

# **THE UNSEEN SECTOR: SUPPORTING MSMES, CREATING JOBS**

## **WORLD BANK GROUP REPORT ON THE MSME OPPORTUNITY IN SOUTH AFRICA**

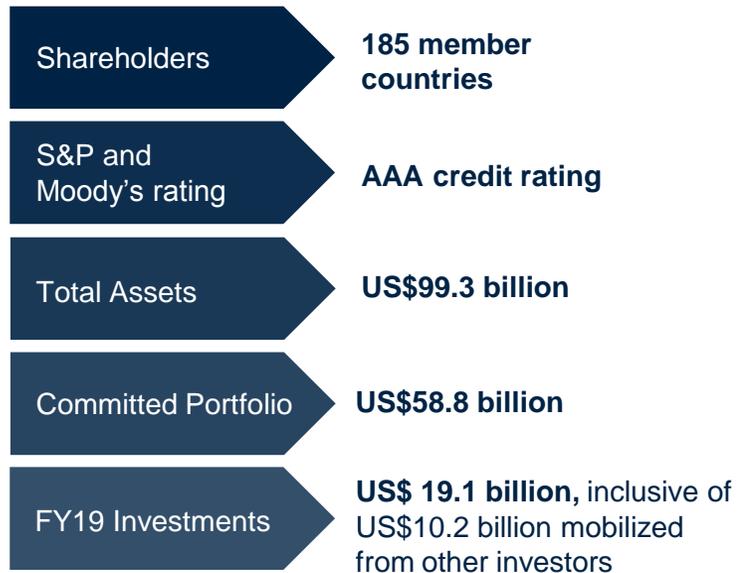


*Creating Markets, Creating Opportunities*

Portfolio Committee on Small Business Development  
13 November 2019

# IFC: A member of the World Bank Group

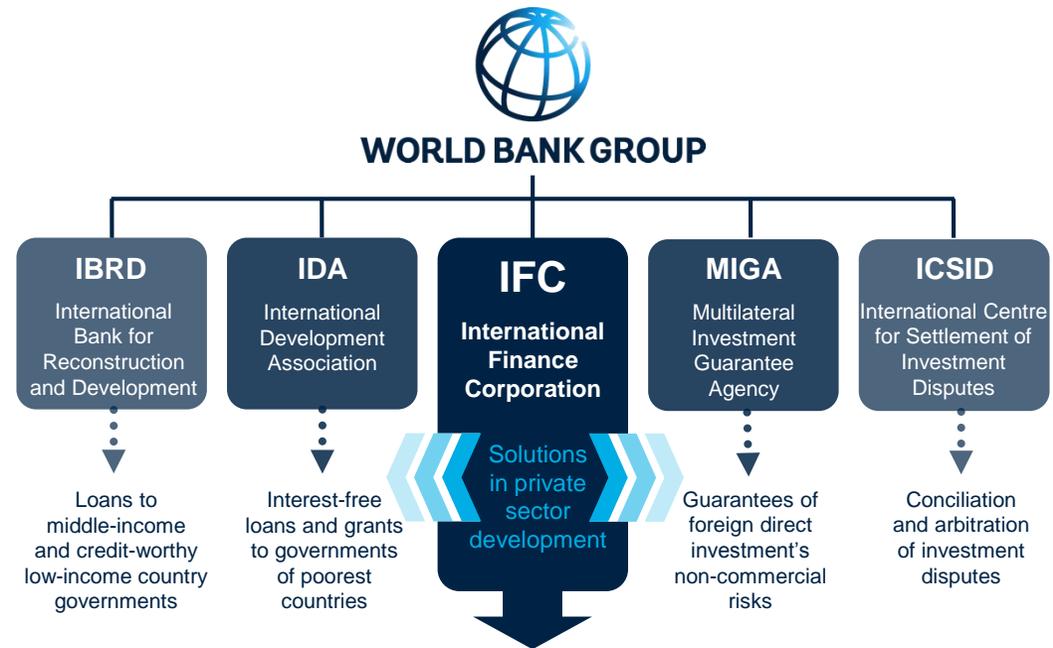
## Overview (FY19)



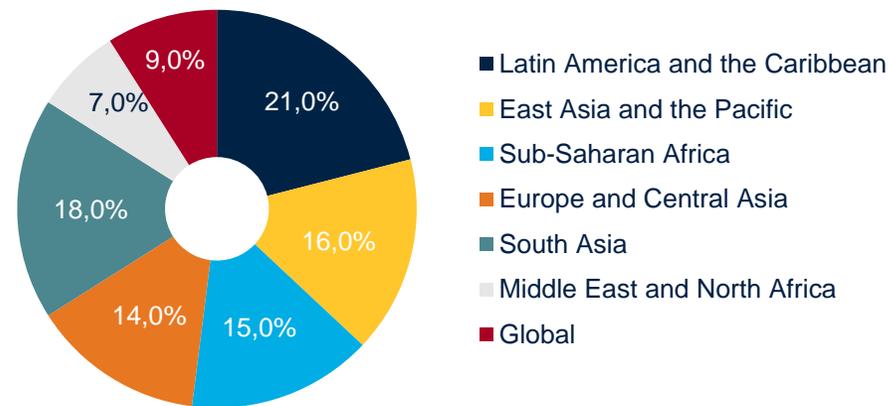
More than **100** regional offices present in **93** countries worldwide, AAA credit rating

**3744** Staff (54% are based outside Washington, DC)

## WORLD BANK GROUP



## IFC Own Account Commitment By Region



# IFC Financial Institutions Group: Integrated Solutions, Increased Impact



3 Product Areas

## Investment

Loans, Equity, Trade Finance, Syndications, Derivative and Structured Finance, Blended Finance

## Advisory

Value-adding knowledge; either integrated into IFC investments or standing alone at a broader level

## IFC Asset Management Company

Mobilizing and Managing Capital for Investment



4 Focus Industries

Financial Institutions (FIG)

Manufacturing Agribusiness and Services

Infrastructure and Natural Resources

Telecommunications and Information Technology



11 Business Lines in FIG

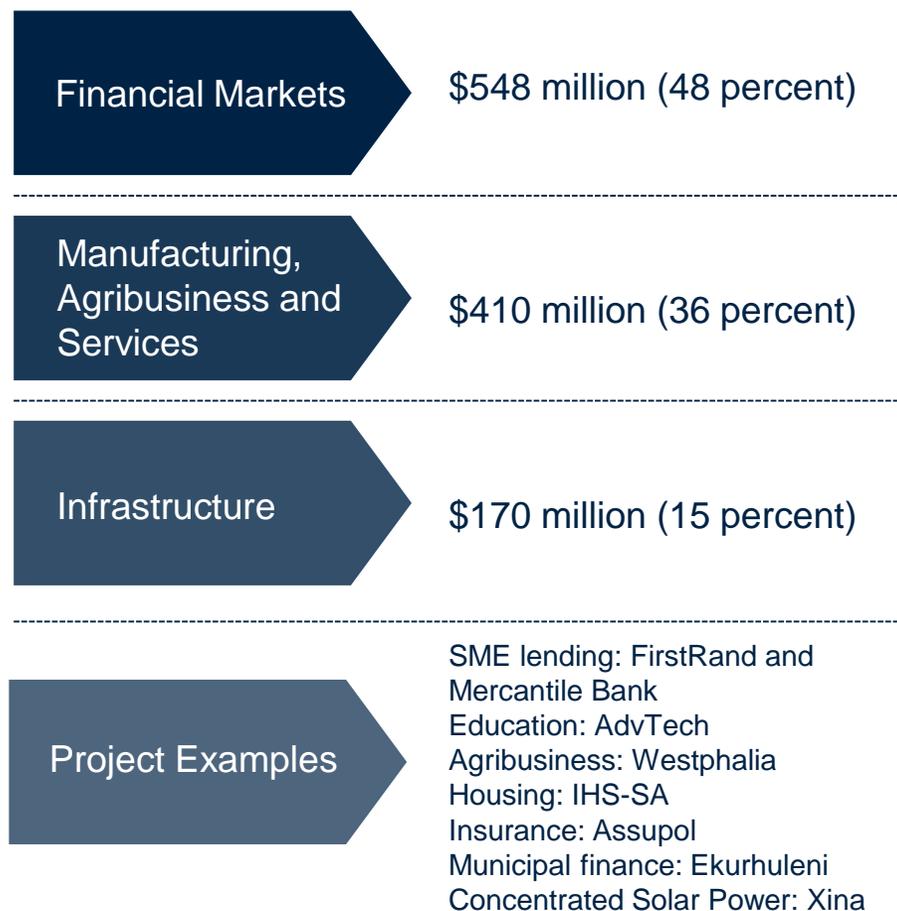
- Distressed Asset Recovery
- SME Banking and Finance
- Microfinance
- Insurance and Pensions
- Digital Financial Services/ Alternative Delivery Channels
- Capital Markets – Bonds, Securitizations (cross-cutting)

- Climate Finance – Sustainable Energy (cross-cutting)
- Banking on Women Program (cross-cutting)
- Housing Finance
- Trade Finance
- Trade and Commodity Finance

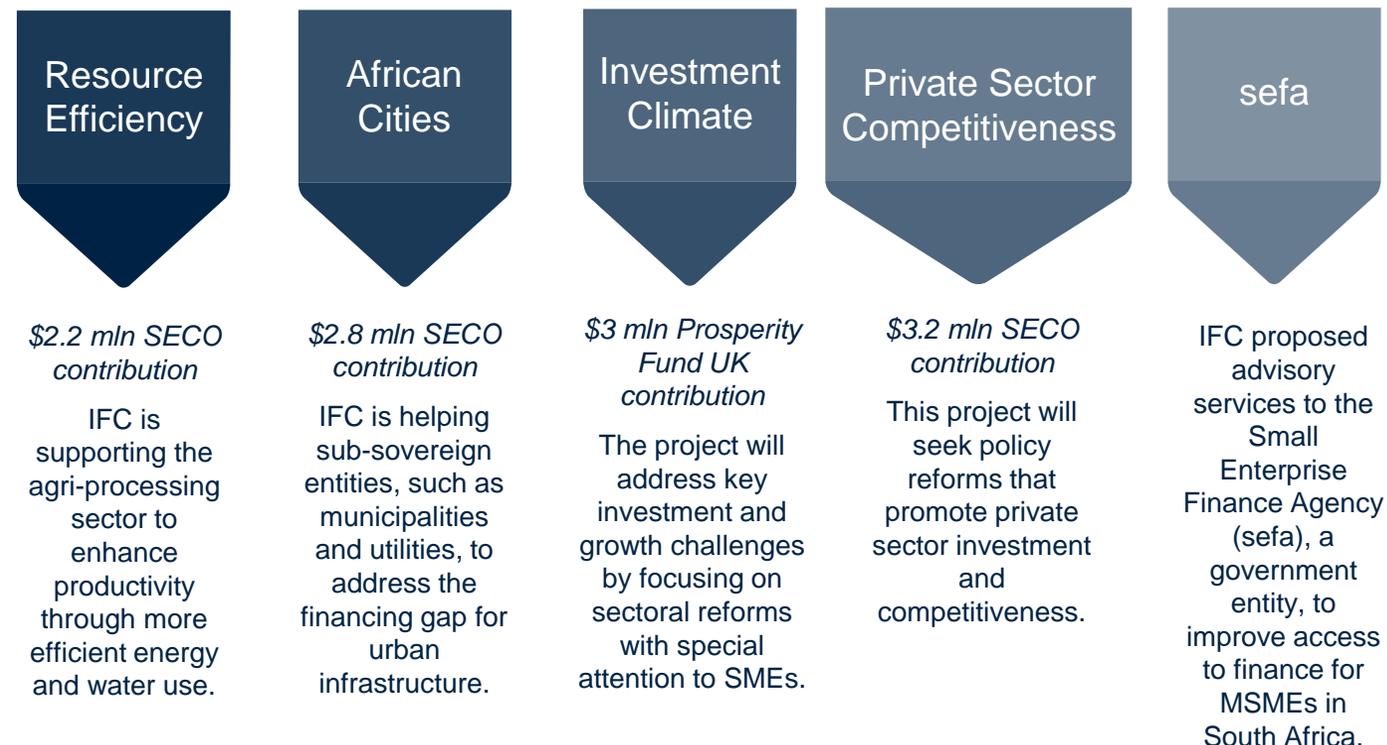
# IFC in South Africa: Where we work

IFC has been engaged with South Africa since 1991 and has a **current investment portfolio of \$1153 million (R17b) across 34 clients** and an **advisory portfolio of \$10.6 million across 20 projects**. IFC's Johannesburg office is the largest in Africa with around 180 staff.

## IFC Investment Portfolio



## IFC Advisory Projects





## The Unseen Sector

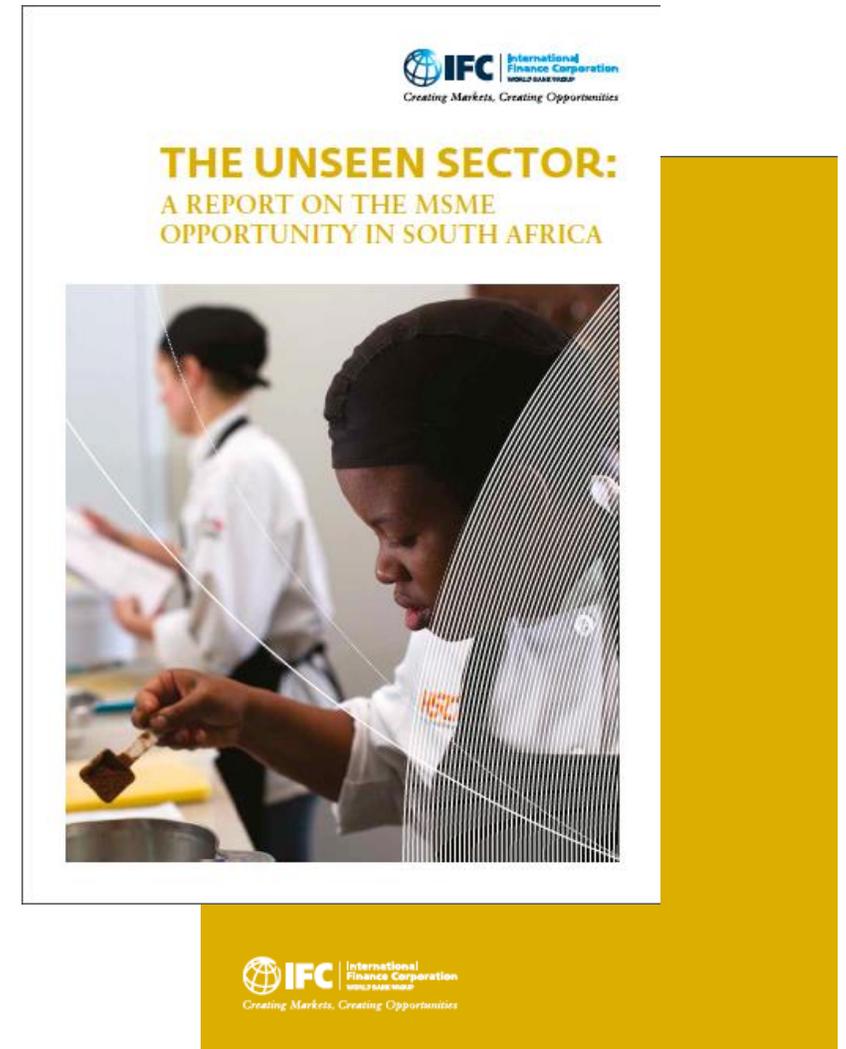
# The Unseen Sector: A World Bank Group report on the MSME opportunity in South Africa

“The Unseen Sector” is an in-depth assessment of the micro, small and medium enterprise landscape in South Africa. The report offers a [foundation for constructive dialogue between the public and private sector](#) to strengthen MSMEs and their contribution to the South African economy and job creation.

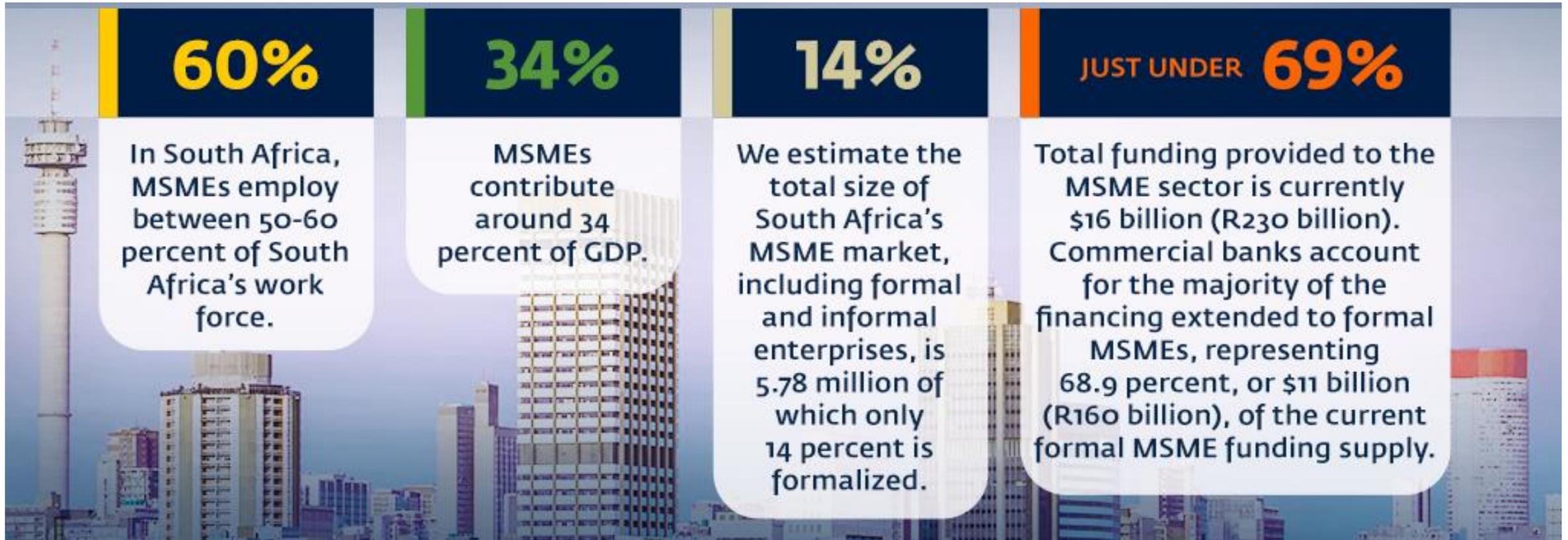
The report measures the [MSME sector size](#), [MSME financing availability](#) and illustrates [key barriers MSMEs face](#) in terms of access to finance, access to skills and access to markets in South Africa.

The report findings are generated from research and interviews on the business, financial and regulatory environment related to MSMEs. IFC and the World Bank produced the report with the help of Genesis Analytics in partnership with South Africa’s National Treasury.

“The Unseen Sector” forms part of IFC’s SME Push Program focused on optimizing the job creation potential of MSMEs.

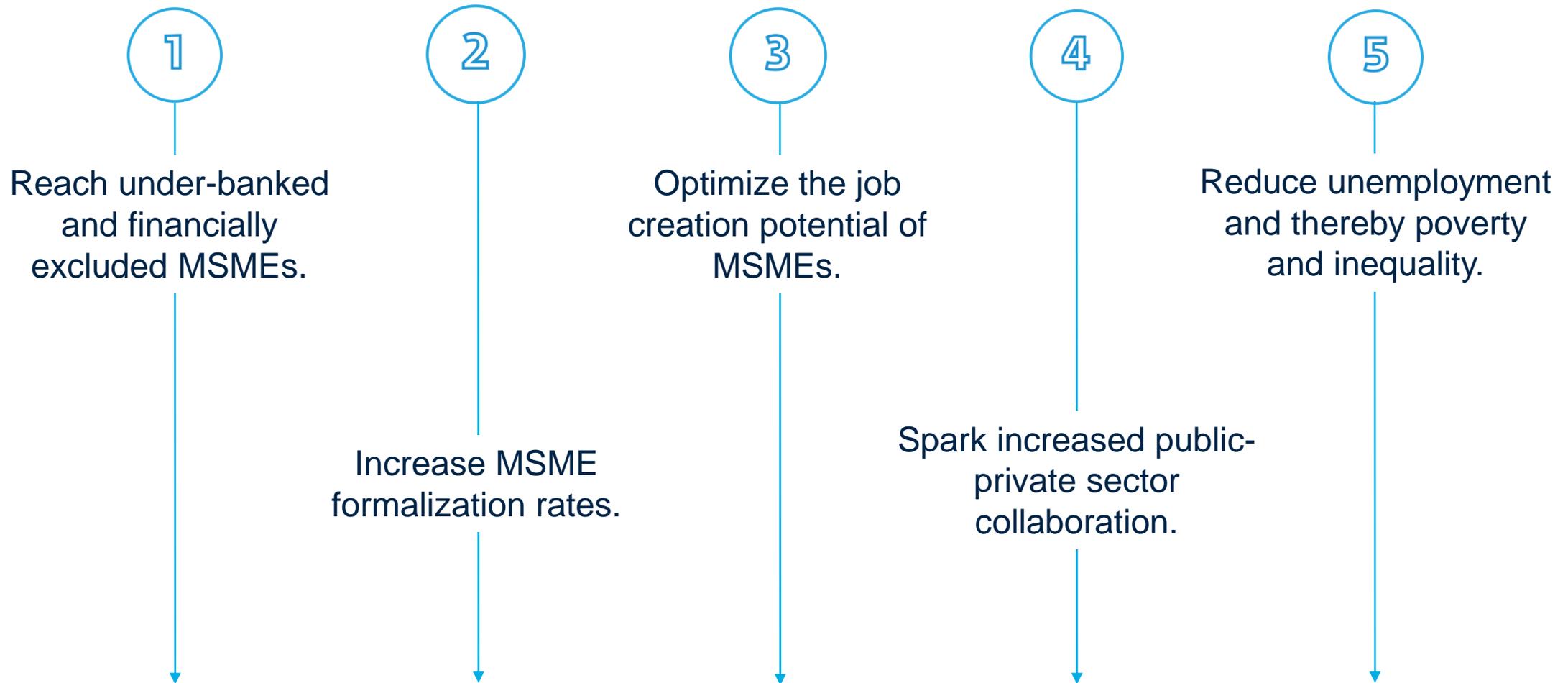


# What does South Africa's MSME sector look like?



# Our Goals

IFC works with partners to grow the MSME sector because we believe small businesses have a vital role to play in the economy. Our aim by producing this report is to:





# Key Report Themes

# The report's key findings demonstrate the big opportunity for financial and government actors to strengthen the MSME environment

There are many challenges to small business growth ranging from regulatory issues to finance access. We outline the eight key findings where we believe coordination between the public and private sector can make a big difference to MSMEs.



Stagnant Sector



Low Rate of  
Entrepreneurship



Bigger Than Expected  
Sector Size



High Level of  
Informality



Urbanization



Declining Black  
Ownership



Drop in Female  
Ownership

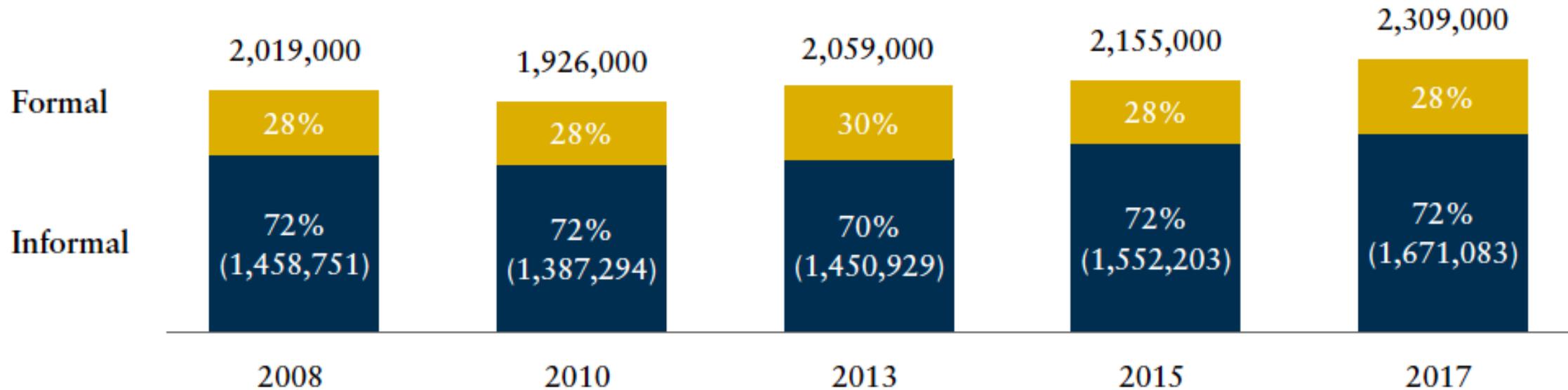


Limited Diversification  
of Funding Sources

# The MSME sector has been relatively stagnant over the last decade



The number of **MSMEs** grew by **14% between 2008 and 2017**. The limited growth in small business numbers indicates the sector is not making as meaningful a contribution to the South African economy as its potential.



# The total size of South Africa's MSME market, including formal and informal enterprises, is 5.78 million



Many micro and very small enterprises are creating opportunities for self-employment while only a few medium- to large-sized enterprises have the capacity to employ more people. Given the complexity distinguishing between MSMEs and sizing the market, the figure visualizes the market sizing data within a framework that separates survivalist micro enterprises from firms that are more opportunity-driven.

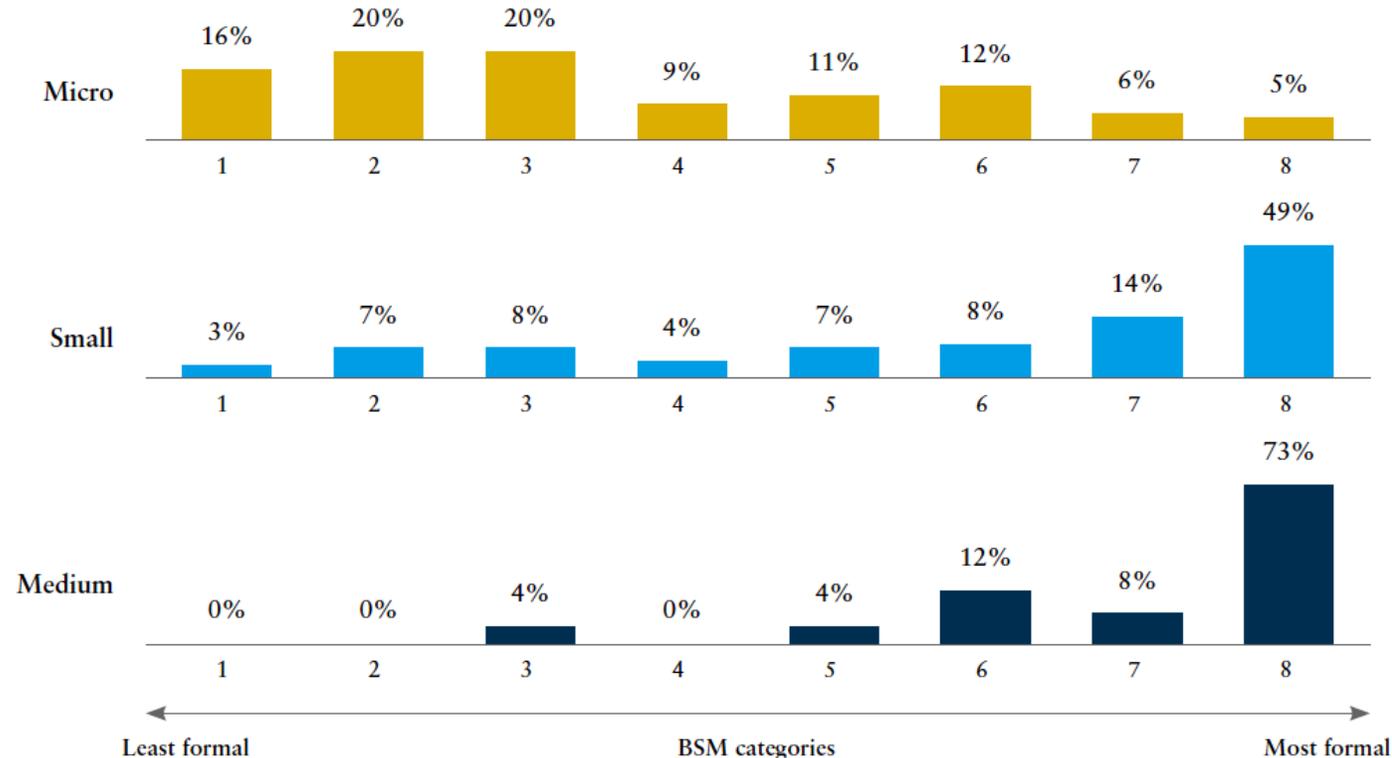


# Only 14% of the South African MSME sector is formalized



There is no commonly-agreed definition for small business formality in South Africa. For this report, we use if an MSME pays company income or value-added tax, as captured by SARS, to indicate formality. Counting the number of MSMEs operating in the informal sector is more difficult – the informal sector by nature comprises firms that are unregistered or that do not pay tax. The size of the informal sector is therefore estimated through surveys.

Distribution of MSMEs across the formality spectrum by firm size using annual turnover

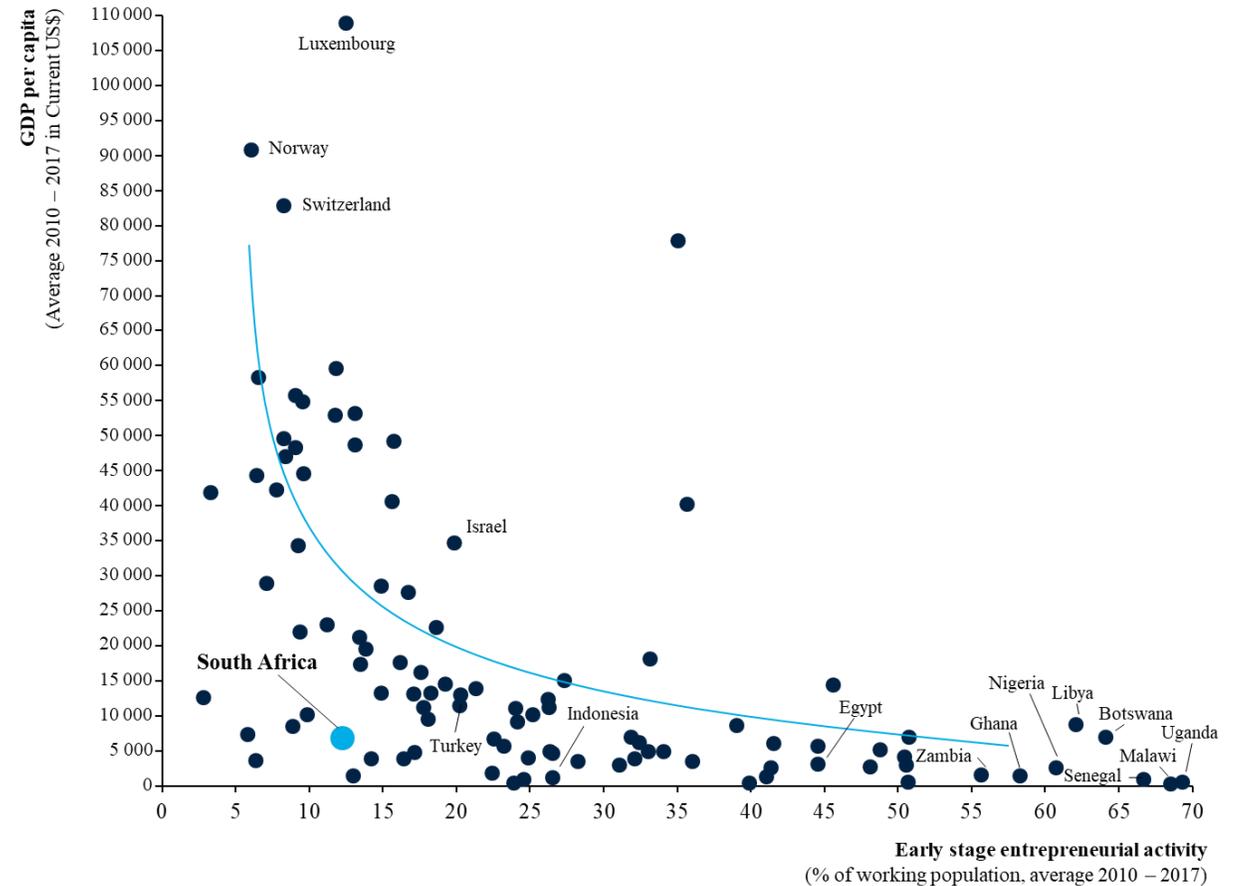


# South Africa's rate of established entrepreneurship is extremely low compared to other African countries



Data from the annual Global Entrepreneurship Monitor indicates countries with higher GDP per capita have lower rates of early-stage entrepreneurship because the economy is less reliant on small enterprise creation to provide employment. Given South Africa's GDP per capita, South Africa should have a rate of early-stage entrepreneurship three times greater than the current rate. With fewer start-ups and a low rate of survival, there is a thin pipeline of businesses with a high chance of scaling.

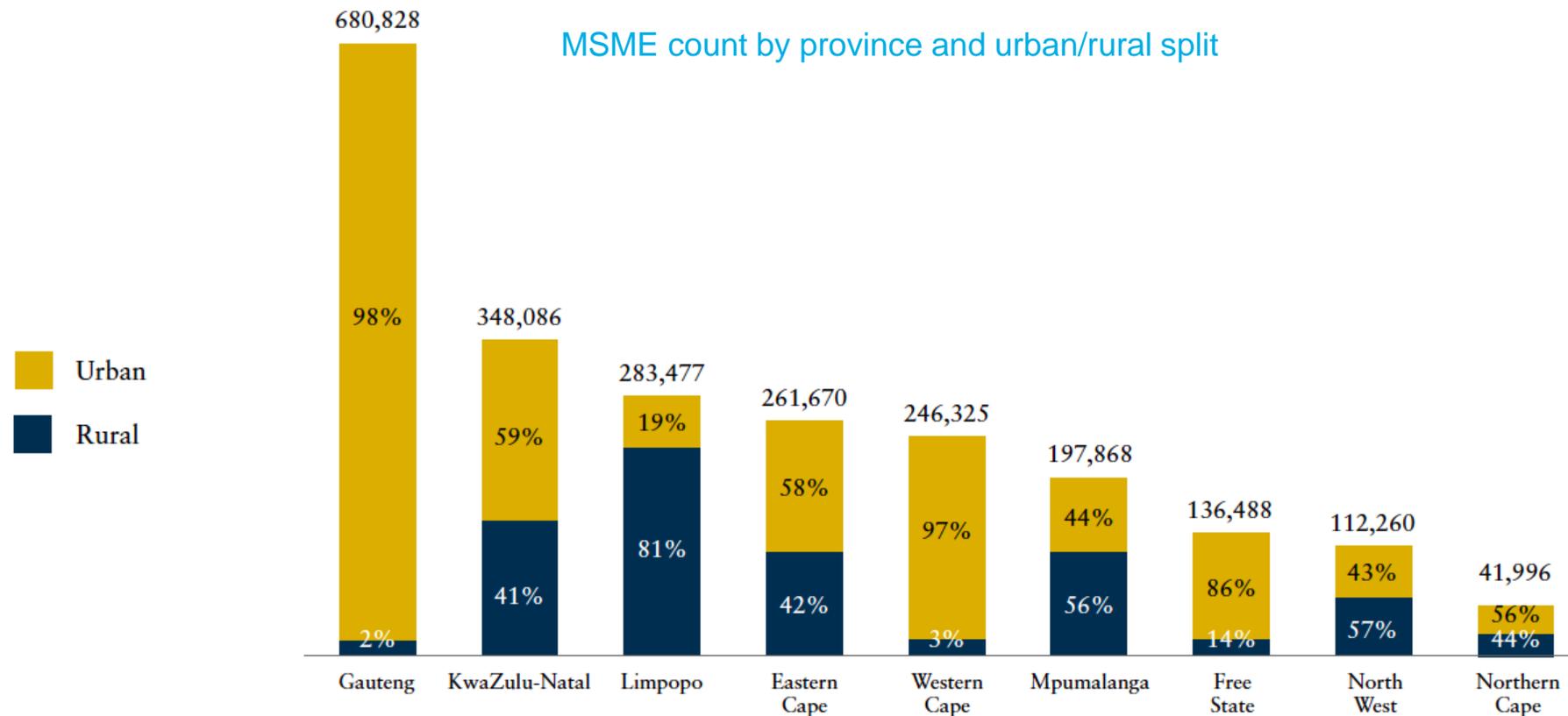
### Early-stage entrepreneurship and GDP per capita



# MSME activity indicates increased urbanization in the past 10 years



The proportion of MSMEs in urban areas increased to 69 percent in 2017 from 62 percent in 2008. This is similar to the urbanization rate for the whole population. Gauteng accounts for more than half of MSMEs and they are almost entirely urban, while Limpopo MSMEs are mostly rural.

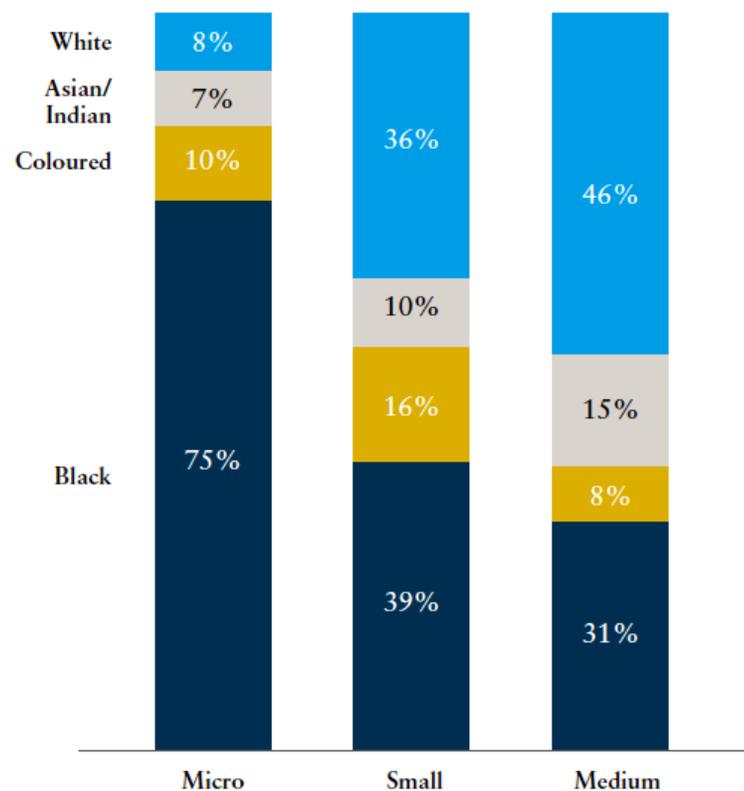


# MSME ownership reflects South Africa's socio-economic undercurrents



The data shows that black ownership has been declining in the past 10 years to 76 percent in 2017 from 79 percent in 2008, and that white ownership is disproportionately high relative to national demographics. Black ownership remains heavily concentrated amongst micro enterprises, and then decreases steadily as the size of the business grows representing less than a third of medium-sized enterprises.

MSME ownership by race



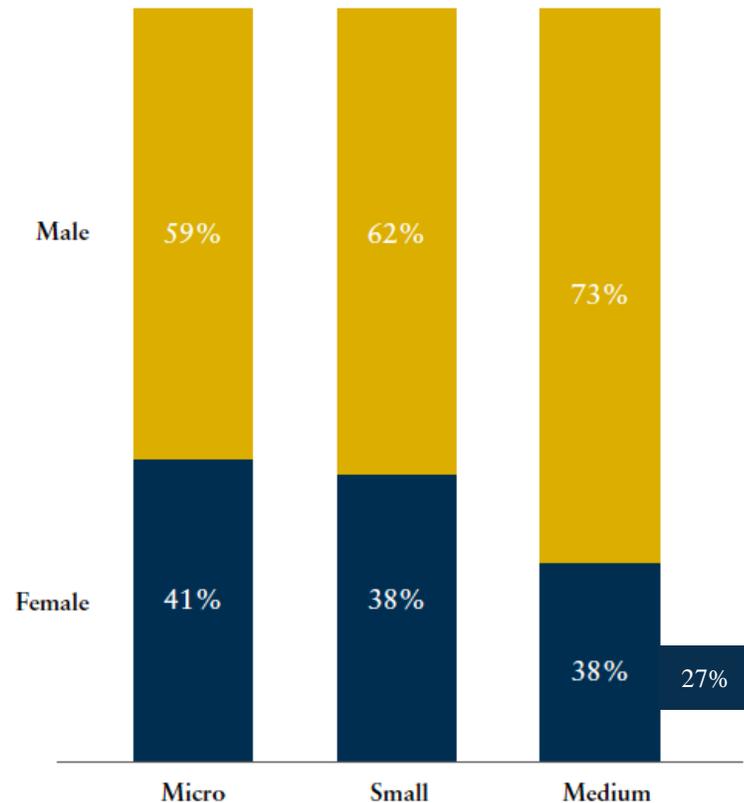
	2008	2010	2013	2015	2017
Black	79%	74%	71%	75%	76%
Coloured	6%	5%	7%	4%	5%
Indian/Asian	3%	4%	3%	4%	4%
White	12%	17%	19%	17%	16%

# Female MSME ownership is in decline, concentrated in the informal



Female ownership of MSMEs is more prevalent in the informal sector where the majority of micro enterprises are located. Overall, female ownership declined over the past decade to 38 percent in 2017 from 48 percent in 2008.

MSME ownership by gender



	2008	2010	2013	2015	2017
Male	52%	55%	60%	62%	62%
Female	48%	45%	40%	38%	38%

# Total funding to the MSME sector is currently \$16 billion (R230 billion)



Expanding access to finance for small businesses can help firms move along the ladder of formality, to grow their businesses and employ more people. MSMEs access finance from a range of institutions. For each credit provider, the table shows the typical MSME segment that the provider serves and provides an estimate of the quantum of MSME financing. Commercial banks account for the majority of financing extended to formal MSMEs, and government and microfinance institutions account for the bulk of finance extended to the informal sector.

	Banks	MFI	PE/VC	AltX	Fintechs	Government
Typical segmentation						
Estimate of financing volume	Aggregate loan portfolio of R160 billion	Total unknown – business loan portfolio upward of R1.5 billion	Allocation to MSMEs unknown – estimate of R36 billion for PE and R3.5 billion for VC	Market capitalisation of R12.95 billion	Total unknown – lending upward of R500 million	Upward of R17 billion

# Financial services to the informal sector needs to be strengthened



Currently funding support to survivalist enterprises and informal small businesses is largely channeled through the microfinance sector. The microfinance industry carries a number of challenges including poor financial literacy amongst borrowers, lack of required FICA documentation, high levels of indebtedness, and the use of loans for consumption rather than productive purposes – all of which make this a high-risk segment to serve.

## Sector contraction

Both the Development Microfinance Association and Microfinance South Africa have experienced a contraction in the sector due to the scarcity of donor resources and pressure on financial sustainability.

## Burdensome regulatory environment

MFIs are subject to the same set of regulations as banks including the FIC Act, Protection of Personal Information Act, National Credit Act, caps on interest rates and credit life fees, data collection and submission requirements. As a result, South Africa has a significant number of invisible and illegal credit providers.

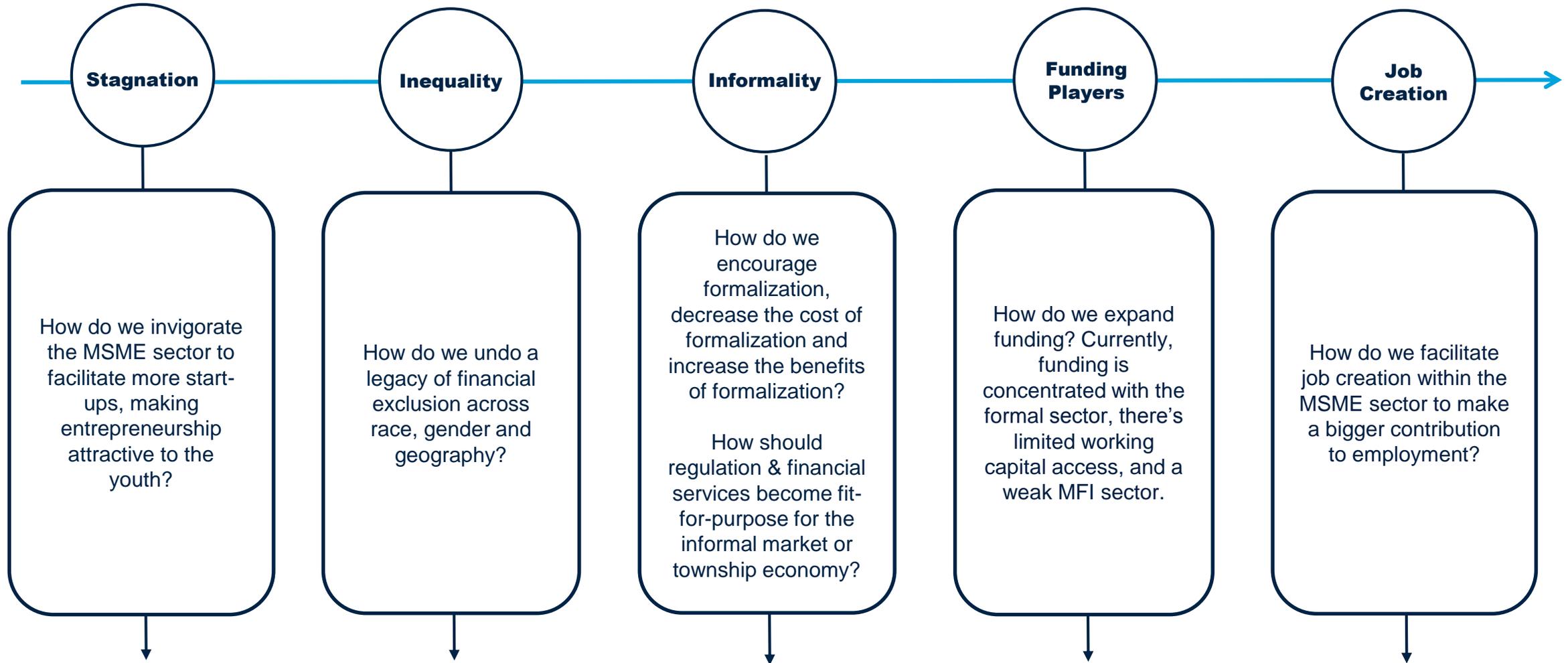
## Cost of reaching the financially excluded

MFIs carry the upfront cost of assisting potential borrowers to become funding ready as well as the ongoing cost of financial literacy training, high staff turnover, manual reconciliation processes, operational controls to prevent fraud, the cost of physical rather than electronic and automated credit evaluation, travel costs and the cost of disbursement and collection processes, which utilizes bank infrastructure in a model that is very dependent on cash, and in particular, coins. As such, for-profit microlenders struggle to profitably serve high-risk clients profitably, meaning potential customers are forced into an unregulated illegal microlending market.

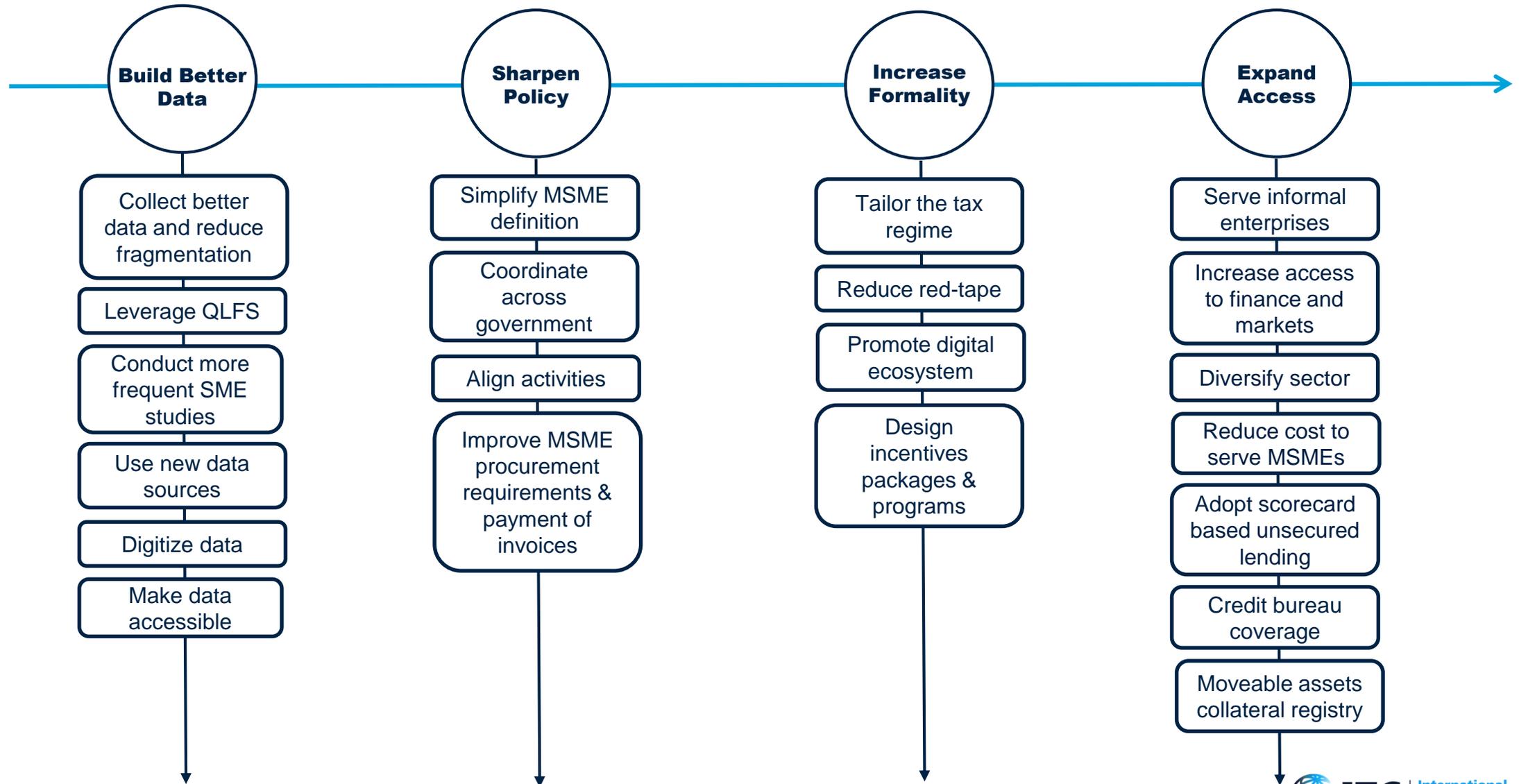


## Recommendations for Action

# The Big Issues



# Recommendations to build a stronger MSME sector



# What's next? The Unseen Sector study was followed by a second phase of research to hear from the small business owner



The objective of the second phase is to perform an in-depth assessment of the MSME owner financial needs and obstacles to access markets and finance. The findings should inform solutions to unlock finance channels and market entryways for small businesses, with a focus on both the formal and informal sector as well as male and female ownership differences.

- A qualitative study which comprised of in-depth open-ended interviews with 45 MSMEs
- A quantitative survey amongst MSMEs to gain representative insights on financial product penetration, financial needs, challenges, use of different financial service providers/market share statistics, etc. across geography, size of business, sector and gender as well as specifically unpacking differences between informal businesses (sample of 1000 MSMEs) and formal businesses (sample of 1555 MSMEs)
- The above, at a combined level of 2600 face-to-face interviews allowed us to determine and provide a MSME market segmentation for South Africa
- The report, combining the insights from the qualitative interviews, informal and formal quantitative surveys and MSME market segmentation for South Africa will be available in November 2019

# Empowering Small Business in South Africa: World Bank Group Initiatives



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