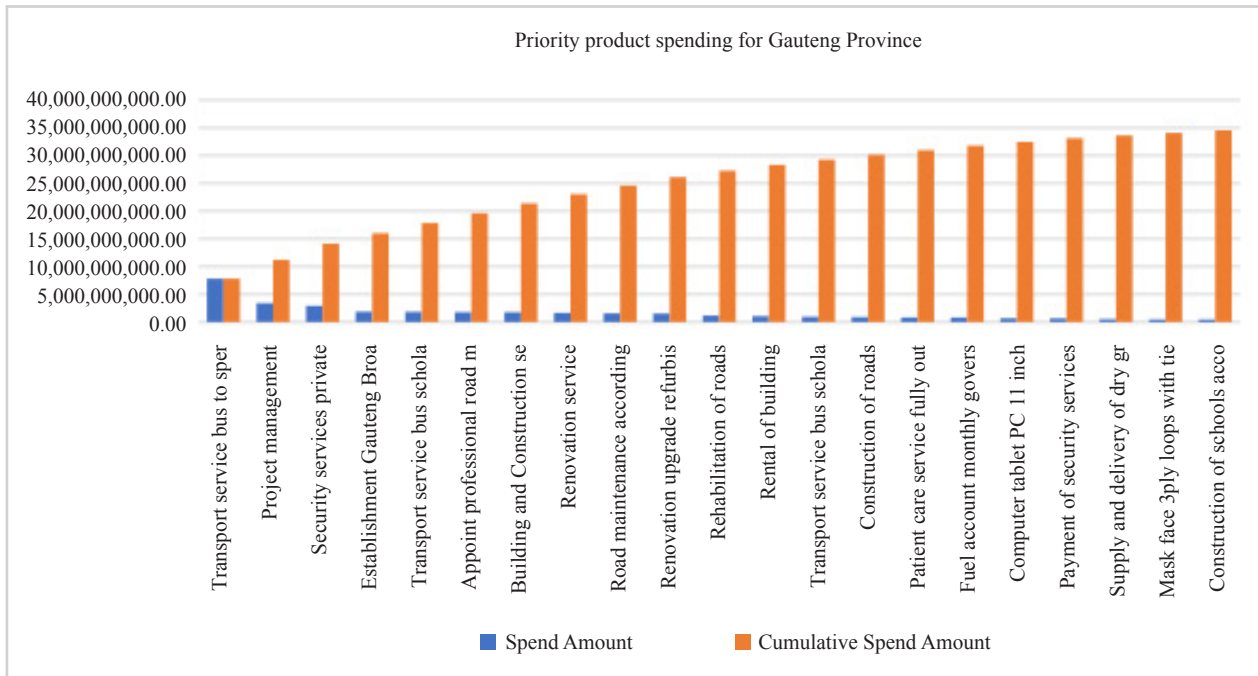


Figure 6. Spending per product within the Gauteng Provincial Government

Source: Gauteng Provincial Treasury (2021)

Thakoor (2020) suggested three main reasons for South Africa’s product market concentration. First, the apartheid sanctions led to the creation of a concentrated market structure that has not been transformed since the enactment of the Black Economic Empowerment (BEE). Secondly, government policies protect existing industries from market concentration. Third, incumbents tend to engage in uncompetitive behaviors to preserve their market share. The Competition Commission of South Africa (CCSA) has shown evidence that some firms resorted to mergers and exclusionary behaviour that prevents competition (CCSA, 2017; 2018). Surveys conducted on Small Medium Enterprise (SME) perceptions in South Africa reveal perceptions of strong barriers to entry, access to finance, insufficient economic infrastructure, and regulatory burdens (Thakoor, 2020). In addition, the government’s inability to transform the DFIs’ apartheid structure to enable increased support for MSMEs negates the transformation agenda. The high barriers to entry for MSMEs, exacerbated by the lack of skills and the DFI mismatch continue to be an Achilles heel for most township enterprises.

6.8 Procurement spending

The researcher also analyzed and discussed data on Gauteng’s spending on township-owned businesses. The results are provided as follows (Figure 7).

The Gauteng Department of Social Development was singled out as the sole government department meeting the 30% threshold earmarked for township businesses, achieving 45.51% of procurement spending. It is worth noting that most of the department’s township spend emanated from transfers, with 82.36% of their payments going to non-profit organisations (NPOs). Most funds or transfers to NPOs comprise low-value-added products and social events, including event management, catering, security, and related services (Gauteng Provincial Treasury, 2021). The Gauteng

provincial government's total township spend was 12.38% in the 2020-2021 financial year, translating to a variance of -17.62% against the target of 30%. This continues to be the domain of multinational corporations, while local township businesses benefit through mark-ups from imported products. Most computers for government departments (77.72%) are also procured from non-township businesses (Gauteng Provincial Treasury, 2021).

Despite the challenges of economic exclusion, multinational corporations have the potential to develop local suppliers through effective contracting with SMEs and local sourcing of inputs (Bosiu & Vilakazi, 2020). They further argued that strong policies can help foster the participation of SMEs within some of the value chains dominated by African Multinational Corporations. The maintenance of infrastructure under the auspices of the Department of Roads and Transport, including upgrades, refurbishments, and rehabilitations, continues to benefit non-township businesses (77.72%), with 13.79% of services procured from township-based suppliers (Gauteng Provincial Treasury, 2021). Despite the set-aside, township suppliers are required to compete equally and fairly against other suppliers, regardless of size and location. This neo-classical approach advocates for open competition in domestic public procurement, which is the antithesis of the global practice of breaking down tenders into smaller portions to cater to marginalised businesses.

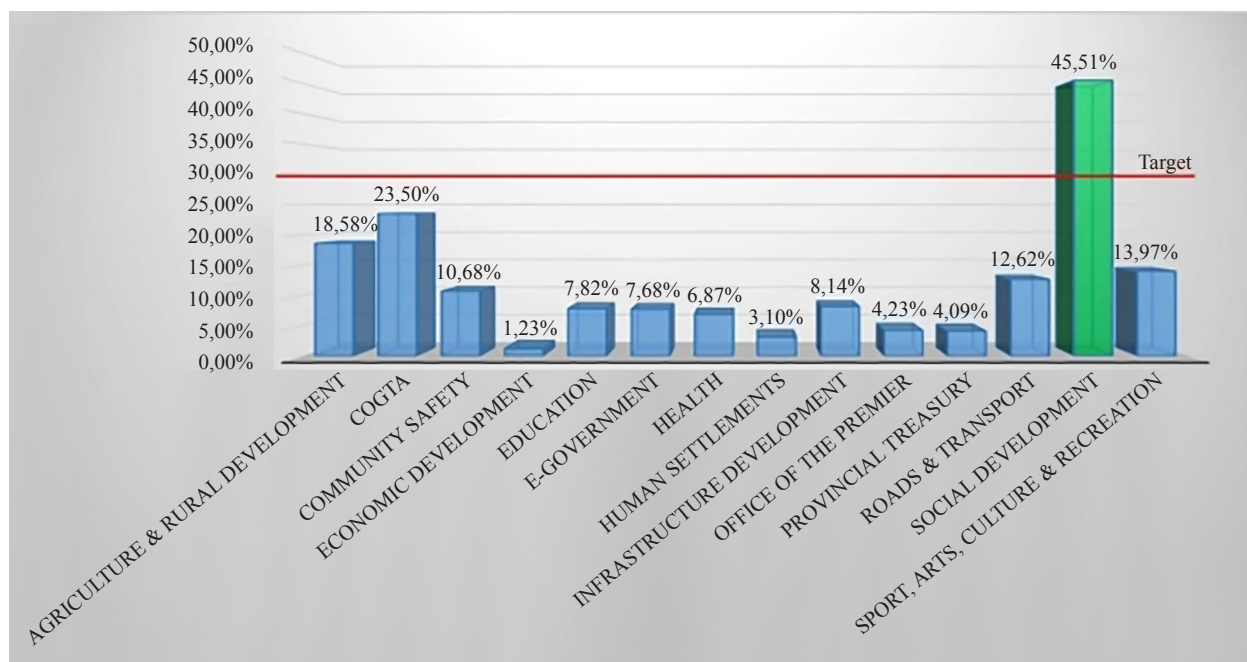


Figure 7. Gauteng department's spending on township-owned businesses

Source: Gauteng Provincial Treasury (2021)

7. Recommendations

There needs to be a major change in DFIs' structure to grow the economy from below and change ownership patterns in line with the transformation agenda outlined in the Constitution, section 257(2). This resonates with the National Treasury's (2018) recommendation (after its review of agencies or entities) for DFIs' restructuring and re-engineering in South Africa to meet the country's socio-economic needs. Conversely, the mismatch between R&D within institutions of higher learning needs to change; there is too much focus on research and less on economic development. The repositioning and repurposing of R&D in institutions of higher learning to stimulate local economic development within the city region are critical. Prioritising a significant portion of R&D to develop and enhance specific products would accelerate economic growth in the country.

To ensure integration into the economic mainstream, institutions of higher learning should be measured based on new products being developed as an investment rather than their number of publications. In other progressive

developing countries, institutions of higher learning are at the centre of the city region's development. An approach of this nature could maximize the economic potential of the province and the country. Government expenditure on universities in South Africa is well below the OECD average, while higher education institutions' R&D intensity of 1.18% of the GDP is also far below the OECD average (Pouris & Lotz, 2014). The percentage of government funding for higher education is 0.71, the lowest compared to other countries like Cuba (4.5), Ghana (1.44), Senegal (1.38), and Brazil (0.95) (Pouris & Lotz, 2014). Public procurement should also allocate a certain portion of funds so MSMEs can innovate and develop new products. This practice is also a trend in the EU countries, assisting to reduce the oligopolistic and monopolistic structures of the economy, reduce high inequality levels, and increase the economy from below (local production).

A structured approach to MSME development with a clear pipeline should be developed, linked sectorally with public procurement and private market opportunities. This structured pipeline of MSMEs should be linked with the Enterprise Development Model and MSME Monitor to ensure these enterprises transition to various stages of development until they attain growth, maturity and exit for greater economic opportunities linked to the export-led industrialisation path. A structured approach to MSME development should ensure an increased number of new businesses producing and supplying some of the public procurement priority products. It should ensure increased participation among township MSMEs in public procurement and the manufacturing of goods and services in line with the localisation strategy. This would change ownership patterns and reduce the inequality gap.

8. Conclusion

The rollout of economic infrastructure to create a conducive environment for MSMEs to develop and expand needs to be prioritised. A customised or targeted approach to Enterprise Supplier Development should focus on support for product development and services. This has the potential to create local production and create sustainable and competitive enterprises. The institutions entrusted with the responsibility to improve local production must be accessible and well-equipped to deal with the complex nature of processes and product development. The setting up of shared production facilities and productivity enhancement for MSMEs would assist in increasing economies of scale and meeting larger contractual demands. Current efforts to integrate all the regulatory bodies, development finance, and other stakeholders has the potential to change the current economic landscape and foster the participation of MSMEs in the mainstream economy. The revitalisation of traditional industrial hubs and the setting up of incubation centres would assist in addressing the lack of economic infrastructure to stimulate local production and drive industrialisation from below. While set-aside opportunities allow MSMEs to compete in the mainstream economy, open bidding for economic infrastructure exposes micro and smaller firms to unfair and unequal competition. This further reduces the growth of township MSMEs and supports the dominance of big firms, while relegating small and micro firms to a state of perpetual underdevelopment.

At the same time, the study indicates there is political will to increase MSMEs participation (53% of respondents supported this argument). This claim is also supported by the newly developed Gauteng Township Economic Act of 2022, which prioritizes township businesses. The government's lacklustre approach in forcing main contractors to assist MSMEs to improve their grades, products and transition from low to upper stages of development remains a challenge. There is consequently the proposal to enforce the 30% set-aside to be paid directly to subcontractors. In addition, a clear disbursement plan should be developed based on the milestones to ensure the development of smaller players is realized or achieved. Respondents suggested that enforcing the 30% set-aside should be the priority of the Auditor General. Additionally, the discussion included the low procurement spend on township businesses, the concentration of resources (Development Finance Institutions (DFIs)) and spread or distribution by province and sectors. Lastly, the Localisation Policy, the Gauteng Township Economic Act, Township SMME Fund, establishment of township economic zones, and Enterprise Supplier Development that is product-specific are critical plans and programmes in realising the Growing Gauteng Together 2030 strategy.

Conflict of interest

The authors declare no competing financial interest.

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