

Bee retooled:

Steps in the right direction

An interview with **Rob Davies**

South Africa's minister of trade and industry. Ben Turok interviewed him on 5 November 2013

BEN TUROK: Let's talk about black economic empowerment (BEE) and the perception of how effective government strategies have been so far. I'll start with a favourable comment by Thami Mazwai, who says, "BEE reverses the effects of [discriminatory apartheid] policies and gives blacks special opportunities to enter the economy. Since its inception, BEE has produced scores of successes, but we need hundreds more." ("Treasury continues to fail black business", *Business Day*, 16 October 2013).

That's a very positive statement. Do you think it's a fair one?

ROB DAVIES: When this administration took office and President Zuma appointed the BEE Advisory Council, we looked quite critically at what had been achieved. It is true that there have been some successes in BEE, but we found in 2007 that the overall level of performance of the private sector in South Africa was BEE Level 7, which is almost non-compliance. It's just off the bottom: Level 8 is completely non-compliant.

Also we found that there was far too little performance in those parts of the programme that were intended to support black entrepreneurs through "enterprise development" and "supplier development". And yet, that part of the [BEE] scorecard is actually quite critical. To create productive entrepreneurs in this economy, we actually do need to have relationships, not just in supplying government, but also in supplying bigger companies, to develop something of the symbiosis there is between big and small companies in successful Asian economies.

On the other side, we found a considerable amount of – what I can say – "passive shareholding": deals that shaded over into fronting. The stereotype of fronting is that the cleaner or the gardener is called the CEO and the company presents itself as black-led, while the real control is in the hands of some white executive somewhere. That very crude form of fronting doesn't exist much anymore. What we've got is more complex fronting, where people enter into a deal thinking that they're going to be significant players on the board and then find themselves pushed into some subordinate role. The company concerned is entering into this deal because it wants to present



itself to government for some benefit as a black-empowered company.

Sometimes, too, we found that, if you pay a bit more to the verification agency, you can go up the scale. And all of this was detracting from the impact that BEE could have.

AMENDING THE BEE ACT

So we introduced an amendment bill, and one of the main things it does is to introduce a statutory definition of fronting. Up to now, the only way to deal



with a case of fronting is through the common-law definition of fraud. Of course, it is fraud – because you’re presenting yourself as something you’re not in order to gain economic benefit – but it’s difficult to follow through with that sort of criminal process. So we’ve introduced a statutory definition of fronting. We’re also introducing a commissioner who will receive complaints about fronting. The commissioner can try to find solutions, but in the case of out-and-out fronting, the commissioner can also resort to legal remedies, take people through a judicial process. If convicted, they can go to jail. They can also be barred from doing business with government. So that’s one of the main things that we’ve introduced there.

We’re also regulating the verification industry, which has not been subject to regulation up to now. We’re also bringing the [sector] charters into line with the [BEE] codes – something that’s been long outstanding. We’ve also made some changes in the codes themselves, which are secondary legislation. The gist of them is to say, “Well, you’ve been able to earn points for all these sorts of things, but we don’t see enough performance.” And that refers to three priority areas. One is a new category called *supplier development*, which was previously “enterprise and supply development”. We’re saying that you actually have to achieve 40 percent of the target. You have to do the same in *skills development*. And then you can’t just perform there and not deal with ownership, so we’re going to do *ownership*, as well. And if a company doesn’t achieve 40 percent of the target in those three categories, then it goes down one level. So if you were BEE Level 4 and you don’t achieve the minimum, you go down to Level 5.

Another thing we found was that small black companies looking to perform with big companies have often been told they must go to a verification agency and spend R30–40 000 to get a certificate to say that they’re black-empowered. We’re saying this is nonsense. This is red tape, bureaucracy gone wild – private bureaucracy, if you like.

From now on, what will happen is that a 100-percent black-owned company will automatically be recognised as Level 1; if it’s 50-percent-plus-1, it will be Level 2. Anybody who deals with these companies will have to accept an affidavit. If they think you’re lying, they go to the commissioner instead of making you get an expensive verification certificate. So we’ve eased the burden for small black-owned companies.

Those are the main changes that we’ve tried to bring about. We think that BEE has scored some successes, but not enough in the areas that we have tried to focus on. And also we need to align BEE with the direction we’re trying to move, in terms of business development.

The president has asked, “Where are the black industrialists?” and this is actually the next big project

Everything that we’re doing is to support the emergence of real productive entrepreneurs among black people who can be suppliers of real value-added goods and services to both government and the private sector. And where they do participate in big companies, that they are part of effective management and decision-making leadership in those companies.

for the BEE Advisory Council: to work on a broader package of measures to support the emergence of black industrialists on a much more substantial scale in this country.

BT: It seems to me that this is a very elaborate way of making BEE more effective. People will say it’s very bureaucratic, very rule-based.

RD: Well, there were codes in place already. Those codes were being worked on by companies, who were scoring themselves or getting scored by verification agencies...

BT: With the help of many advisors and consultants. It’s spawned an industry.

RD: We’ve reduced the number of categories from seven to five. We’ve tried to make it easier, for example, for small black contractors.

INCUBATORS FOR ENTERPRISE

The point I want to make is that we don’t see BEE as the only tool to achieve those kinds of transformation. We’ve been rolling out incubations and an incubation-support programme. We now have approved 30 projects. I rolled out the first of these in Sasolburg, the SASOL ChemCity ...

BT: What is an incubator?

RD: It brings together a group of entrepreneurs who are beginning to develop a particular line of business.



It involves access to machinery and equipment in their sector, and a physical location to access informal mentoring from more-established people. They probably also get some formal training. And basically they go through the process of setting themselves up as a real productive-sector entrepreneur.

BT: And these are black businesses?

RD: They are. These programmes have been very successful in many parts of the world, even in South Africa. But we have far too few of them. The Small Business Development Agency has increased the number that it is supporting – but it’s not the only support we’re providing.

This is now what we want to use the [BEE] codes for. We want supplier development. If a bigger company wants someone to supply an input, they don’t want bad inputs, and so they get involved in supporting those companies to become effective suppliers of what they need.

I went to a place in Japan called Toyota City, where you see a whole range of small companies that supply into Toyota dotted around the Toyota plant, all integrated into its supply chain. That’s the sort of model that we need. In South Africa, we have far too much monopolisation – the “same old same-olds” – and far too little opportunity for new suppliers to enter the supply chain.

BT: There are many countries where small enterprises are abundant.

RD: The problem that we have in South Africa is that small business among historically disadvantaged black people was not just neglected under apartheid: it was actively discouraged, discriminated against and disadvantaged. That’s the point. So when we talk about small business development in South Africa, we’ve actually got quite a backlog.

BT: How do you overcome the absence of skills and business culture?

RD: The DTI [the department of trade and industry] has latched on to the incubator programme. We need to increase that. The other thing we’re focusing on now is township entrepreneurship. We’ve had too much of a “ladder” mentality: that it’s all about people graduating out of the informal and into the formal sector. But actually, if people improve their productive capacity and their income-generating opportunities while still remaining in the informal sector, that can be a huge boost to inclusive economic growth. That’s our next big project in small business development.

Again, we try to use the tool of BEE, and earning BEE points, as a lever to encourage greater involvement in active supplier development. Because we think that small black businesses should of course be suppliers to the state – but they shouldn’t just see their horizons

as limited to the state. They should also be in supplier relationships with private companies.

BLACK BUSINESS CRITICS

BT: Let’s turn to an article in *Business Report* (4 August 2013) by Hlengani Mathebula, chairperson of the Black Business Executive Circle. This is a rather damning article. He complains about the apologetic nature of BEE, that it’s an afterthought and not a central policy of government.

RD: I haven’t read the article, so I don’t know how the conclusions are reached there.

I would make the simple point that BEE is a matter of equity, social justice and a political imperative – but it is also an economic imperative. If our economy is going to be managed, organised, led by people drawn from only a proportion of the population, and if the access to jobs and everything is going to be limited to that part of the population, then we’re going to deprive ourselves of an economic opportunity, of drawing on the talents, the abilities and the spending power of a much larger part of our population. That’s the economic imperative.

Has BEE lived up to what it promised, or should have delivered? Well, I said already that we made a critical review and we don’t think that it had enough of an impact, or the right impact. Which is why we’ve introduced changes in the law and in the codes.

BT: First of all, Mathebula says that BEE is a threat to the local retail industry. He says that business should wake up and be part of the global market, the huge overseas market. And that this is something that should spur BEE. Do you think that BEE threatens local retail?

RD: The retail sector in general? I think we are looking to encourage the retail sector to work with the local productive industries, so that the retail sector becomes a tool of development of the productive forces of our country. There are a number of dimensions to that. For example, some of the retail firms in the fashion and clothing industry are working with local clothing manufacturers, and this has led to something of a new revival. Those are the kinds of relationships we’re seeking to build. I don’t know what the other problems of the retail sector are, that are identified there [in the article], but we support the retail sector becoming a vehicle for much more support for local manufacturing.

BT: Well, he seems to suggest that government is trying to confine black people to tuck shops and hair salons. Is there any truth in that?

RD: Part of the thrust is for black people to become involved in the productive economy and we’re responding to the call by the president for the creation of many more black industrialists. That’s what the changes that we’ve made up to now are intended to



contribute towards. And as I said already, the next big project of the Black Economic Advisory Council is to look at a broader set of programmes to try to achieve that.

We would say that the ability of black industrialists to emerge and to become globally competitive exporters would actually be desirable. But let's start where we can start. We don't have tons of people who are poised to play that role right now.

BT: The next argument refers to the loan given to Luminance [Ndalo Luxury Ventures]. Mathebula says, "Luxury industries are not immune to empowerment. They're not the preserve of some and not others."

RD: We went in some detail through the Luminance transaction and we met with the [parliamentary] portfolio committee. We said there that there are no holy cows: we can't say that some parts of the economy are not areas for empowerment. Supporting a luxury goods sector is not a problem *per se* for the National Empowerment Fund. But we did say that we need to look at how that retail outlet relates to productive activities in South Africa. That transaction, even the work done by the NEF, led to improvements in the local procurement of that particular enterprise. Their shop was supporting co-operatives and locally made products.

We also were concerned that some part of that loan finance was going to import finished stock. Where [state] entities are giving grants, loans or support incentives for the import of finished goods, there has to be a higher barrier – and the DTI needs to be part of that, as the executive authority and accounting officer. We need to be part of that decision.

We've issued a new instruction to all the entities that the provision of resources from the DTI should not, in general, be made available to support imported finished goods. And if the entity feels there's an overwhelming case – in terms of some economic argument – that there should be a variation from that, they must approach us and we must be part of that decision. That's what we said in terms of the Luminance transaction, and it gets back to what I've been saying about retail. Retail can be a tool to support local production and manufacturing. If government is providing resources and support for retail, that is what we want to see in return.

BT: Going back to Thami Mazwai. His article objects very strongly to the Preferential Procurement Policy Framework Act (PPPFA), alleging that black business is heavily discriminated against by the Treasury. Speaking on behalf of the Black Business Council, he says the Council

wants the Act scrapped as it negates the spirit of BEE. According to the Act, preference is given for BEE on the basis of an 80:20 formula for contracts

The problem that we have in South Africa is that small business among historically disadvantaged black people was not just neglected under apartheid: it was actively discouraged, discriminated against and disadvantaged. That's the point. So when we talk about small business development in South Africa, we've actually got quite a backlog.

worth R500 000 or less; and 90:10 for those worth more than R500 000. This means BEE will account for only 20 percent or 10 percent of contracts and the remaining 80 percent or 90 percent will be for pricing, expertise, competency, etc.... The Treasury argues that it must protect the taxpayer...

He uses some rather strong language: "It appears that the Treasury does not care a hoot what black business thinks." This isn't directed at your department, but Treasury is part of the cabinet and therefore there is a collective responsibility and you're part of those discussions.

RD: I know that the Black Business Council does support a change in that formula and they're very critical of the PPPFA. It's ultimately Treasury's call and it's work in progress.

But what we do need to safeguard is that, where we award preferential contracts and empower black-owned companies, we are actually empowering people to become real performers and real players. Not agents. I think that's going to be the thing. We don't want people who get a contract they can't carry out, then go to the white business and just add a premium for government. That model is not acceptable.

BT: How widespread is that?

RD: I don't know, but we hear many, many anecdotes about the price of things procured by government. We need, I think, to address that question frontally and substantially. The DTI is part of those processes, debates and discussions, which are not concluded at this point.



THE BOTTOM LINE

BT: I think that our readers would like some general observation from you about the feeling in cabinet concerning black entrepreneurs and the current style of doing business. Is there something generally worrying? Is there a considerable amount of genuine entrepreneurship that is productive and adding value? Is it a box-ticking system?

RD: Everything we're doing is to support the emergence of real productive entrepreneurs among black people who can be suppliers of real value-added goods and services to both government and the private sector. And where they do participate in big companies, that they are part of effective management and decision-making leadership in those companies. That's what all the work we've done is intended to achieve.

BT: How successful are you in promoting that?

RD: Again, it's work in progress. As we have been signalling that this is the direction we're moving, we see that there is a degree of progress – for example, in the research that was presented at the BEE Summit. We know that many black entrepreneurs who want to be productive do find themselves frustrated in one form or another, by fronting and things of that sort. That's what we're trying to deal with.

On the other hand, I don't know the extent or the numbers, but we know that there are people around – we come across them all the time – whose practice is simply to go to the established white-owned supplier to buy something, add a premium, and then sell it to government. We know that this is the case.

Government is unapologetically saying that we're not interested in that any longer. We're moving away from that model. You come along and say you can give us a value-added service? We will work with you to enhance your capacity to do that. We will support you in various ways. But the idea that we're going to come along and just allow you to rent-seek – which is what it amounts to – without in any way transforming social relations or ownership patterns or skills development? We're not interested.

BT: Are you able to actually build in and impose conditions like this?

RD: These are normally things that are built in by Treasury. I think their new Office of the Chief Procurement Officer is dealing those kinds of matters.

BT: But DTI doesn't build it into your contracts and programmes?

RD: As a department, we're not a big procurer. We don't have lots of tenders. But one of the things we have been pushing for is the designation of local content. We need consistency. So whoever is going to be a player – supplying to the infrastructure programme

or regular services in government – is going to have to start adding more value in this economy. To a decreasing extent are we wanting to sit around and buy fully imported products, and even less do we want to buy fully imported products from people who are agents, who are just adding a premium.

BT: Your department has had a long history of engagement with BEE. It's had black advisory councils going back to the days of Alec Erwin. Standing back, do you feel that all this effort has helped to create a progressive, productive, black middle class or business class? Or has it in fact facilitated – let me use a simplistic term – a parasitic category in our society?

RD: For many years after 1994, BEE was a policy focus, but it didn't have any shape or framework. It was only in 2003 that the BEE Act came into force, so we're talking about ten years of BEE legislation.

Before that, there were many models developed in the private sector, and a number of those had some element of fronting, some were enriching people as individuals. A lot of "recycling" and so on. The Act was intended to avoid all the identified weaknesses of BEE, to broaden it, and to create a lever whereby entities that seek a tender or a regulatory or other benefit from government have to show some performance in BEE. As I said, we've identified a number of weaknesses, and we're trying to strengthen the framework in the direction of support for more productive black entrepreneurs who are capable of adding value in this economy. That's what we're trying to do. Will it achieve everything we want? I doubt it. Is it a step in the right direction? I'm sure it is.

The institution that I've mentioned a few times, the BEE Advisory Council, was provided for in the Act and did not come into existence until the start of this administration. It is chaired by the president, and has been the sounding board, the advice centre, which has underpinned all the work we've done in this administration to try to improve BEE.

BT: Given that the main objective of the government and the ANC is to transform the economy, and given that the economy is heavily dominated and heavily monopolised, does this whole BEE process – even the productive aspects – make a dent?

RD: We shouldn't overload what BEE is expected to achieve. It's one policy instrument, one policy thrust, among several others. We also need to industrialise our country; to support small business activity in other ways; to address concentration, particularly where it results in undesirable behaviour like the cartels in the construction industry. There is a whole number of other instruments that need to come together. Of course we have to combine empowerment with all the other objectives we're trying to achieve. That's really the challenge. 🇿

