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Business development and local economic development in South Africa: addressing the disconnect

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Local economic development is a critical challenge for much of sub-Saharan Africa, particularly in South Africa. This article aims to examine the limits to successful local economic development (LED) in South Africa which emerge from the 'disconnect' between business development and LED. One reason for the disappointments surrounding 15 years of LED planning relates to this "disconnect" between business development and LED planning. This issue is now acknowledged as national government has launched a series of initiatives to develop the connections between enterprise development, on the one hand, and local economic development, on the other. The discussion points to four themes, namely the improved market confidence of the private sector in local government; the capacity to identify opportunities for and to exploit competitive advantage; the need to build a business environment friendly for private sector investment, and the intensification of enterprise support at local level for the development of small businesses.

Besigheidsontwikkeling en plaaslike ekonomiese ontwikkeling in Suid-Afrika: om die onverbondenheid aan te spreek

Plaaslike ekonomiese ontwikkeling is 'n uiters belangrike uitdaging vir 'n groot deel van Afrika suid van die Sahara, veral in Suid-Afrika. Hierdie artikel ondersoek die beperkings van suksesvolle plaaslike ekonomiese ontwikkeling (PEO) in Suid-Afrika wat uit die "ontkoppeling" tussen sake-ontwikkeling en PEO spruit. Een van die redes vir die teleurstellings die afgelope 15 jaar rakende PEO-beplanning hou verband met hierdie "ontkoppeling" tussen sake-ontwikkeling en PEO-beplanning. Hierdie kwessie word nou erken, aangesien die nasionale regering 'n aantal inisiatiewe van stapel gestuur het om enersyds die verbande tussen ondernemingsontwikkeling en andersyds PEO te ontwikkel. Die bespreking fokus op vier temas, naamlik die verbeterde markvertroue van die private sektor in die plaaslike regering; die vermoë om geleenthede vir mededingende voordeel te identifiseer en ontgin; die behoefte om 'n sake-omgewing tot stand te bring wat gunstig vir die ontwikkeling van die privaat sektor is, en die intensivering van ondernemingsondersteuning op plaaslike vlak vir die ontwikkeling van klein sake.

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The enhanced significance of locally driven development processes is a critical aspect of global development discourse (Christensen & Van der Ree 2008, Pike *et al* 2011).[1] Put simply, the advance of globalisation "gives LED strategies a bigger role to play in international development" (Rodriguez-Pose 2008: 24). Arguably, Pike *et al* (2011: 4) point out that the meaning of local and regional development is context-specific and often articulated in different ways in different parts of the world. One common thread, however, is that the activity of local economic development (LED) builds upon the economic strengths of each locality and supports the foundations for economic growth, such as productive investment and enterprise upgrading (Rodriguez-Pose 2008). Within an array of different contemporary interventions and practices designed to promote and encourage local development, the boosting of "endogenous" development processes, more particularly in the form of small business development, remains at the forefront of international debates (Pike *et al* 2006).

National governments can provide considerable support for small enterprise development programmes which can animate local economies (Rogerson 2011). Todtling (2011: 335) stresses that the policy focus should be directed to the developmental challenges and growth potentials of incumbent small firms, new firm formation and a strong focus on entrepreneurship. Hadjimichalis (2011) draws attention to how internationally SMEs have long been associated with local and regional development initiatives. Nevertheless, it is argued that scholarly focus in LED needs to shift away from the paradigmatic innovative and networked 'flex-spec' small firms which inspired debates on industrial clusters and 'industrial districts'. Instead, there is a great need to acknowledge the important role and contributions of what is styled as "everyday entrepreneurialism" which can contribute towards a more inclusive trajectory of LED (Hadjimachalis 2011: 382). It is contended that, while 'ordinary SMEs' are less flashy and famous than the 'paradigmatic' innovative small firms, they represent the predominant form of entrepreneurship and small enterprise development worldwide. In the global South, in particular,

1 The University of Johannesburg is thanked for research funding support. Wendy Job is acknowledged for producing the four maps.

the urgency to incorporate and support 'ordinary' small enterprise development as a central focus for LED is clearly evident from both Latin America (Gomez & Helmsing 2008, Vazquez-Barquero 2011) and sub-Saharan Africa (Nel 2011).

Over the past two decades several key influences underpin a surge of LED activity across Africa (Rogerson & Rogerson 2010, Nel 2011). Rodriguez-Pose & Tijmstra (2007: 522) believe the major explanations relate to "slow economic growth and poverty, combined with the changes in the national and international economic environment, and the effective inability of many central states to intervene at the local level have provided a fillip for locally based initiatives". Within scholarship and debates concerning LED in Africa, analysis of the South African experience is significant because of the extensive devolution and decentralisation of powers that has taken root in the country (Nel & Rogerson 2005, Turok 2010). However, it is evident that, while LED enjoys a "high profile" in development planning in South Africa (Stoquart & Schubert 2010a: 21), its developmental contribution often is assessed as suboptimal or disappointing (Marais & Botes 2007, Nel 2011). For example, one recent evaluation of the impact of European Union initiatives to support enhanced economic and social development in Limpopo from so-called 'strategic' partnerships formed by SMMEs concluded that it was "very limited" (Lyonette & Pearson 2010: 26). Another provincial assessment disclosed the impact of LED projects in the Free State as "a distressing picture" (Cohen 2010: 25).

Against the backcloth of the centrality of small business development for LED, this article aims to analyse the limits to successful LED in South Africa which emanate from the 'disconnect' between business development and LED. In national government planning documentation a number of core strategies are identified as essential foundations for the successful achievement of the goals of the 2006 National Framework of Local Economic Development (DPLG 2006). In essence, four strategies are deemed critical: to improve public and market confidence in local municipalities through good governance and enhanced service delivery; to identify and exploit local competitive advantage of 52 so-called municipal regions; to enhance the local business environment for private sector investment, and to support the roll-out of national government's Integrated Small

Business Development Strategy (ISBDS) and, correspondingly, to intensify enterprise support in local areas (DTI 2006a). These four themes represent the organisational architecture for this article. The analysis critically draws from a range of recent South African evaluations and key stakeholder interviews concerning the challenges of LED planning and its impacts for the period 2006-2010. The key argument in this investigation is that recently several important policy initiatives have been launched to re-connect business development and the activity of LED in South Africa.

1. Improved market confidence in municipalities

The 2006 National Framework made it clear that "improving confidence in municipalities is a critical first step in attracting investment and building loyalty to local areas" (DPLG 2006: 23). At the heart of strengthening market confidence in municipalities was the challenge to improve governance and service delivery of local governments. Support was to be provided to municipalities under a number of government programmes, such as Project Consolidate. It must be acknowledged that key support initiatives have catalysed some notable progress in terms of both increasing the extent of hands-on support provided to local government and creating a systematic mechanism and framework (in terms of five key performance areas) within which local government can work (DCOGTA 2009a: 12). The extent to which the goals of obtaining market confidence have been achieved has been limited, as is evidenced by the 2009 State of Local Government Report produced by the Department of Cooperative Governance and Traditional Authorities (DCOGTA), the re-styled DPLG.

Subsequent to the release of that report, DCOGTA launched the Local Government Turnaround Strategy, which is meant to recommit to the principles of developmental government (DCOGTA 2009a, 2009b, 2009c). This Strategy states that "nine years into the new Local Government system, despite impressive progress in many areas, local government is in distress and there are worrying trends and signs that are undermining the progress and successes achieved thus far" (DCOGTA 2009c: 2). The Turnaround Strategy commits that the goal of "growing our economy inclusively can only be realised through a responsive, accountable, effective and efficient local government system that is part of a developmental state" (DCOGTA 2010: 5). One element of the ideal municipality is that it can fulfil the mandate of "promoting economic and social development" (DCOGTA 2009c: 6). The State of Local Government Report mentions that "on the whole local government is struggling to fulfil this developmental mandate, and many municipalities are failing altogether" (DCOGTA 2009a: 7). This assessment is confirmed by a recent European Union evaluation which concluded that a "large number of municipalities are poorly governed and managed, with many municipalities not functioning effectively" (Stoquart & Schubert 2010b: 2).

The State of Local Government Report provides a body of detailed evidence which reveals that, while local governments in South Africa have been contributing to economic and social development advances in the past decade, this progress "is increasingly being overwhelmed by a range of factors and negative practices both internal and external to municipalities" (DCOGTA 2009a: 4). Several worrying trends in the directions of local government are discerned. First, there is the general low level of confidence which surrounds local government. Secondly, South African local government practice is not matching policy intent. Attention is drawn, in particular, to the fact that certain key aspects of the mandate of local governments, such as the provision of democratic and accountable government, the sustainable delivery of services to communities, and the promotion of social and economic development were "being addressed only in a limited way by most municipalities and not equitably for all residents within specific municipalities" (DCOGTA 2009a: 5). Thirdly, there is the uneven appreciation of the role of local governments. In this respect, the activities of local municipalities are "often undermined by National and Provincial Government policies and processes"; state-owned entities disregard the needs of municipalities; there is a lack of critical information sharing, and municipalities do not properly pursue the objectives of integrated development and intersectoral alignment. Fourthly, there is weak support and oversight of local government. Stoquart & Schubert (2010b: 2) point out that "policy failures undermine local government effectiveness". It is argued that there are no effective mechanisms for redistribution and that the existing governance system "has led to complex and confused functional arrangements" (Stoquart & Schubert 2010b: 2). In addition, "as there is uncertainty about provincial government's role in service delivery, the consequence is intergovernmental conflict and competition over powers and functions between provinces and their local governments. As a whole, the State of Local Government report reveals that "the Intergovernmental Relations System is not effective in its objective to coordinate planning across the three spheres of government and to strengthen accountability towards achieving critical and targeted development outcomes" (DCOGTA 2009a: 7). In addition, the system is viewed as poorly supported by the intergovernmental structures established to drive cooperative governance. Overall, it is concluded that the existing cooperative governance model in South Africa has not succeeded in striking the correct balance between securing national policy interests and protecting local government autonomy and that "local government cannot be expected to coordinate the entire state in local areas through its municipal integrated planning process" (Stoquart & Schubert 2010b: 2).

Finally, a marked differentiation between local municipalities has not been adequately defined or addressed. It is apparent from existing work by DCOGTA that there is considerable differentiation between different local municipalities as far as their capacity, resourcing and implementation potential are concerned (DCOGTA 2010). Under the classification of municipalities, which was developed for the Municipal Infrastructure Investment Framework (MIIF), municipalities were disaggregated on the basis of their spatial characteristics, population and percentage urban classification. This index is considered to be indicative of a municipality's capacity to roll out infrastructure for service delivery and its ability to optimally use infrastructure grant funding. In terms of this categorisation, local municipalities are grouped as follows:

A: Metros (6) Large urban complexes with populations of over 1 million and accounting for 56% of all municipal expenditure in the country.

B1: Local municipalities with large budgets and containing secondary cities (21).

B2: Local municipalities with a large town as its core (29).

B3: Local municipalities with small towns, but relatively small population and significant proportion of urban population but with no large town as a core (111).

B4: Local Municipalities which are mainly rural with communal tenure and, with at most, one or two small towns in their area (70).

C1: District municipalities which are not water service authorities (25).

C2: District municipalities which are water service authorities (21).

It is evident that this MIIF method of categorisation is useful to understand at a first level of approximation the nature of different South African local municipalities (LMs). Nevertheless, it is apparent that the major problem with the MIIF classification is that it does not provide a rational indicator of capacity, and it is for that reason that other classifications of municipalities have evolved. The National Treasury evolved a hybrid method of classification that combines space economy characteristics with performance indicators in order to identify the relative resourcing of municipalities. Seven indicators are used in order to classify a municipality as low, medium or high: percentage of households without access to basic services; property rates per capita; poverty rate; percentage staff vacancy; municipal debt per capita; municipal densities, and national contribution to gross value added. Using the National Treasury classification of LMs, 38.4% of LMs are classed as low, 50.6% as medium, and only 11.0% as high in terms of relative resourcing using the criteria applied by the National Treasury (DCOGTA 2010: 23).

The last major categorisation of South African LMs is an important classification applied by DCOGTA in terms of their differentiation framework. The methodology applies four indices, each with a number of underlying indicators. The four indicators relate to legislative categorisation as refined in the MIIF; an index of socio-economic vulnerability; the National Treasury classification, and audit opinions, the latter indicating a municipality's ability to exercise sound governance and good management practices. Four classifications of LMs emerge, ranging from municipalities which are classed as highly vulnerable (class 1), vulnerable (class 2), stabilising (class 3) or performing (class 4). The application of this framework or differentiation approach produces the result that 22.7% of LMs are Class 1 or highly vulnerable; a further 26.6% are Class 2 or vulnerable; 40.3% are Class 3 or stabilising, and only 10.5% are Class 4 or performing.

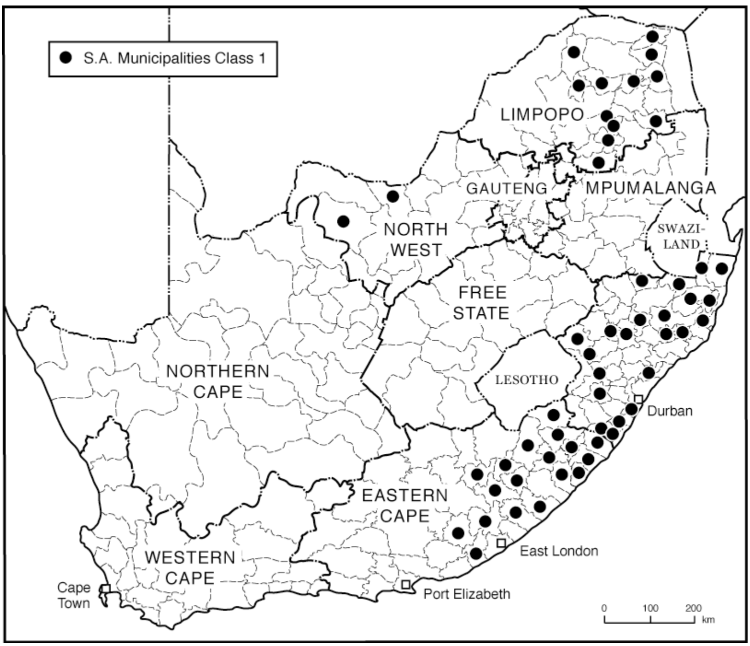

Figure 1: Class 1 municipalities – highly vulnerable

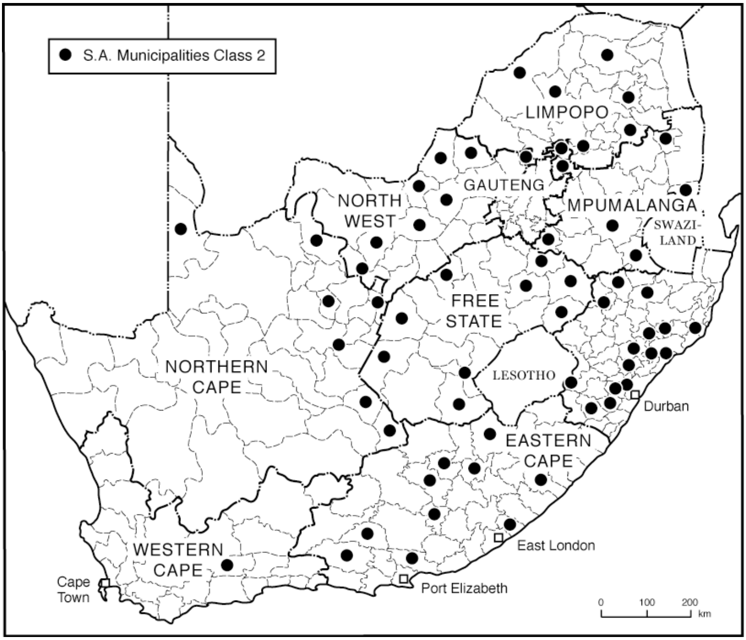

Figure 2: Class 2 municipalities - vulnerable

Figures 1 to 4 reveal the patterns of these different LMs. It is evident that a large swathe of LMs in the Eastern Cape, KwaZulu-Natal and Limpopo provinces are highly vulnerable and the group of vulnerable municipalities begins to encompass parts of the Free State, Mpumalanga, and North-West provinces. It is important to note that these maps reveal markedly different governance, resourcing and institutional capacities of local governments across South Africa. The State of Local Government report recognises that "the assignment of powers and functions, and many other governance arrangements such as integrated development planning and financial reporting did not take into account the significant capacity and functional capacities of different municipalities" (DCOGTA 2009a: 25). In addition, there is mounting acknowledgement that the 'one-size-fits-all' framework for functional responsibilities of local governments is not based on municipal realities on the ground and needs to be radically reconsidered. It is admitted that the distinct differences in capacities and institutional context within South Africa's 283 LMs means that they have not all been able to pass through the phases of establishment, consolidation and sustainability at the same rate (DCOGTA 2009a: 23).

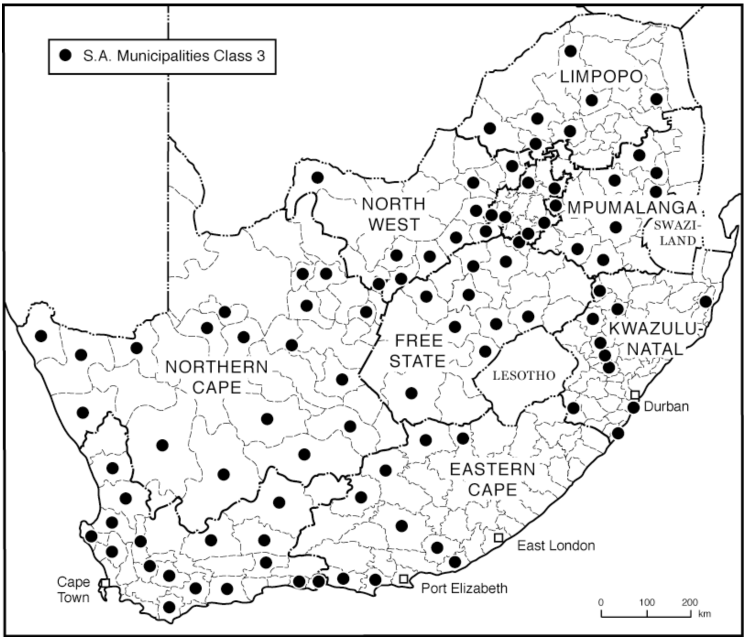

Figure 3: Class 3 municipalities - stabilising

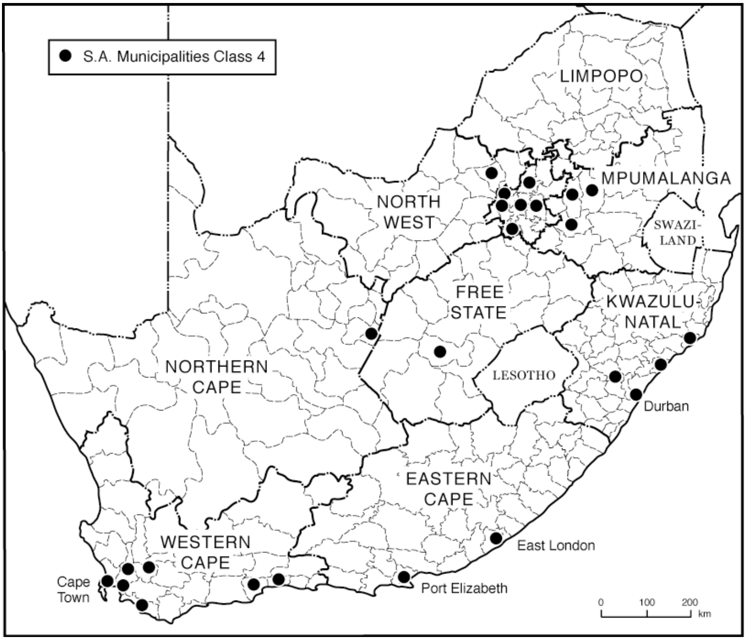

Figure 4: Class 4 municipalities – performing

The DCOGTA report shows that "much of local government is indeed in distress". Figures 1 to 4 show the existence of geographical variations in municipal capacity. It is evident that "the nature of distress is very different for urban municipalities and those municipalities located in former homelands or predominantly rural areas" (DCOGTA 2009a: 8). The core issues relate to those economically weak municipalities situated in predominantly rural areas and the former Bantustans, which have the highest backlog of services and highest welfare dependence. In these areas local government is described as "either vulnerable or dysfunctional" (DCOGTA 2009a: 8). In addition, as local government is often "the sole employer, public office can be the difference between being poor and well off which creates the conditions in which patronage and corruption flourish" (DCOGTA 2009a: 8).

Several summary clusters of problems are recognised in different types of municipalities. First, there are municipalities in which accountable local government and rule of law either are collapsing or have already collapsed. Secondly, a large number of other municipalities are simply poorly governed or managed. As a whole these municipalities are situated in economically weak areas with a low skills and revenue base that are unable to attract qualified professionals. Thirdly, it is critically acknowledged that a “one-size-fits-all” model for local government is unrealistic. Under the Constitution “by and large governance and financial management frameworks, functional arrangements and policy targets apply uniformly irrespective of the vast capacity and economic differences between municipalities” (DCOGTA 2009a: 10). It is now conceded that this model is “ineffective and a more realistic and pragmatic model is needed over the long term” (DCOGTA 2009a: 10). The uniform requirements that national government enacted “have placed an onerous burden on low capacity municipalities” (DCOGTA 2009b: 26). Indeed the “state has tended to make uniform policies and regulations rather than relating them to specific circumstances and conditions, reinforcing the gap between policy and reality” (DCOGTA 2009b: 57). One of the key recommendations of the Local Government Turnaround Strategy is to limit the functions of weaker municipalities albeit that their operations are still to be conducted within the parameters and vision of developmental local government (DCOGTA 2009a: 102). Fourthly, as alluded to earlier, the national government’s capacity to supervise and support local government is inadequate, the provinces singled out for particular criticism. Accordingly, a range of policy failures undermine the effectiveness of local government and erode the market and public confidence of municipalities (DCOGTA 2009a, 2009b).

2. Identify local competitive advantage

A second key strategy, as identified in the National Framework, relates to identifying and exploiting the comparative and competitive advantage of the 52 municipal regions and, corre-spondingly, of all LMs across the country. It was argued in the National Framework that this would result in optimising the contribution to national product of all areas across the national space economy (DPLG 2006:

25). Improving the competitiveness of the country's 52 municipal regions by providing an approach to developing local economies with the participation of all relevant stakeholders is a second pillar of the National Framework (DPLG 2006). It is recognised that there are different approaches towards improving local competitiveness. At one level, improved competitiveness can be an output of improved governance by local authorities simply 'getting the basics right' and undertaking their core business in an efficient and transparent manner. This element of enhancing competitiveness must be viewed as an activity that all South African local authorities must aspire to and could be nurtured through several support programmes.

Nevertheless, for local authorities the enhancement of local competitiveness must go beyond 'getting the basics right' and instead involve the identification and exploitation of competitive-ness. For Lawson (2009: 6), the core purpose of LED in South Africa is to improve the competitive advantages of the local business environment in order to enable more businesses to succeed and, in so doing, contribute towards poverty reduction. It is clear, however, that the capacity to undertake the identification of local competitiveness is lacking at various levels. At the highest level in one recent European Union evaluation by Lyonette & Pearson (2010: 6) it was asserted that DCOGTA lacks "the internal capacity for economic analysis at any level". Although the National Framework document claims that "the critical capacity required across government [is] to understand local economies better and to identify opportunities for growth" (DPLG 2006: 25), it is evident that this critical capacity is not always in evidence. The capacity for economic analysis and identification of comparative advantage is clearly absent in many localities. Recently, it was admitted that municipalities in peripheral regions or remote areas experience the "challenge of access to skills and little understanding of their spatial and economic realities" (DCOGTA 2009b: 29). This is one aspect of the lack of financial and human resources feeding into an inability of many LMs to deliver on their constitutional mandate.

Earlier government reports such as the National Spatial Development Perspective and the (draft) Regional Industrial Development Strategy policy documentation (The Presidency 2006, DTI 2006b) highlighted the imperative to identify local and regional competitive advantage. In addition, the process of developing LED internal profiles of localities reinforced the need for identification of competitive advantage as a critical basis for formulating LED strategies as well as investment promotion (Rogerson 2008). The significance of undertaking economic research to identify competitive advantage is a strong theme which runs across the (former) DPLG LED profiles for 2005-2007, with many District Municipalities criticised for failing to recognise or capitalise on their competitive advantage. In Gauteng it was revealed that many LMs do not engage "in substantive analysis of economic trends within their area of focus" (DPLG 2007). The identification of comparative and competitive advantage underscores the importance of evolving a better understanding of the changing dynamics of local economies (Rogerson 2010a).

Recent evidence of the problematic nature of identifying competitive advantage comes from research conducted by the GTZ in Mpumalanga in 2006 and 2009 (GTZ 2009). The longitudinal research reveals a maturity in LED within Mpumalanga such that 90% of LMs could be described as "having at least the basics in place" as compared to the 2006 assessment (Cohen 2010: 18). Nevertheless, this research underscores the difficulties of LMs in understanding their own local economies. In 2006 it was reported that LMs across Mpumalanga lacked the understanding of their economic space. This results in the construction of LED strategies which cannot be implemented. Arguably, there is a fundamental absence of understanding "the comparative and competitive advantage of their economic space and the performance of different economic sectors within the municipality" (Cohen 2010: 20). Notwithstanding some improvement in the LED environment by 2009, the few quality LED strategies signalled the continued intractable problem of understanding and interpreting local economic space.

A better local understanding of local economies, in turn, hinges upon the collection of accurate economic data to enhance LED planning (Rogerson 2008). The key issues for defining comparative advantage are those of the collection of reliable economic data to track local economic trends and define competitive advantage. Broadly speaking, it is evident that a collective responsibility exists across many levels of government (in particular, of Statistics South Africa) for gathering data that can be used to monitor local economies and define competitive advantage. Improved availability of good data for understanding local economies and for LED planning is the *sine qua non* for municipalities to identify comparative advantage and then exploit that in terms of enhancing competitiveness. Question marks are raised, however, as to the reliability and quality of certain existing official data for undertaking local economic planning in South Africa. Cohen (2010: 32) points out that “the fact that many local authorities do not have up-to-date and/or relevant economic data about their areas is an impediment to their ability to develop sensible LED strategies” which must be founded upon an understanding of the local economy. The most important basic data requirements for local authorities are the following: annual data (as opposed to 5-year gaps in census data) to track actual progress in LED indicators and outcomes; basic demographics (age, highest level of education, unemployment and location); employment (numbers of employed persons, type of employment - full- or part-time, sector in which people are working, level of job); sectoral analysis; infrastructure and infrastructure capacity, and enterprise analysis (numbers of companies and their size).

Overall, it is evident that there are certain serious deficiencies that must be addressed in the existing spatial data sets in order to inform and improve local level planning. In the absence of improved local economic data the objective of identifying comparative advantage and of packaging different investment spaces based on their real production and business opportunities, including for small enterprises, is unlikely to be realised.

3. Building a conducive business environment for private sector investment

A fundamental shortcoming of two decades of LED planning in South Africa relates to the fact that local government-driven LED has had only limited success in involving non-state actors, particularly outside of South Africa’s major cities (Rogerson 2010a, Rogerson & Rogerson 2010). Throughout most of South Africa, the private sector either has been left out or chosen not to be involved as a result of the mutual suspicion that exists between public and private sectors, making dialogue between the two groups extremely difficult (Rogerson 2010b). Mistrust is premised on divergent ideological beliefs and, correspondingly, on different priorities. Essentially, the public sector believes that business is anti-poor and business believes that government is welfarist and anti-profit in outlook (Rogerson & Rogerson 2011). Private-sector apathy towards local government-led LED has been further enhanced by its experience of local government bureaucracy, red tape and unproductive 'talk shops' where much is promised but little of benefit to the private sector is actually produced (Lawrence & Hadingham 2008: 44). The inherent tensions between public and private sectors are compounded by the need to transcend the apartheid legacy of a mainly white-owned and -controlled private sector and predominantly black public sector. The core problem is a need to construct "the necessary 'soft factors' of cooperation – trust and social capital" which internationally are considered as essential for effective cooperation between state and non-state actors (Ruecker & Trah 2007: 47).

Since 2006 the World Bank jointly with the International Finance Corporation (IFC) has undertaken subnational and regional 'Doing Business' reports which capture differences in business regulations and their enforcement across different locations within a single country. The surveys are described "as a kind of cholesterol test for the regulatory environment for domestic businesses" (World Bank & IFC 2010: vi). The results of these surveys point to considerable geographical variations and important subnational differences in the ease of doing business. In addition, these survey reports recommend local reforms for improving the 'local business environment' for private sector development, particularly concerning the need for transparent business regulations. It is stressed that "where regulation is burdensome and competition limited, success tends to depend on whom you know than on what you can do" (World Bank & IFC 2010: vii). In particular, these surveys confirm that addressing red tape by local governments is a significant building block for improving local business environments since "it is at the local level that the public sector interacts with the private sector on a day-to-day basis" (Hindson *et al* 2009: 1).

The lead issue for involving the private sector is to improve the local business environment in order to allow private enterprises – large and SMMEs, formal and even informal enterprises – to engage with or drive LED. Improvement in the local business environment for the activities of the private sector has been shown from international experience to be an essential base for energising LED activities and, in particular, for creating more competitive local economies which attract and retain private sector investors (World Bank & IFC 2012). In South Africa national government has recognised this imperative and with the support of international donors (most notably, GIZ) and the South African Local Government Association is seeking to foster improvements in local business environments across the country. The Development Bank of Southern Africa (DBSA) asserts that "improving the local business environment should be part of every LED process" and concedes that initiatives to pursue LED "will only show very limited and isolated effect on the local economy if they are designed within a disadvantageous or even hostile local business environment" (DBSA 2008: page numbers?).

Recent research provides some insight into the challenges of improving the local business environment for more effective LED in South Africa (Rogerson 2010b, 2010c). One study involved a national survey in 2009 with 30 business chamber associations (Rogerson 2010b); a second investigation analysed the conduciveness of local business environments in the Eastern Cape and Mpumalanga provinces with interviews across 16 LMs with private sector business associations (Rogerson 2010c). Arguably, the findings from these two studies point to radically differing perceptions of the private sector and local government towards LED, questions of trust and mistrust between private sector and the public sector, and highlight the imperative for greater dialogue in order to provide the foundations for local partnerships and improving the local business environment for private sector-led LED. The research disclosed an urgent need for closer public-private dialogue and communication in order to foster trust and better working relationships between local governments and the private sector (Rogerson & Rogerson 2011).

It is acknowledged more widely now that a "conducive business environment is a key ingredient to the creation of vibrant local economies across South Africa" (DPLG, DTI, SALGA & GTZ 2009: 1). The local level and local government are considered to have a crucial role to play in creating a favourable business climate (GTZ 2006, DPLG, DTI, SALGA & GTZ 2009). National government views the establishment of better business environments for shared local economic growth and development as essential to influence the positive contribution which can be made by or levered from the private sector towards social and economic development. Building on the international experience, in South Africa improvement in the local business environment for the activities of the private sector has been shown to be an essential foundation for catalysing LED activities and, in particular, for creating more competitive local economies which might attract or retain private sector investors (World Bank 2010). It is observed that the "national business environment creates conditions for business activity across the country, but increasing levels of decentralisation and the drive for better local governance makes improving the local business environment critical for local economic growth and poverty reduction" (DPLG, DTI, SALGA & GTZ 2009: 1).

Nationally, one critical issue for creating 'business-friendly environments' concerns the need for partnership between South African local governments and the private sector for 'red tape' or local regulatory reform. Until recently, local governments in South Africa tended to concentrate overly upon aligning local planning processes with provincial and national guidelines, resulting in a tendency to overlook the potential 'quick wins' that might arise from reforming the demand side of the local business environment (Christianson 2008). Identification of local regulations that can and need to be reformed revolves around implementing the LED concept of partnership between local government and local business (Christianson 2008). From international experience, Hindson *et al* (2009: 1) aver that "addressing red tape is an important building block of a local economic development initiative". Nonetheless, opportunities to facilitate investment have often been missed in South Africa because of the low priority given to improving local business environments and cutting red tape.

Overall, South African policy circles are recognising that an improved business environment reduces the costs of doing business for all enterprises and, in particular, for small enterprises (GTZ & InWent 2006). The national integrated strategy on the promotion of small enterprises emphasises the importance of easing the regulatory constraints and compliance burden on small enterprises (DTI 2006a). Many constraints are considered to be either inappropriate or unduly restrictive legislative and regulatory conditions which can unintentionally obscure or inhibit market access and opportunities for small enterprise providers of goods and services. This issue links directly to the building of better business environments for LED. The 2006 National Framework for Local Economic Development urges local governments to foster conditions that stimulate and enable the general environment in which business is done (DPLG 2006). Two government departments - the DTI and DCOG – are currently charged with joint responsibility to prepare recommendations on how to improve the regulatory environment for small enterprises in municipalities across the country (DTI & DCOG 2011). This responsibility entails the creation of an enabling environment, establishing a regulatory impact assessment framework, and initiating business environment monitoring mechanisms.

Currently, the DTI and DCOG are engaged in a partnership to undertake 'red tape' reduction in 12 pilot municipalities across the country (DTI & DCOG 2011: 3). This initiative aims to identify the most critical red tape issues and afford a starting point for local improvement processes. With respect to red tape there is widespread evidence that small and medium enterprises ultimately pay disproportionately higher costs of compliance with administrative rules, regulations and procedures, thus impeding their market access (GTZ 2006: 6). The approach of reducing local red tape thus represents a pro-active and locally-driven approach for building a better local business environment and linking business development with LED (GTZ & InWent 2006).

4. Intensification of enterprise support in local areas

By 2006 a fundamental policy break had occurred from the apartheid period when the SMME economy either was to a large extent ignored by policy-makers or, in the case of black-owned enterprise, actively discouraged by an array of repressive measures, particularly at the tier of local government. Since the democratic transition, the promotion of the SMME economy in South Africa has been associated with a range of new optimistic policy objectives, including poverty alleviation, job creation and enhancement of national economic growth (Rogerson 2004). Overall, mixed assessments were offered of the impacts, successes and disappointments of the first decade of government support for SMME development in South Africa (Berry *et al* 2002, Thomas 2004). As a result of certain acknowledged disappointments concerning the impact of national government SMME support, important institutional changes were enacted in December 2004, the most significant being the launch of the national Small Enterprise Development Agency (SEDA). The core role of SEDA is to drive the future development and upgrading of South Africa's SMME economy anchored upon a revised national support programme, the Integrated Small Business Development Strategy (DTI 2006a).

The national roll-out and intensification of support to small enterprises was considered an essential prerequisite for successful LED in South Africa in the National Framework for LED. The intensification of enterprise support relates to business development services and the extension of business infrastructure development in local areas. The key channels for achieving this were through the implementation of the ISBDS and of associated initiatives for extending access to finance for small enterprises (DTI 2006a). The major responsibility for small enterprise development, including access to finance, is with the DTI and its two key implementation institutions, SEDA and Khula. The former organisation was responsible for a range of non-financial support BDS interventions, the latter was charged with the mandate of extending financial support to the small enterprise sector.

Between 2006 and 2010 a network of government and private sector support schemes emerged which began to grapple with some of the key constraints on growing the SMME economy. An assessment completed by the World Bank in 2010 concluded that it was not clear "how far these schemes have succeeded in reaching out to microenterprises in general, and to the more promising of informal enterprises in particular within that group" (World Bank 2010: 74). One survey of the uptake of national government enterprise support disclosed that fewer than 10% of the sample had received any assistance from key national government enterprise support programmes and that less than 15% had sought any such assistance (World Bank 2010: 94). The 2010 assessment by the World Bank echoes findings presented earlier in the decade (Rogerson 2004), suggesting that fundamental problems of intensifying enterprise support remain unresolved. Critically, the World Bank report points out that, while existing support programmes are assisting the larger end of the SMME spectrum, the existing data does not "show significant coverage of microenterprises, formal or informal" (World Bank 2010: 74). Among the core barriers to microenterprise development in South Africa remains that of difficulty of getting access to finance (World Bank 2010: x). It was concluded that access to finance was most difficult for microenterprises as compared to "small enterprises and more difficult for small enterprises than large enterprises". Similar findings concerning the weakness of government support for enterprise development are found in the 2010 Finscope South Africa Small Business Survey, possibly the first comprehensive nationally representative survey of small businesses in South Africa. This study revealed low awareness levels of support; 74% of small business owners were unable to name any organisation that provided help or advice to small businesses and 94% claimed never to have accessed any support (Finscope 2010: 3). In large measure, these disappointments in the intensification of enterprise support reflect the workings and performance of DTI's key institutions involved in support delivery.

SEDA is legislatively mandated to design and implement support programmes for SMMEs, to build capacity for other role players in the sector and to promote a service delivery network that increases the contribution of small enterprises to the South African economy. Seven basic services are offered in terms of its range of non-financial support services: assistance with business registration; business planning; facilitating SMMEs access to markets; facilitation of access to finance; support for cooperatives; enterprise training and mentoring, and assistance with access to technology. Several shortcomings were observed in the mid-term review of SEDA (completed in April 2010). It was asserted that SEDA's core focus was "more relevant to existing ventures than start-ups, and aimed more at larger businesses than micro or small enterprises" (NSRA 2010: 28). Awareness levels were conceded to be low of SEDA support services (NSRA 2010: 28). The quality of business support offered by SEDA was compromised by the lack of capacity of its network of business advisors – described as "often under-skilled to meet the needs of clients" (NSRA 2010: 128) – who interfaced with small business entrepreneurs (NSRA 2010: 77). In addition, banks complain of the poor quality of business plans that are the outputs of SEDA support for business planning (NSRA

2010: 85). Indeed, SEDA's relationship with the banking sector has been difficult and relationships "have not proved to be as successful as originally envisaged" (NSRA 2010: 98). In addition, the absorption of the former National Manufacturing Advice Centre (NAMAC) activities, which were recognised as a success story of the first decade of enterprise support, "has been problematic" as the specific kinds of support supplied by NAMAC have to a large extent been lost as SEDA has become "more generalist in approach" (NSRA 2010: 81).

At the core of the SEDA delivery model is the national network of 42 branch offices and Enterprise Information Centres (EICs), which are described as "the front end of service delivery" for the SEDA network (NSRA 2010: 146). By 2008 only 53 EICs were in operation, substantially less than the envisaged total target of 324 (NSRA 2010: 147). The national and geographical roll-out of these vehicles for intensification of enterprise support has been unsatisfactory and "particularly troubling" (NSRA 2010: 148). The result is a shortfall in the provision of key support services in many local areas of the country. The problems of service delivery to small enterprises, however, have not simply been internal to SEDA but are also linked to problems of underfunding. The organisation has suffered severe budgetary constraints such that during 2008 there was a moratorium on offering services for six months of that year (NSRA 2010: 57).

In addition to the weak performance of non-financial enterprise support, continued problems have been recorded in extending access to finance both through the operations of Khula and the newly established South African Microfinance Apex Fund (SAMAF). Khula functions as a provider of wholesale finance to the SMME economy and its activities go back to 1996 (Rogerson 2004). The organisation's mandate is to maximise access to finance for SMEs and to achieve the maximum development impact while remaining financially sustainable. Khula operates mainly through a network of funding Retail Financial Intermediaries which lend directly to small enterprises. Another aspect of its activities is the provision of a credit indemnity to support lending to small businesses by the formal banking system. Since the formation and launch of SAMAF in 2006 Khula has concentrated its efforts on providing finance lending to SMEs rather than SMMEs.

One evaluation of Khula showed that the organisation had improved its performance as compared to the first decade of its operations (Rogerson 2004). Nonetheless, the recent uptake on the credit indemnity has been slow and limited. The core problem of Khula operations is reliance on intermediaries. It is evident that, while Khula has the ability to influence the lending role of intermediaries, as a remote facilitator it does not directly control the lending operations and its delivery to the target market (DTI *s a*). Thus, in relation to intensifying enterprise support through extension of access to finance, Khula's interventions and impacts "are thus driven by the risk appetite of its intermediaries" (DTI [*s a*]: 13). Accordingly, in order for Khula to "deliver developmental impact at scale and grow the SME market, it will be crucial for the institution to proactively channel its resources in line with Government's objectives and provide support to SMEs that remain neglected despite current State and private sector interventions" (DTI [*s a*]: 14-5). This can be achieved only through Khula incorporating a direct lending approach into its current wholesale model. This direct lending is taking place through the new model of KhulaDirect which partly is to reposition Khula operations by acquiring all or a majority stake in the targeted RFIs that it wants to control (DTI [*s a*]: 15). Overall, it is argued that Khula has undertaken an outreach through its wholesale finance lending operations and that in order to maximise development the organisation must move to a hybrid business model which will permit it "to provide sorely needed finance to segments of the SME market that remain grossly underserved" (DTI [*s a*]: 20).

Finally, in terms of understanding the problems with access to finance to the SMME economy, brief mention is necessary of the activities of SAMAF which was established as a trading entity by DTI to implement a three-year national pilot project "aimed at extending microfinance services for the benefit of the poor through financial intermediaries" (Deloitte 2010: 3). Although this initiative – modelled on the successes of the approach of the Grameen Bank in Bangladesh – has recorded some positive impacts on its financial intermediaries as well as ultimate borrowers, several problems are observed. First, the performance of lending activities has been disappointing as far as volume, growth and loan quality are concerned. This underlines the problem of a limited number of eligible intermediaries to channel on-lending of loans to ultimate borrowers. Secondly, problems have been experienced in terms of geographical outreach: it is made clear that the beneficiaries so far have been concentrated in the Gauteng, Limpopo and Mpumalanga provinces (Deloitte 2010: 4). Thirdly, SAMAF has lacked the necessary capacity to nurture and monitor its intermediaries and requires both institutional strengthening and extended funding in order to deliver fully on its mandate. On a wider scale there is a shortage of skills in South Africa as a whole concerning micro-financing which makes it difficult for SAMAF to function effectively (Deloitte 2010: 5).

5. Conclusion

In many parts of the global South the significance of 'doing LED' is increasing in currency.[2] In South Africa the promotion of successful LED practice is considered an essential ingredient for addressing the challenge of achieving "inclusive growth" or shared prosperity in the country (Turok 2010, 2011). The South African experience of LED, however, is significant beyond the country's borders. The long-established South African programme for LED is considered as a learning base for the development of LED programmes in other countries of sub-Saharan Africa (Rogerson & Rogerson 2010). In this instance, it is argued that a precondition for successful LED in Africa is that of linking it to wider issues of business development and more specifically the growth of opportunities for 'ordinary' SMEs. One factor in the disappointments with respect to 15 years of LED planning in South Africa relates to the 'disconnect' between business development and LED planning activities. Arguably, this disconnect has now been acknowledged by national government which is launching a series of initiatives to address the nexus between enterprise development, on the one hand, and LED, on the other. This analysis discloses the specific importance of four themes, *viz*, the improved market confidence of the private sector in local government; the capacity to identify opportunities for and to exploit competitive advantage; the imperative to build facilitative business environments for private sector investment, and the intensification of enterprise support

2 *Cf* Christensen & van der Ree 2008, Rodriguez-Pose 2008, Nel 2011, Vazquez-Barquero 2011.

at local level for the development of small enterprises. Continued monitoring of these important issues and, more particularly, of their articulation with LED processes is essential.

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