

## BACKGROUND DOCUMENT: BUSINESS APPROACH TO BLACK ECONOMIC TRANSFORMATION FOR INCLUSIVE GROWTH

### EXECUTIVE SUMMARY

A business approach to black economic transformation for inclusive growth is contained in this Position Paper (“**Position Paper**”), with the following key themes emerging:

- The desired end-state of Black Economic Transformation is an economy that seeks to broaden and deepen economic benefit and participation by all South Africans (“**Economic Transformation**”).
- Economic Transformation is required to achieve and maintain a competitive economy, secure inclusive growth and employment.
- The pace and depth of Economic Transformation has been insufficient to support a growing economy, employment and social development in South Africa. Business is fully committed to accelerating this process together with Government and key social partners, including organised labour.
- Economic Transformation is to be achieved through sustainable interventions to accelerate the quality education and skills development for black people, employment creation (particularly among the black youth) and large scale black enterprise development. Business’ approach includes:
  - Inculcating a transformative culture within businesses and building social cohesion.
  - Large scale enterprise development, focussed on expanding opportunities and removing regulatory and other exclusionary practices that are barriers for emerging black enterprises.
  - Quality and demand-led education and skills development which requires enhanced support for basic education and a significant review of the current institutional skills structure so that skills development is informed by current and future business needs.
  - Clear blockages to employment, with systemic interventions to promote sustainable youth job creation.
- Corruption, maladministration and State capture will undermine Economic Transformation unless decisively addressed.
- Economic Transformation interventions need to be more transformative, developmental and systemic in nature and be designed to be inclusive of diverse and cyclical businesses from all sectors, regardless of size and/or format.
- Accelerated Economic Transformation will require Government, business and other key stakeholders, such as organised labour, to collaborate and work together in partnerships – be that at an institutional level, such as in National Economic Development and Labour Council (“**Nedlac**”) on providing business’ input to key policy interventions, or, in partnering on systemic initiatives and programmes.
- Recalibrating and comprehensively measuring Economic Transformation is necessary to determine the current status and progress.

## INTRODUCTION

Between January 2017 and June 2017, BUSA embarked on a process, under the guidance of an Economic Transformation Think Tank and its policy committees, to develop this approach for and on behalf of business (the “**Business Approach**”). The Business Approach has been endorsed by the BUSA Board and its membership and represents a collective business view.

The Business Approach identifies the guiding principles for business on Black Economic Transformation, the current status, as well as the desired end-state of a economy that seeks to broaden and deepen economic benefit and participation by all South Africans. The gap between the desired end-state and the current status is interrogated with a view to identifying key shifts required in the private and public sectors to meaningfully and substantially broaden participation and enable inclusive growth and employment. Achieving and maintaining a competitive economy that harnesses the full economic potential of South Africa is a key hallmark of this approach.

The size and complexity of this work is not to be underestimated. To this extent, the Business Approach does not seek to provide a masterplan for business, but rather provides a basis to capture the collective views of business on the status and steps that are required by business collectively, alongside partners from the public sector, labour and civil society, to transform and move the economy onto an inclusive growth path. In this regard, there is a compelling case for strengthening the role of Nedlac as a forum to thoroughly engage on Economic Transformation policy, addressing unintended consequences and optimising collaborative opportunities.

## GUIDING PRINCIPLES FOR THE BUSINESS APPROACH

The following guiding principles inform the Business Approach:

- The **pace and depth of inclusive Economic Transformation has been insufficient**<sup>1</sup>. Economic Transformation is central to achieving and maintaining a competitive economy and securing inclusive growth and employment.
- There is a **need for full and equitable participation by a broad base of black people in the South African economy**, with an emphasis on those that are most disadvantaged (black women, youth, people with disabilities and people from poor households, township economies or rural areas).
- Business’ ability to transform rapidly is greatly enhanced with **Government playing a significant role in creating the enabling conditions for growth**.
- **Corruption, maladministration and State capture will undermine Economic Transformation** unless decisively addressed.

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<sup>1</sup> A number of sectors, through the sector Charter and Code approach have had mixed results. The mining, financial and ICT sectors are illustrative of sector specific solutions being reached where success factors include: the active involvement of business and labour, with Government playing an enabling and supportive role, as well as long term commitment and efforts to transform. However, other sector processes have also been marred with discord arising out of a lack of mutual understanding.

- A **collaborative, partnership approach** to Economic Transformation within business<sup>2</sup> and with Government, organised labour and other social partners, based on trust and mutual commitment to social and economic development through institutions such as Nedlac is needed
- A **proactive, innovative, systemic<sup>3</sup> and scalable approach** is required, which takes into account the **diversity and cyclicity of business sectors, formats, and relative sizes** and is cognisant of the short and medium term trade-offs for longer term Economic Transformation
- A **substance over form approach**, focusing on systemic interventions built upon **social cohesion** is required. **Recalibrating and comprehensively measuring Economic Transformation** is necessary to determine the current status and progress.

## BACKGROUND AND CONTEXT

Despite the progress made<sup>4</sup>, **poverty, inequality and unemployment** translate into structural social and fiscal challenges and an underperforming economy. Over 17 million elderly, young or disabled South Africans are dependent on social grants to alleviate the effects of persistent poverty. With 36% unemployment (under the broad definition) and 63% youth unemployment, many black South Africans do not have the means to support themselves and meaningfully participate in both the supply and demand of goods and services. These challenges are inherently unsustainable and threaten the social and economic stability of South Africa.

The economy grew at an average real rate of almost 4% between 1994 and 2007. However, growth was not sufficiently inclusive and driven by sectors that were, on a relative basis, not labour intensive. As a result, South Africa's employment growth rates were well below the rate at which the economy grew. The current global economic outlook is not as favourable as it was a decade ago.

Economic inclusion is the best mechanism to unlock South Africa's economic and social potential. The National Development Plan ("NDP"), endorsed by business, seeks to ensure Economic Transformation through a virtuous cycle of development, and places emphasis on the role of a

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<sup>2</sup> It must be recognised that working collaboratively as business is challenging since individual B-BBEE status is a form of competitive advantage for business. B-BBEE levels can influence procurement decisions, driven by Government procurement, licencing, and private sector procurement. This makes it harder for businesses to collaborate on programmes.

<sup>3</sup> Business recognises that Apartheid systematically engineered (through law, the education system, and business decisions) significant aspects of the economy and society in favour of the white population. To address this, systemic solutions are required.

<sup>4</sup> The Department of Performance, Monitoring and Evaluation reports significant social progress. From 1994 to 2012, the economy grew at 3.2% per year; tax revenue increased from 3 million tax payers in 1996 to 20 million in 2014; employment grew from 9.5 million in 1994 to 16 million in 2015; a black middle class has emerged; poverty halved between 2001 and 2011. Since 1994 there has been significant improvements in households with the addition of 4 million new houses, electricity being extended to 95% of South African households, and water to 85% of South African households. By 2015 98.8% of 7-15 year olds were attending education institutions; with progressive improvement in the quality of education, although this still remains inadequate. Between 2012 and 2015, the number of qualifying TVET students obtaining annual financial assistance has increased from 188 182 to 235 988 and the number of students enrolled in public higher education at universities has increased from 950 000 to 985 212.

social compact between Government, business,<sup>5</sup> labour and society. The NDP, provides the programme to advance Economic Transformation through economic interventions, harnessing the capabilities of South Africans and the capacity of the State, and, active citizenry to eradicate poverty, reduce unemployment to 6% and reduce the Gini coefficient on inequality to 0.60 by 2030.

The NDP defines inclusive growth as a rapidly growing economy that is increasingly broad-based across sectors and inclusive of the country's labour force ("**Inclusive Growth**"). Inclusive Growth refers both to the pace and pattern of growth. This definition captures the importance of structural transformation for economic diversification and competition. The BEE Commission, in South Africa's Economic Transformation Strategy, affirms:

*"Economic growth, development and BEE are complementary and related processes... No economy can grow by excluding any part of its people and an economy that is not growing cannot integrate all of its citizens in a meaningful way. As such this strategy stresses a BEE process that is associated with growth, development and enterprise development, and not merely the redistribution of existing wealth".*

While there are multiple interpretations of Racial Economic Transformation ("**RET**")<sup>6</sup>, the common theme is one that acknowledges that accelerated and substantial deracialisation is needed to grow the economy, and ensure the necessary social, and economic conditions for the country. Business aligns with the definition of RET as articulated in the Medium-Term Strategic Framework 2014 – 2019 ("**MTSF**") mandate of Government, namely:

*"to accelerate growth, create decent work and promote investment in a competitive economy through RET and a range of mutually supporting initiatives and improved implementation of existing and new strategies...<sup>7</sup> Government's programme of radical economic transformation is about placing the economy on a qualitatively different path*

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<sup>5</sup> Business is recognised as the key lever to generate employment, economic growth and thereby create the fiscal space to address social developmental challenges.

<sup>6</sup> President Zuma in the 2017 State of the Nation Address stated that RET requires the "... fundamental change in the structure, systems, institutions and patterns of ownership, management and control of in favour of all South Africans, especially the poor, the majority of whom are African and female..."

Minister of Trade and Industry, Rob Davies, speaking to Business Day at the launch of the 9th Industrial Action Plan stated on 8 May 2017 "Radical economic transformation is essential. But it is not about quick fixes and big bangs. It is hard, painstaking work. It needs pragmatism. It requires dialogue. It requires policy certainty and programme alignment. It requires a collaborative effort with the private sector."

<sup>7</sup> "The New Growth Path targets five million new jobs from 2010 to 2020. This target will require vigorous action to reduce concentration and diversify the economy, while ensuring adequate infrastructure, skills and appropriate regulatory frameworks. It also requires that the State promotes and supports new and innovative activities that can add value and generate employment on a large scale. We need to ensure growth in the core productive sectors of manufacturing, mining and agriculture and open new areas of economic growth such as the oceans economy, the green economy and shale gas. Small business needs to make a much larger contribution to growth." MTSF, page 6.

The MTSF identifies the main pillars for achieving RET as being: productive investment crowded in through the infrastructure build programme; competitiveness enhancement in productive sectors of the economy; addressing imbalances, including spatial imbalances, in economic opportunities; elimination of unnecessary regulatory burdens; workers education and skills development to meet economic needs; a macroeconomic and financial framework to support employment-creating growth; workplace conflict reduction and improved cooperation between Government, organised business and organised labour; expanded opportunities for historically excluded and vulnerable groups, small businesses and cooperatives; and public employment schemes to provide relief for the unemployed and build community solidarity.

*that ensures more rapid, sustainable growth, higher investment, increased employment, reduced inequality and deracialization of the economy”.*

In the context of the private sector accounting for approximately 80%<sup>8</sup> of South Africa’s total production and employment, addressing the private sector’s challenges will be pivotal for Economic Transformation. The MTSF acknowledges that growth requires an:

*“economic environment that encourages business investment and rewards competitiveness, especially in sectors that can catalyse longer term growth and job creation”.*

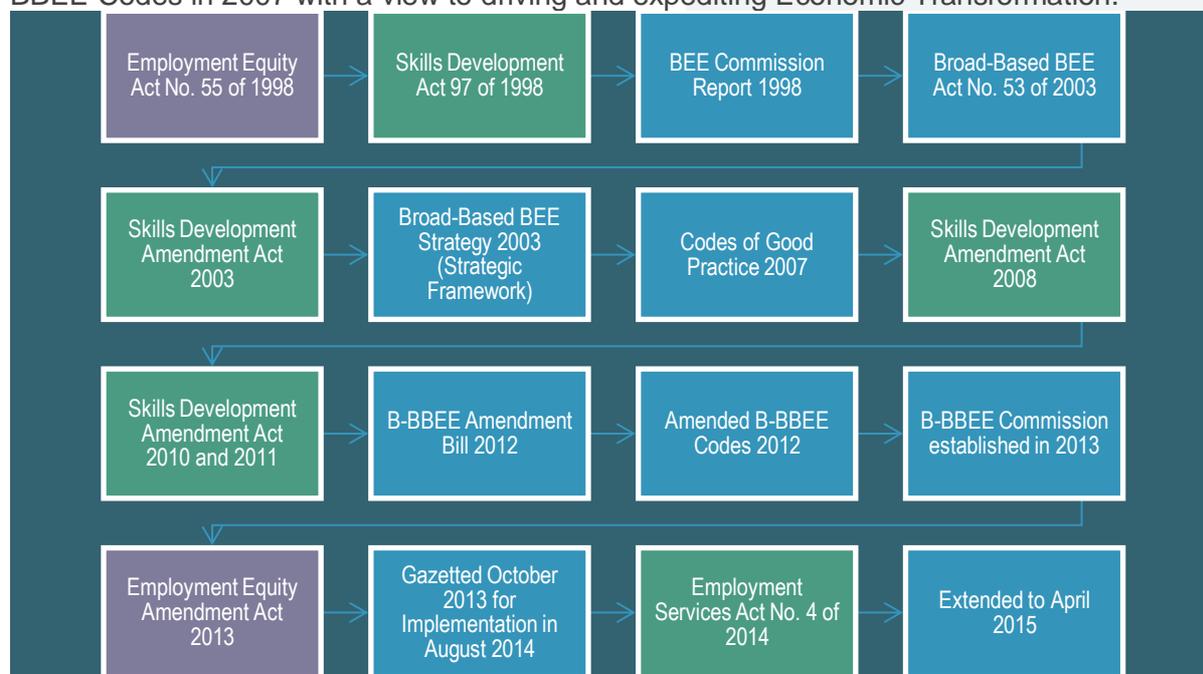
## CHALLENGES TO INCLUSIVE GROWTH

- Smaller businesses contribute only 65% to employment, compared to a worldwide average of 95%, indicating the potential of sustainable black enterprise development as an enabler of inclusive growth
- The regulatory environment has many best in class laws, but in application fails to create the requisite certainty and conditions for competitiveness, economic inclusion and growth
- Energy and water supply and road, rail, transport and IT infrastructure are inadequate, unreliable and too costly to enable businesses of all sectors, formats, and relative sizes to be more competitive
- A productive and stable labour market is required in order to positively contribute to business confidence
- There is significant leakage from the fiscus due to corruption, mismanagement and insufficient accountability of public funds. Funds allocated to supporting black and small business development is inadequately focused and managed and is often inaccessible and misspent
- Basic education, compounded by poor childhood nutrition, fails to provide an adequate foundation for young people to enter post-school education and training or employment
- There is a significant mismatch between skills being generated by the basic and post-school education system and the current and emerging skills demands required for a growing economy
- The current Social Security system is fragmented, inefficient and inadequate to sustain the large number of marginalised, predominantly black, South Africans, Increasing the dependency on those employed and the costs of employment on businesses
- Trade regimes, agreements, support structures and incentives are not optimally designed and implemented to enable South African businesses, of all sizes, to participate fairly and competitively across national borders in order to drive growth opportunities. Through regional integration, SADC countries can reap efficiency gains, take advantage of economies of scale and reverse migration to South Africa.

## ECONOMIC TRANSFORMATION LEGISLATIVE FRAMEWORK AND STATUS

<sup>8</sup> *Medium-Term Strategic Framework 2014 – 2019, page 6.*

Business fully and unconditionally endorses the transformational intent of broad-based black economic empowerment (“**B-BBEE**”)<sup>9</sup>, Employment Equity and Skills Development legislation<sup>10</sup>. There has been a significant increase in regulatory activity since the publication of the first B-BBEE Codes in 2007 with a view to driving and expediting Economic Transformation.



The regulatory framework needs critical consideration with a view to determining the degree to which the legislation has successfully realised its transformational intent.

Legislation	B-BBEE Act 53 of 2003, Codes 2007, Amended Code 2012	Employment Equity Act 55 of 1998	Skills Development Act 97 of 1998
<b>Objectives</b>	<ul style="list-style-type: none"> <li>• Meaningful participation of black people in the economy</li> <li>• Substantial change in the racial composition of ownership and management structures</li> <li>• Promoting access to finance for empowerment 2012 Amended Codes</li> <li>• The emphasis on procurement from black</li> </ul>	<ul style="list-style-type: none"> <li>• Prohibition of direct and indirect discrimination in employment.</li> <li>• Provides for equal pay for work of equal value</li> <li>• To transform the structure of the labour force through a progressive affirmative action approach</li> <li>• Affirmative action in employment is focused on black people, women</li> </ul>	<ul style="list-style-type: none"> <li>• Systematically grow the skills base of employees, with an emphasis on black people and women, to make them more employable</li> <li>• Establish Sector Education and Training Authorities</li> </ul>

<sup>9</sup> As defined in the Amended B-BBEE Codes. The current B-BBEE regulations should continue to provide the legislative framework for B-BBEE.

<sup>10</sup> As per the Employment Equity Act and the Skills Development Act, dealt with in more depth later in the paper.

	<p>youth, women, people with disabilities, people living in rural or undeveloped areas and townships, cooperatives and military veterans</p> <ul style="list-style-type: none"> <li>• Introduction of priority elements of ownership, skills development and enterprise and supplier development</li> <li>• Greater alignment with other transformation legislative instruments addressing fronting by criminalising such action and providing for heavy penalties.</li> </ul>	<p>and people with disabilities.</p> <ul style="list-style-type: none"> <li>• Rigorous firm level penalties of up to 10% of annual turnover for administrative non-compliance</li> </ul>	<p>(“SETAs”) and the National Skills Authority. Employers contribute an amount equivalent to 1% of payroll towards skills funding amounting to approximately R17bn per year. However, the regulatory environment is not achieving this intention. The institutional structures are fraught with contestation, inefficiency, maladministration and other leakages.</p>
<b>Status</b>	<ul style="list-style-type: none"> <li>• No up to date authoritative, consistent and comprehensive national study that measures all aspects of transformation, and performance over time<sup>11</sup></li> <li>• Studies focus on the top echelon of JSE companies<sup>12</sup>, with all</li> </ul>	<ul style="list-style-type: none"> <li>• National data is available, although the methodology and analysis of the Employment Equity reports can be critiqued<sup>14</sup></li> <li>• Legislation has driven a compliance, and transactional approach,</li> </ul>	<ul style="list-style-type: none"> <li>• No national comprehensive data on skills development across the economy.</li> <li>• Throughput rates at post-school education and training institutions are generally</li> </ul>

<sup>11</sup> A number of studies have been conducted that provide limited information including the B-BBEE Baseline Report, Empowerdex Trailblazers Survey, Jack Hammer Executive Report, KPMG Annual B-BBEE Survey and NEF Ownership Survey.

<sup>12</sup> In a recent paper by Roger Southall<sup>12</sup>, he outlines the major shifts in ownership patterns in the private sector in the past few decades with reference to a number of the top JSE companies. Southall points out that in 1981, 70% of the total assets of the top 138 companies were owned by State corporations and eight privately owned conglomerates. By 1990, three domestic and white owned conglomerates controlled 75% of the total capitalisation of the Johannesburg Stock Exchange. By 2016, white South African ownership was down to 22%, foreign ownership at 39%, direct Black ownership 10% and indirect black ownership (through pension funds) at 13%. Southall makes the point that large scale capital is now less monopolised and more diversified, there is now significant participation in ownership of the economy by Black people, and foreign owned financial institutions. While the above study is indicative of progress, other studies are needed to authenticate and measure ownership across the broad economy.

<sup>14</sup> The reports rely on self-reporting, so the accuracy and coverage of the information may be compromised. The report analysis deals only with percentages, rather than numbers and percentages, making it difficult to understand the impact. Top management movements appear to be out of sync with the numbers of individuals employed in this category.

	<p>JSE listed companies estimated to constitute only a third of private sector activity in the economy</p> <ul style="list-style-type: none"> <li>• Wide ranging, often opposing views</li> <li>• Studies reveal that between 1995 – 2015 there have been more than R600bn in the gross value of BEE transactions<sup>13</sup></li> </ul>	<p>rather than substantive transformation.</p> <ul style="list-style-type: none"> <li>• In the 15 years since the first Annual Employment Equity Report in 2001, the number of companies reporting has grown from 8 250 to 26 255 in 2016. In 2001 the number of employees reported was 3.3 million, whereas today it covers just over 7 million employees, representing approximately half of the formal working population.</li> <li>• Substantial progress in the proportion of black people and women in the workforce at all occupational levels<sup>15</sup> However, much more limited progress in higher management levels.</li> </ul>	<p>lower for black people and people from poorer households</p> <ul style="list-style-type: none"> <li>• With the focus on supply of skills and long term qualifications without the requisite matching to business needs, large numbers of individuals, particularly youth, remain unemployable.</li> <li>• In a study on barriers to doing business for SMEs, conducted for BUSA through the ILO, lack of access to skilled people was identified by small and formalising businesses as the primary constraint to doing business</li> </ul>
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<sup>13</sup> DPME

<sup>15</sup> Demographic Composition per Occupational Level

	African		Coloured		Indian		White		Foreign National	Male	
	2001	2016	2001	2016	2001	2016	2001	2016	2016	2001	2016
<b>Top Management</b>	6%	14.4%	3%	4.9%	4%	8.9%	87%	68.5%	3.4%	87%	78%
<b>Senior Management</b>	9%	22.1%	5%	7.7%	5%	10.6%	81%	58.1%	1.4%	80%	66.7%
<b>Professional/ Mid Management</b>	33%	41.5%	5%	9.7%	6%	8.5%	56%	37.5%	2.8%	62%	54.4%
<b>Skilled Junior Management</b>	58%	60.2%	18%	11.5%	6%	5.8%	18%	20.8%	1.8%	60%	54%
<b>Semi-Skilled</b>	58%	76.1%	18%	12.3%	6%	3.1%	18%	6.2%	2.3%	61%	57.2%
<b>Unskilled</b>	98%	83.2%		11.4%		0.8%		1.2%		71%	59.3%

Source: Commission for Employment Equity Annual Report 2001 and 2016

## SECTOR PROGRESS

In developing this Business Approach, an attempt was made to critically evaluate the progress and status of B-BBEE, across different sectors. The B-BBEE Commission conducted a 2014-2016 study that collates all the information from the B-BBEE verification processes. While this provides a composite verification view of progress relative to the Amended B-BBEE Codes, it does not provide information on the value and extent of transformation in the South African economy.<sup>16</sup>

The existence of a sector structure or process to focus on transformation is clearly beneficial. For transformation to be sustainable, of necessity it requires consideration of industry specific dynamics, and the need for businesses, regardless of size, sector, formality or ownership structure, to participate competitively in the economy. Accordingly, transformation efforts must be customised to specific industry and business dynamics.<sup>17</sup>

## UNLOCKING THE DESIRED END-STATE

The desired end-state requires that the economy grows inclusively with strong, transparent and sustainable redistributive elements. To achieve this end-state, the MTSF identifies that:

*“Government will increase its engagement with business to unlock private sector initiative, build investor confidence, promote trust and seek long-term commitments to implementation of the NDP.”*

The desired end-state includes:

- Deracialisation of the South African economy to enable equitable participation by all South Africans in the economy.
- A vibrant, diverse and globally competitive economy that enables all South Africans regardless of race, gender, age or other attributes to have the opportunity to participate in the economy and earn a sustainable livelihood for them and their dependents.

## CRITICAL ANALYSIS OF THE ELEMENTS OF THE B-BBEE CODES

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<sup>16</sup>Those sectors with Charters, Councils and Codes, or those that had embarked on sector transformation processes such as agricultural manufacturing, ITC, mining and the financial sector had more access to information. In other sectors such as business services and manufacturing, the wide and overlapping nature of industry tended to make information seeking more challenging. Those sectors with many small and emerging enterprises such as retail, retail motor and tourism are also not well documented. Generally, the specific sectors evaluated similar elements in different manners, also making it difficult to collate the information into a coherent picture.

<sup>17</sup> For example, it would be misguided to adopt the same approach to the agricultural sector during a drought as one would to the gold mining sector when commodity prices fluctuate. Failure to craft industry and business specific solutions, by applying a numbers-driven approach, is likely to lead to superficial, unworkable solutions that are incapable of implementation. It would be important to have a sector-by-sector view of transformation as we need to draw upon best practice across sectors and leverage institutional capacity and experience that already exists.

This section identifies the key challenges, provides an assessment of the current status and the shifts required by business to address the deficits. Across all the elements of the Codes, there is recognition that the evaluation mechanisms, through seeking to identify numerical and quantifiable measures, has often resulted in a transactional approach to B-BBEE where compliance and improved levels are inadvertently targeted, rather than deep and systemic Economic Transformation.

## OWNERSHIP

### Key Challenges

- No single, credible, comprehensive source of information for the economy.<sup>18</sup>
- The measurement of Ownership does not cater for the varied nature of sectors and/or businesses.
- Despite extensive investment and costs, including financing costs, funding of B-BBEE Ownership transactions in a sustainable manner, with limited equity from B-BBEE parties, translates into limited influence by and limited value generation.
- The treatment of institutional investments and offshore interests<sup>19</sup> results in unintended consequences.
- There is insufficient clarity as to the appropriate measurement of trusts, including employee share ownership schemes, the application of the modified flow through principle and mandated investments.
- As a result of volatile and, more recently, weak equity market performance, a significant number of B-BBEE Ownership transactions have not created net value. As a consequence, the experience of lenders has often been negative, further depleting the pool of available financing.

### Assessment

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<sup>18</sup> Examples of this include the debate around black ownership of the JSE, with the NEF positing that 3% of the JSE is black-owned compared to the JSE's figures of 23% black ownership of the JSE's top 100 companies. Complications arise around whether passive black shareholding should be included or excluded from the analysis; whether the shareholdings of Development Finance Institutions such as the IDC, holding of the Public Investment Corporation (PIC), etc. should be included. Another complication arises around how to amend funding structures to achieve net value targets, particularly where third party debt is involved in financing transactions. Further, these studies fail to differentiate value (both gross and net value) that has accrued to black shareholders from the influence that black shareholders have on, inter alia, the strategic direction of the investee company. Some indication of black ownership in the economy can be inferred from the JSE top 100 company study. However, it is important to note that based on relative corporate income tax paid, the JSE represents approximately a third of South Africa's private sector and, as such, is not necessarily representative of the South African private sector. South African companies have significant operations outside of South African, rendering them multinational. In a study narrowly focused on the top 100 JSE listed companies, foreign institutions own 39%, black indirect ownership constitutes 13%, direct black ownership 10% and white ownership is at 22%. 16% of the market not measured.

<sup>19</sup> To the extent that offshore operations increase in contribution relative to South African operations, the effective BEE shareholding in the South African operations increases (assuming a BEE shareholding at a holding company level)

- Overemphasis on Ownership as it has largely failed to deliver meaningful control and value<sup>20</sup> to black people given that shareholdings are generally insufficient to exert direct influence on the strategic direction of investee companies.
- Ownership redistribution is costly and limited to a concentrated number of established business.
- Difficult to address Ownership in the unlisted environment in the context of determining fair value, access to capital and the ability to monetise value for the B-BBEE shareholders (both practically and at an appropriate value).
- Limited available capital hinders the ability to implement B-BBEE Ownership transactions.
- Overreliance on highly geared funding structures and complex third party funding mechanisms.
- The efficacy of the 25% or 26% black ownership interest is questionable. The original intention of this was to ensure negative control for B-BBEE parties, but this has in practice rarely been achieved.
- The achievement of the annual “net value” target is subject to material fluctuations often outside the control of companies (e.g. share price movements for listed companies). This creates uncertainty for enterprises.

## Shifts Required

- Drive significant growth of black business through providing access to markets, capital and skills to support entrepreneurship in order to create black owned and black-controlled businesses.
- Work with government to enhance the success and scale of programmes such as the Black Industrialist Programme.
- Interrogate and contribute to solutions on how to structure B-BBEE ownership transactions so as to stimulate value generation in a cost-effective manner.
- Place greater emphasis on asset sale transactions as part of establishing new black-controlled businesses.
- Recalibrate the ownership element to ensure its applicability across multiple sectors and businesses of varied sizes and structures with a focus on innovative forms of financing (including vendor funding) and an alternative assessment of the financial parameters of net value.

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<sup>20</sup> B-BBEE Ownership transactions can potentially be viewed as not delivering real value to black shareholders. In certain circumstances, the value (i.e. dividends and capital appreciation) of the shareholding is often retained in the structure of the B-BBEE transaction in order to service the cost of the associated transaction funding. Over the term of the B-BBEE Ownership transaction, and to the extent that the collective value attributable to the B-BBEE shareholders is less than the cost of the associated transaction funding, no “net value” will accrue to the B-BBEE shareholders. Any net value that is realised is largely dependent on equity value appreciation, typically takes a significant amount of time to accrue and imposes large direct and indirect costs on both the investors and investees.

## MANAGEMENT CONTROL

### Key Challenges

- While there has been an increase in the representation of previously disadvantaged individuals in middle management, professional and technically skilled levels, there has been slower and often little progress at top and senior management levels.<sup>21</sup>
- Appointment of black managers into top management, does not necessarily result in management control and influence in the company.
- Systemic societal and organisational factors inhibiting participation and progression in the workplace have been inadequately addressed in many workplaces.
- The economic value of diversity (improved performance and competitiveness) has not been generally recognised by business.<sup>22</sup>
- There are insufficient professionals graduating and gaining skills necessary to meet the needs of a growing economy and society.
- A one size-fits all approach fails to recognise that: smaller businesses may not have space nor capacity to diversify their management; multinational enterprises (or those with certain shareholding structures) do not have the same flexibility to adjust management control as do other enterprises; and that business conditions can inhibit the ability of a business to transform its controlling management structure.

### Assessment

- As more skilled people from previously disadvantaged groups enter the workforce, this filters up into higher management levels. This would be accelerated with economic growth that would create the necessary space to rapidly deracialise management control.
- Failure to recognise the economic benefits of diversity, results in adequate attention being given to diversity as a driver of business competitiveness.
- Availability of skilled professionals, as well as individuals skilled in governance and managerial responsibility, is insufficient to drive the needs of the economy. This is more pronounced for historically disadvantaged groups.
- The current employment equity framework focuses on numerical targets and appointments rather than measuring genuine management influence. Substantive diversity enablers and processes that can shift management influence are not recognised in current measurement methodology.
- The current framework is not easily applicable into businesses of all types, ownership structures and sizes and in different business contexts.

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21 The 2016/2017 Annual Employment Equity Report of the Commission for Employment Equity reflects that only 32% of top management is black, and 22% female.

22 The recent South African study on gender equality by Bain and Company identifies the economic value of diversity. Harvard Business Review paper by David Rock and Heidi Grant points to a number of studies including McKinsey and Credit Suisse demonstrating that nonhomogeneous teams are smarter and yield higher returns on equity and net income growth than firms that are homogenous

## Shifts Required

- Research and advocate the investment case for diverse leadership and management as part of business competitiveness.
- Build transformative capabilities in order to accelerate and enhance diversity and change capabilities through mentorship, fast-track programs, diversity management tools and the support of black employees. A differentiated approach that is applicable to different businesses and industries, is required.
- Improve the analysis of employment equity information, including adopting an approach that critically considers and addresses the identified barriers. Business can contribute by supporting the assessment of, and discerning the lessons from, the qualitative information contained in the employment equity reports.
- Drive diversity and change capabilities, beyond the current numerical approach.
- Work with government to reframe the measurement of management control so that transformative processes are emphasised and recognised.

## ENTERPRISE & SUPPLIER DEVELOPMENT

### Key Challenges

- Confirming the B-BBEE credentials of suppliers, large and small is often problematic.
- Significant investment, time and effort is required in order to address enterprise and supplier development.
- The Black Industrialists programme, while promising, has not yet delivered enterprise support to black businesses on the scale that is possible and required.
- There are mixed effects in relation to enterprise and supplier development dependent on the nature of the industry, the size of firm and the product and services required.
- Extensive barriers to entry exist for emerging black-owned businesses, particularly in relation to regulatory compliance. Without easing regulatory barriers to entry, many emerging businesses will remain in the informal sector or fail to survive.
- Inefficiency and corruption undermines enterprise development, particularly when Government's financing and project initiatives intended to support development of black-owned enterprises, are poorly or fraudulently applied.
- Private and public sector support, be it in the form of access to finance, business support, mentorship, or access to skilled staff is generally haphazard, inaccessible and inefficiently deployed. This also makes it difficult to measure the return on investment and employment contribution of such initiatives.
- Economic Transformation is difficult to achieve in relation to non-discretionary spend, particularly where a business has no choice but to purchase the bulk of its products or services from suppliers such as multinationals.
- Given that enterprise and supplier development is a key element of competitive advantage, it makes it difficult for firms to collaborate in developing black suppliers.

### Assessment

- Enterprise development is one of the key enablers to deracialise the South African economy, grow employment and lift South Africa out of its current growth trap.
- Corruption, maladministration by public institutions and State capture will undermine enterprise and supplier development.
- There is significant opportunity to accelerate, and improve the effectiveness and efficiency of public and private support of emerging enterprises.<sup>23</sup>
- Enterprise and supplier development takes time and resources and can impact on short term competitiveness. New enterprises may have information gaps and lack of the required skills to supply specialised products and services.
- Sourcing from smaller businesses is generally a challenge when global best practice states that 80% or more of a procurement bill should be spent on a few strategic suppliers in order to optimise efficiencies.
- There is an inherent paradox that requires larger businesses to support enterprise development as part of transformation, yet there is a point at which the enterprise becomes a supplier and procurement from such suppliers become, by necessity, more competitive. This enhances the need for Government-led cluster and industry enhancing programmes, recognising that individual businesses in supply chains do not always collaborate with each other, although they would want to be involved in contributing to a sector wide effort in partnership with Government (including the DTI, Economic Development and the Department of Small Business Development).
- The entrepreneurship pipeline is inadequate - systemic solutions, focused on building entrepreneurship and value chains will optimise transformation efforts.

## Shifts Required

- Government and business partnerships in sectors and regions to be leveraged to provide greater efficiencies, support and coordination.
- Business taking a leading role and leverage its understanding of the business environment and what is required to access markets, capital and skills and reduce unnecessary regulatory burdens.
- Mainstreaming sector development strategies could include: creating and maintaining a database of suppliers per region; specific training and skills development interventions; industrial support; job creation projects; or clearing regulatory or trade barriers.
- Local, scalable initiatives (such as business-hubbing, enterprise support, skills development and mentorship) should be championed and systemically introduced, particularly in township economies, outlying areas and growth nodes.
- Advocate for greater alignment between the Amended B-BBEE Codes and Government's procurement policy.

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<sup>23</sup> *The motor industry and textile industry incentive programmes provide helpful benchmarks to what can be done at an industry level to stimulate growth, inclusivity and employment.*

- Particular attention should be paid to unblocking regulatory barriers acting as constraints to emerging enterprises. Business should advocate for Government-wide, socio-economic regulatory impact assessment (“SEIA”) that includes business insights on what is required to ease regulatory burdens that impede enterprise development and growth.
- The Amended B-BBEE Codes should be reconsidered in relation to non-discretionary spend, so as to avoid unintended consequences.
- Business should collaborate to comprehensively consider how it can support the Black Industrialists programme to be more successful and widespread.
- Decisively deal with fraudulent use or maladministration of enterprise development funding, through the criminal justice system. Business should reinvigorate its efforts to work with and support the criminal justice system to take action in this regard.

## SKILLS DEVELOPMENT

### Key Challenges

- The basic education system is generally not producing the skills required to enable youth to access work and post school education. This perpetuates racial disadvantage for black people, particularly youth, women, people from poorer households and rural areas.
- There is a severe skills mismatch and lack of alignment of labour market supply and demand for skills.
- The current post-school education and institutional training structures combined with the lack of partnership between business and the State, is not conducive to optimising on-demand, quality skills that would enable employment, productivity and growth.
- Quality training is inadequate to improve the competitiveness of South African businesses.
- There are inadequate mechanisms to measure the return on investment and impact of skills development interventions. Measurement mechanisms do not adequately take account of: mentorship and progression; acquisition of short term and adaptable skills that enable a person to rapidly progress and be successful.
- There are inadequate mechanisms to rapidly certify qualifications and localise international qualifications.
- Mixed and inadequate SETA performance with many SETAs under administration, being poorly governed, and large amounts of funding being misdirected or wasted. Maladministration and fraudulent use of skills-related public funds substantially undermines skills delivery.
- For many small, family-run businesses, accessing skilled workers and post-school education and training for workers is extremely complex and largely inaccessible – this constitutes a major inhibitor for emerging, formalising and growing black businesses.
- The current SETA mechanisms fail to adequately professionalise and support entrepreneurship, often placing such training into the same category as support for the unemployed, rather than an investment into future enterprises.
- Ineffective and poor management of skills enhancing partnerships between business and Government, business and Tertiary Vocational Education and Training (“TVET”) colleges to deliver workplace experience.

- Insufficient, unaffordable and inaccessible higher education opportunities to accommodate learners.

## **Assessment**

- It would be helpful to assess best practices and the return on investment for skills development so as to demonstrate the real benefits that can materialise as a result thereof.
- Substantive investments have been made by businesses in workplace experiential learning programmes, employee skill development programmes, higher education environment and tertiary education. These can be scaled into the broader economy.
- The institutional and regulatory framework is complicated, fraught with governance challenges, perceptions of patronage, and it is not delivering the required skills to the country.
- Maladministration is a significant problem with a number of SETA's under administration, with billions of Rands not being disbursed as required by the legislation.
- Despite an annual contribution of R17bn by business to skills development through the 1% skills levy, and an estimated further R15bn – R20bn through voluntary and sector Code and Charter related initiatives, there is insufficient directing of funding to business-relevant skills development. Business is increasingly disillusioned by being unable to work with their SETAs to support their own, and broader skills development for the sector.
- Small and emerging enterprises do not have access to sufficient employees with work-ready skills and have limited ability to secure skills development for their staff. There is no accessible pool of skilled staff that can be relied upon and the institutional framework is too complex to enable emerging enterprise to operate competitively with the benefit of skilled staff.
- For the large part, business has not collectively taken the lead in driving the development of the requisite skills to make businesses, sectors and the economy more competitive. Business has generally not actively participated at a sector level. Increasingly in SETAs, business expertise and insight in driving relevant skills has been outweighed by other constituencies and the Department's emphasis on the unemployed.

## **Shifts Required**

- Focus on building solutions to address the impact of the Apartheid legacy on the basic education system aimed at improving the quality of staffing and the school curriculum. Business should give consideration on how, through mechanisms such as the National Education Trust, it can contribute in this regard.
- Promote, at business, sector and national levels, a more demand-led approach to skills development. This requires an overhaul of the institutional and regulatory framework, including the SETAs, to make the system more adaptable.
- Assist in ensuring that all business funded public systems, structures and programmes should be fit for purpose, free of maladministration and fraud.
- Focus on enabling emerging enterprises to access post-school education and training systems so as to draw work-ready, skilled youth and enable them to grow and develop.
- Partner with government to optimise the post-school education and training system. Resulting in a collaborative, co-designing social partnership that meets present and future needs,

including the co-design of the Tertiary Vocational Education and Training system, SETAs and qualifications authorities.

- Proactively investigate how to expand access for youth through enhanced apprenticeships and learnerships and work integrated learning experiences.

## SOCIO-ECONOMIC DEVELOPMENT

### Key Challenges

- Data and information on SED investment by the private sector is not readily available.
- Significant financial and human resources are expended by the private sector on socio-economic development but efforts are fragmented, sometimes duplicate the same beneficiaries and leave gaps in other areas.
- There is wide ranging spend spanning, areas such as education, entrepreneurship, health, housing and sport. However, there is a need to comprehensively evaluate the return of investment and best practices in relation to socio-economic development.
- Corporates have tended to focus on larger, well administered and already better resourced SED organisations to the detriment of smaller grassroots organisations and those in township areas.

### Assessment

- Embedding SED into business strategy limits collaboration opportunities.
- There is wide ranging spend spanning on education, entrepreneurship, health, housing, culture and sport. While SED investment is outside the scope of normal business, corporate citizenship and the triple bottom line makes this an important contributor to transformation.
- The effectiveness of socio economic development spend is however impacted by public services and resources outside of business' control.
- Scalable widespread projects and initiatives will go a long way to enhancing SED.

### Shifts Required

- Find mechanisms to support basic municipal services as the foundation for value added SED.
- Form a body of SED best practice that can be scaled with greater efficiency.
- Do more on a sector basis to target and expand specific SED outcomes pertaining to health, education and employment.
- Form strategic partnerships and collaboration in order to amplify the impact of SED.

## THE PROCESS TO ACHIEVE THE END-STATE

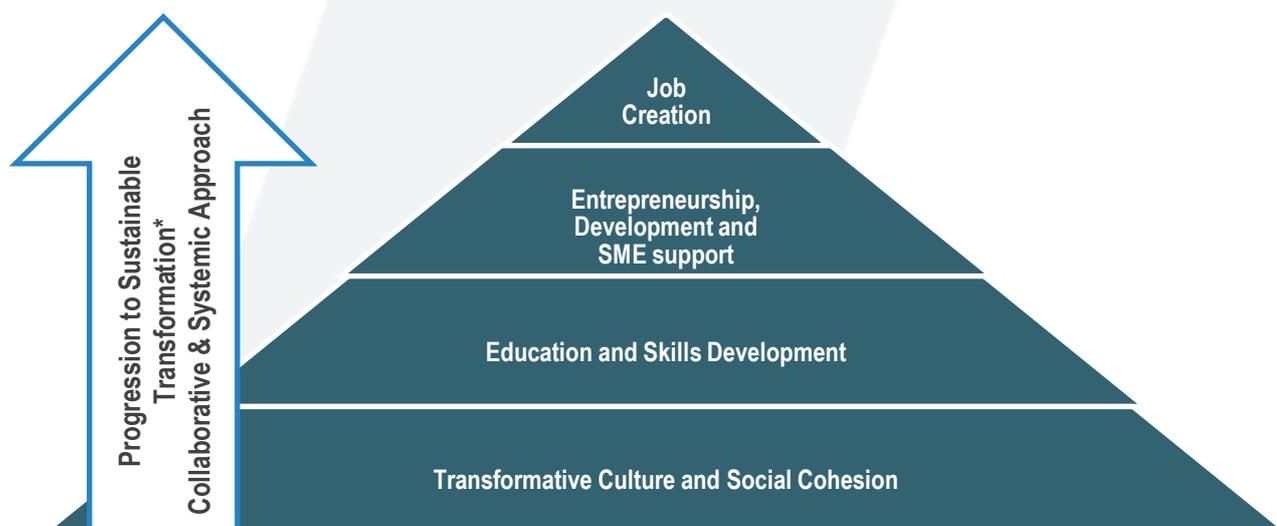
A Business Approach to Economic Transformation will be enabled through an emphasis on education and skills development, job creation, particularly among the youth and enterprise development and SME support. This section identifies the pivotal enablers required by business and Government to deliver the required interventions.

The process to arrive at the end-state is critical. A concerted and collaborative effort between Government, business, and organised labour will not only result in better solutions, with higher prospects of successful implementation, but it will also visibly demonstrate the joint commitment by social partners to act in the national interest. The journey and partners on this journey, have a critical role in demonstrating the necessary social cohesion that will deliver the desired end-state. Key elements of the process include:

- An approach that acknowledges the complexity of transformation, critically evaluates the challenges as well as the progress made.
- An approach that is adaptable, and regularly unblocks systemic and sector related challenges to Inclusive Growth.
- An approach that includes recalibrating the measurement of B-BBEE to focus more effectively on substantive transformation, value and influence.
- An approach whereby business plays a far more active role, in co-operation with the State to create enabling conditions at a sector and sub-sector level for businesses of all sizes across all sectors, with a particular emphasis on the support of black business.

The Business Approach requires a progressive, systemic, scalable and sustainable approach to Economic Transformation through the following key interventions to deracialise the economy:

- Inculcating a transformative culture within businesses and building social cohesion.
- Quality and demand-led education and skills development requires enhanced support to basic education and a significant review of the current institutional skills structure so that skills development is demand-led by current and future business needs.
- Blockages to employment need to be cleared, with systemic interventions promoting sustainable youth employment being scaled and supported.
- Large scale enterprise development includes expanding opportunities and removing regulatory and other exclusionary practices that constitute barriers for emerging black enterprises. Sector programmes to systemically enhance the capability of sectors need to be developed or enhanced.



\* Economic influence, value and control, is substantially achieved through all these elements

## WAY FORWARD

At the outset, it was made clear that this Business Approach is not meant to be the masterplan, but an important step in consolidating a comprehensive and collective approach by business. In this regard, the following next steps are identified for business:

1. Work within business and with government and organised labour and build strategic partnerships to deliver Economic Transformation, using Nedlac more effectively for robust engagements. A key intervention must include fighting corruption, maladministration and attempts at State capture which undermine Economic Transformation.
2. Business needs to enhance its contribution and lend its weight and capabilities to transformative programmes, identify barriers to Economic Transformation and work with institutions such as the B-BBEE commission, SETAs and Employment Equity Commission.
3. Explore, with government, mechanisms to comprehensively and consistently measure Economic Transformation.
4. Partner with government to introduce into the socio-economic regulatory impact assessments process specific considerations for the impact on Economic Development and SMEs, employment, investment and skills development and address barriers to doing business.
5. Rapidly explore, define and implement 4 key elements that can significantly contribute to transformation and social cohesion:
  - Element 1:** Enable a transformation culture in business, with systemic initiatives and developing a research base that demonstrates the economic value of diversity
  - Element 2:** Enterprise development support, including how to scale and support the Black Industrialist Programme, industry development programmes with sectors and leveraging the SME Fund
  - Element 3:** Skills development for current and future business needs, including leveraging the Ikusasa Student Financial Aid Programme and implementing a widespread mentorship programme; and
  - Element 4:** Employment promotion, particularly of youth, including the YES initiative and other systemic contributors to sustainable employment
6. Develop a statement of intent, whereby businesses of all sizes, formats, types, regardless of the ownership structure and composition, can make a conscious commitment to a deracialised and inclusive South African economy.