



The New Policy on Small, Medium and Micro Enterprises

Overview

An important policy development during 1998 was the introduction of the Policy on Small, Medium and Micro Enterprises (SMMEs), which was approved by Parliament in December. The new policy resulted from the recommendations of the SMME Task Force, appointed by the Minister of Commerce and Industry but comprising mostly private sector representatives, that had reported earlier in the year. The SMME Policy is a follow-up to the 1996 Industrial Development Policy.

The main components of the new policy include:

- a new legal and institutional framework for SMME support (Small Business Act, Small Business Council, and Small Business Promotion Agency);
- new sources of finance for SMMEs (a micro-credit scheme, and a credit guarantee scheme to operate through the banks);
- regulatory changes, including reform of the Companies Act, sales tax regulations, licensing laws and reserved activities policy;
- improving business education and training, both through the school system and subsidised short courses for entrepreneurs and managers.

All of these are positive reforms that should help to support and develop the SMME sector. However, the Task Force recommendations went much further than this, and many of the more radical recommendations have been deferred or rejected.

Background to the SMME sector

Recent years have seen increasing attention focused on the SMME sector, in both developed and developing countries. This is partly because SMMEs are seen as a potentially important source of employment generation. At the same time, the growth of SMMEs reflects economic change: the declining importance of centralised mass production, along with technical change, the growth of information technology and the growth of the service sector, has in some industries favoured the flexibility and specialisation that small firms can offer.

In Botswana and other developing countries, SMMEs are predominantly owned by citizens, whereas larger firms are often foreign-owned. The development of the SMME sector therefore involves the economic empowerment of citizens. SMMEs are less likely to be mobile internationally, and should also have closer links to their communities.

Furthermore, it is also well known in Botswana that one of the main economic constraints is a shortage of entrepreneurs capable of running larger firms, while the SMME sector is the main source from which entrepreneurial and

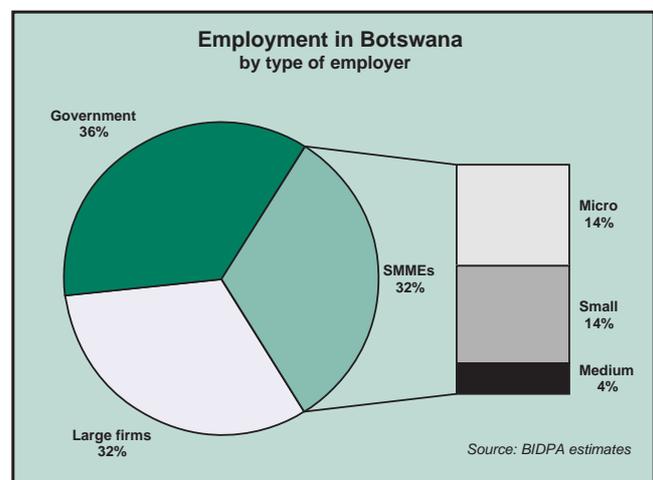
managerial skills will, over time, emerge.

The SMME sector is not well documented, so there is uncertainty over the number of SMMEs in existence and the sector's economic importance. However, as a rough estimate, SMMEs account for 50% of private sector employment, and 15-20% of GDP. What is known, however, is that SMMEs, especially small and micro enterprises, do not have good records in terms of survival and growth. It is estimated that approximately 80% of small enterprises in Botswana cease trading within five years of start-up (a figure that may sound high, but which is in line with international experience). Most micro-enterprises do not fail, as they are "survivalist" enterprises, but very few grow beyond the typical very marginal existence. The Task Force concluded

that the main constraint to SMME growth was a lack of entrepreneurial and management skills and experience, compounded by problems in accessing finance, restrictive regulations, and (especially for small enterprises) a shortage of business premises.

The needs of SMMEs are often different to those of larger businesses, which may have a more direct influence on government policy. However, in view of the potential importance of the SMME sector, the creation of an appropriate enabling environment for them is essential,

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and government is probably the largest single influence on that environment. Hence the importance of an SMME policy, which should encourage entrepreneurship and support SMME start-ups.

Details of the New SMME Policy

Institutional: At the heart of the new SMME policy will be a Small Business Act. This will raise the profile of SMMEs in the country and provide a legal framework for the government's support services. The Act will also establish a Small Business Council, an autonomous advisory body, operating outside of government, to oversee the development of the SMME sector. In particular the Council will review the impact of government policies and programmes on SMMEs, make recommendations about regulatory and policy changes, commission research and data collection on the SMME sector, and monitor SMME support programmes. Its membership will mainly

be drawn from the private sector. The Council will be supported by a full-time secretariat, to be located within the Ministry of Commerce and Industry, named the Small Business Promotion Agency (SB-PA). As it will take time to pass the Act and formally establish the Council, a provisional council will

be established so as to maintain the momentum already built up by the Task Force and policy review in addressing the problems of SMMEs.

Finance: although lack of finance is typically perceived as the major problem facing SMMEs, the Task Force concluded that financial problems were generally symptoms of other deeper problems, especially lack of appropriate business skills and experience. Banks are also unwilling to lend to SMMEs for this reason, and also because small business lending is typically a high cost, high risk and not very profitable activity for the banks. The new SMME policy includes two main initiatives for dealing with the financial problem of SMMEs: the establishment of a micro credit scheme for providing small loans to SMMEs, and a credit guarantee fund, which should help to improve SMME access to bank credit by providing partial loan guarantees. The micro credit scheme will provide loans of P 500 - P 20 000, repayable over periods of up to 36 months at an interest

rate of 18%. The credit guarantee scheme will provide a guarantee of up to 60%, for bank loans to SMMEs from P10 000 to P250 000. Both schemes will only be available to citizens and citizen-owned businesses.

present poor quality loan applications to financial institutions, the new policy also provides for a subsidy to help firms hire professional advisors to help in the preparation of funding applications. A Task Force recommendation that small scale FAP be transformed in to a part-loan part grant scheme, has been deferred pending a full review of FAP due later in 1999.

Education, Skills Development and Training: the new policy acknowledges that the role of business subjects in schools must be enhanced, which will be implemented under the Revised National Policy on Education. An important new initiative is that government will set up a mechanism for accrediting SMME training-providers (who may be NGOs, business associations, private sector institutions or parastatals) to offer subsidised short courses relevant to entrepreneurship and business training. The mechanism through which the subsidy will be provided is still to be specified, but the government has surprisingly rejected outright the Task Force's recommendation that this be done through a voucher scheme, which would offer choice to trainees and encourage competition between trainers; such a scheme works well in Mauritius.

Regulatory Environment: Excessive regulations - relating to licenses, zoning, taxes, company laws etc. - are a major problem for SMMEs, either imposing unnecessary costs or forcing them to operate illegally, and often do not achieve their desired objectives. For instance, it is estimated that 75% of micro enterprises in urban areas operate from residential premises, despite this being illegal. The new policy has made some steps forward: it abolishes license requirements for hawkers & vendors, but a recommendation that licenses be abolished for all citizen-owned businesses has been deferred pending the ongoing review of the Trade and Liquor Act. Businesses with a turnover of less than P75 000 will no longer have to charge and account for Sales Tax, and the ongoing review of the Companies Act will consider introducing a simplified form of incorporation for small companies.

Principles and Objectives of the new SMME Policy

The guiding principles of the new SMME Policy are that it should:

- create an enabling environment in which SMMEs will flourish and grow;
- provide an integrated approach to SMME development which ensures cohesion and linkages between the various programmes;
- ensure that SMME policy is implemented effectively and assessed against measurable objectives, and
- discourage dependency upon Government.

The specific objectives that the policy hopes to achieve are to:

- foster citizen entrepreneurship and empowerment;
- achieve economic diversification;
- promote exports;
- encourage the development of a competitive and sustainable SMME community;
- create sustainable employment opportunities;
- promote linkages between SMMEs and primary industries in agriculture, mining and tourism, and
- improve efficiency in the delivery of services to businesses.

Recognising that in many cases SMMEs also suffer because they

Assessment of Proposals

Overall, the new policy does make some significant improvements in the environment within which SMMEs operate; the Small Business Council and SBPA will provide a permanent forum for monitoring the development of the SMME sector and relevant policies; access to finance should be much improved; as should access to training.

Much will depend upon implementation, however. For instance, the details of how training courses for SMMEs are to be subsidised, and how training providers are to be accredited, are crucial. As for the SBPA, it will need to be staffed with high quality personnel, or else it could easily become another ineffective government agency. Given that part of its role will be to review government policies and their impact on SMMEs, it must not

be deterred from criticising policies where justified, despite being part of government itself; indeed, maybe the SBPA would be better off outside of government, as the Task Force recommended.

Another area of concern lies with the new micro credit scheme. The experience of many other countries shows that although there are many successful micro-credit schemes in operation, there are also many more unsuccessful ones, and furthermore it is very difficult to make such schemes sustainable in the long term, i.e., without dependence upon subsidies. The precise details of how micro-credit operates are important, and a successful scheme must be appropriate for the particular social and cultural characteristics of the country or community in which it operates (e.g. the question of whether group or individual borrowing is more effective in generating sustainability, and the related issue of how to design incentives to secure high repayment rates). The characteristics of successful micro-credit

schemes vary a great deal from one country to another, and a great deal of attention has to be paid to getting the operational details right.

In the case of the new Botswana scheme, it appears that the government is insisting that it is up and running by 1st June, which is unlikely to be enough time to ensure that the details are properly

Types of SMMEs

Although reference is often made to "SMMEs" as a sector, there is in fact a lot of variety and diversity between the types of businesses in the overall category. The new SMME policy distinguishes between the following:

Micro-enterprises (also referred to as informal sector enterprises): although they may employ up to six people, they typically employ only one or two people, including the owner, and may even be part-time operations. They typically operate in an unstructured way, usually from residential premises, and lack formal registration. They can have a turnover of up to P60 000 a year. There are estimated to be around 50 000 micro-enterprises in Botswana, the majority owned by women.

Small enterprises: operate in a more structured way, and may have links to medium or large scale firms as markets for their goods and services. They have less than 25 employees and an annual turnover of between P60 000 and P1 500 000. There are an estimated 6 000 small enterprises in Botswana.

Medium enterprises: have a more outward looking approach to marketing their products, and may be involved in exporting and have links to larger firms, both of which present good opportunities for growth. They have between 25 and 100 employees and an annual turnover of between P1.5 million and P5 million. There are an estimated 400 -500 medium size enterprises in Botswana.

worked out and staff are properly trained. Furthermore, international experience suggests that micro-credit schemes need to charge at least 30%-40% a year (in interest and/or fees) to be sustainable; rates less than this, while seemingly helpful to borrowers, are likely to make the scheme permanently dependent upon subsidies and thus undermine its sustainability. The interest rate of 18% that will be charged is most unlikely to cover the cost of capital, administration and defaults. Given the difficulties involved in setting up a successful micro-credit scheme, a pilot project might have helped to get the practical details right, before launching the scheme nation-wide. This seems to be a case where policy implementation is being rushed at the expense of ensuring that it is right.

Missed Opportunities

Although the package of reforms is a step forward for SMMEs, the new policy does fall some way short of the "radically new ap-

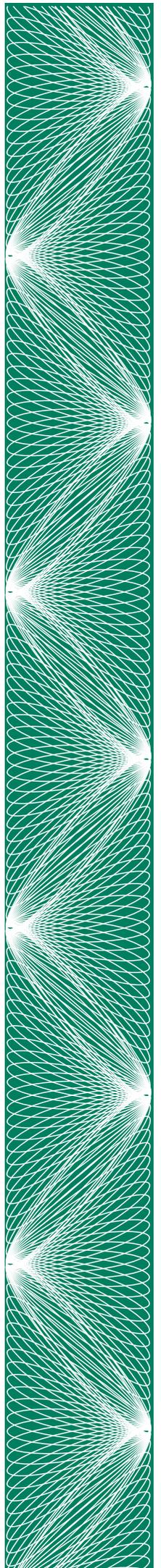
proach to SMME promotion" that was advocated by the Task Force, which would "require government to act boldly and to depart from some well established practices". The hope was that government would move towards playing a facilitating role, in contrast to the present interventionist one.

As part of this new approach, the Task Force intended that as far as

possible, government would withdraw from direct provision of support services (such as training and the provision of finance) to SMMEs, and that these would as far as possible be contracted out to the private and NGO sectors. Government's role would be limited to financing part of the cost of these services, and to monitoring their effectiveness. In the past, the government has not proved itself particularly effective in providing business support services: it tends to have the wrong personnel, with the wrong experience and attitudes - civil servants generally have no business management experience at all. Furthermore, contracting out to the private and NGO sectors would in itself stimulate the further development of the SMME sector, by providing a market for providers of training and business support services.

This broad principle has only been accepted by government to a limited extent. For instance, the new policy envisages that a central role in the provision of business

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support services will continue to be provided by the Integrated Field Services division of the MCI, despite the fact that IFS does not have a good record or reputation. The Task Force wanted the private sector to play a much greater role in direct provision, and the role of IFS to be changed to monitoring the independent service providers. Similarly, the Task Force recommended that the Business Assistance Centres, that the Government has committed itself to under the new Industrial Development Policy, should be run by the private sector and NGOs (as in South Africa). Instead, the new SMME policy firmly rules this out, and confirms that these will only be run by government.

A second of the Task Force's radical principles was that of deregulation. To reduce the regulatory burden on SMMEs, the Task Force recommended extensive deregulation, including the ending of the requirement for citizen-owned businesses to obtain licences, a relaxation of the zoning regulations that prohibit SMMEs from operating in residential areas, allowing hawkers & vendors to operate in public areas, and speeding up land allocation procedures - all of these, where necessary, subject to health, environmental and safety restrictions. Although the new policy partially accepts the licensing recommendation, in general these recommendations have been thrown out. No effective steps are being taken to speed up land allocation procedures, even though these are notoriously slow and bureaucratic. Zoning regulations will remain, and hawkers & vendors will not be permitted in public areas (even neither of these rules are enforceable, and turn most business owners into law-breakers). This approach fails to recognise that one of the advantages that small and micro enterprises have over larger firms is that they can be conveniently locat-

ed near to their customers, thus undermining one of the main potential advantages of SMMEs. The failure to make progress in these areas - which are the responsibility of the Ministry of Local Government and Lands - undermines the Government's other policies and stated intentions to support SMMEs.

Perhaps the most difficult area of SMME policy for both the Task Force and the Government is that of Reserved Activities, where certain industries and retail sectors are restricted to citizen-owned businesses. Although this policy has been in operation for many years, it has largely failed to achieve its objective of promoting citizen entrepreneurship. It has not encouraged the development of large numbers of successful businesses with growth potential; instead it has tended to promote small, fragmented and under-capitalised businesses. For consumers, it has reduced competition and led to higher prices and less choice. It has also harmed those Batswana who have managed to build up successful businesses, by making it very difficult for them to sell those businesses upon retirement or if they wish to pursue other ventures. By restricting the market of potential buyers (to wealthy citizens), the value of these businesses is reduced. This is a particular problem in the rural areas. There is also widespread abuse of the policy, whereby citizens "front" for non-citizens (legally, through loopholes in the law).

The Task Force therefore recommended that the reservation policy be relaxed, by permitting joint ventures between citizens and foreigners in reserved activities, as long as the citizen partner held at least a 45% shareholding in the business. This would help to introduce capital, technology and management skills into these businesses. Although the Government accepted the arguments that the policy has been unsuccessful, it could not ac-

cept the implications that the policy should be relaxed. This was due to its extreme political sensitivity; the general perception is that, if the policy has failed, it is because it has not been properly enforced rather than because of any fundamental flaw. The new policy therefore accepts the relaxed requirement for medium scale businesses only, but for small and micro businesses imposes an absolute ban on any sale of such a business to a foreigner, even if a citizen buyer cannot be found. Although politically appealing, this does not deal with the problems inherent in the policy. The Minister of Commerce and Industry will in due course be faced once again with the problems of dealing with citizen small business owners who wish to sell but who cannot find a buyer, but now he will no longer have the discretion to permit sale to a foreign buyer.

Overall, therefore the new SMME policy is a mixed bag, with some good elements that should have a positive impact on the sector, but with some missed opportunities to make that impact even greater. One characteristic of the Task Force recommendations that have been rejected is that they would all involve government giving up some control, either by handing activities over to the private and NGO sectors to run, or by removing rules and regulations altogether. The fact that government feels unable to do this is disappointing, and undermines its commitments stated elsewhere to reduce its own role in the economy.

Further Reading

Small, Medium and Micro Enterprises Task Force Report (*Government Printer, Gaborone, April 1998*)

Ministry of Commerce and Industry: Policy on Small, Medium and Micro Enterprises in Botswana (*Government Printer, Gaborone, January 1999*)

L. Lisenda: Small and Medium-Scale Enterprises in Botswana: Their Characteristics, Sources of Finance and Problems (*Working Paper No. 14, BIDPA, December 1997*).

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