

Small firms can be the drivers of youth employment in South Africa

Headline results from the SME Growth Index, 2015

According to the University of Cape Town's Children's Institute Child Gauge report, South Africa has almost 3 million young adults with no income and little hope of a better future. The World Employment and Social Outlook report published earlier this year by the International Labour Organisation (ILO) estimates that youth unemployment in South Africa for youths aged between 15 and 24 years is 52% - more than four times the figure for sub Saharan Africa. According to the ILO data, South Africa's youth unemployment ranks as one of the highest in the world, representing 1.9% of global youth unemployment.

There is no hiding the sheer magnitude of the youth unemployment challenge that confronts South Africa.

Policymakers around the world agree that promoting economic growth is the single most important driver for creating jobs. And there is ample evidence worldwide that suggests that small and medium sized firms (SMEs) are the most significant source of new employment, especially for the youth and most marginalised in society.

The preoccupation of policy makers and commentators with SMEs hinges largely on the understanding that these are the firms with the best prospects of creating desperately needed jobs, especially for young people entering our labour force. If policy is to play a constructive role in this respect it is imperative that an in-depth understanding of the dynamics behind SME employment creation, especially for the youth, be developed.

In response, SBP's yearly investigation - the SME Growth Index - is a study geared towards establishing a solid, evidence-based understanding of South Africa's SME community. The research tracks the experiences of a panel of 500 SMEs employing less than 50 people in three key sectors; manufacturing, business services and tourism across three major metropolitan areas. Established in 2011 and now in its fifth iteration, the study has over the years assembled a vast amount of data on the lived dynamics of South Africa's SME community.

SMEs have a bias towards employing young people

Research conducted by SBP and Professor Neil Rankin based on data from Statistics SA's Quarterly Labour Force surveys and the SME Growth Index show that people at the beginning and end of their working lives are much more likely to be working in smaller firms than those in middle age. Relative to a 35 year old, a 20 year old is almost 4 percentage points more likely to be in a small firm. And those with less than a matric are 19 percentage points more likely to be in small firms compared to those with matric or higher.

Latest findings from the survey show that on average firms employing between 40 and 50 people have a staff complement of 17% comprising young people under the age of 30. Deeper analysis shows that as smaller firms grow they increase their staff complement of young people by 2%.

While these findings appear positive in terms of youth employment, overall the research is showing that year on year changes in the sub-indices of the SME Growth Index are showing downward trends. SMEs are battling to survive in a tough economic and increasingly hostile regulatory climate with just over one in five firms on the panel reporting a decline in turnover from the previous year and 21% firms reported a decrease in staff in 2015.

The evidence points to an SME community – the NDP's envisaged driver of employment – that is struggling with the prevailing conditions of low economic growth and increasing burdensome regulations. As the study's latest findings show, the failure of SMEs to take on more staff is a serious problem given the magnitude of South Africa's rising unemployment. It is doubly serious in view of the specific lost opportunities that this represents – especially for young people entering the labour force, since the employment profile of SMEs tend to mirror those least likely to find work in larger firms. A job creating SME community is more likely to create opportunities for the less skilled, less experienced and young entrants to the labour force.

Another finding from the research is that the disincentive impact of the labour regime, frequently reported by the panel as the key barrier to hiring new people, is felt more acutely by firms most likely to employ unskilled staff and young adults.

A national minimum wage

Job creation is an indispensable precondition for ensuring that young people have access to economic opportunities. They cannot find jobs unless those jobs exist. The NDP states that it is "critical to urgently introduce active labour market policies to initiate massive absorption of young people and women into economic activity in the private sector". Yet recent amendments to the raft of labour legislation have in fact tightened, doing little to unlock the labour market for new entrants.

Coupled with these, the possible introduction of a national minimum wage is another factor that could result in perverse consequences by further locking out young people from the labour force. The regulatory impact assessment conducted by SBP for the Department of Labour to assess the potential impacts of the amendments to the labour bills estimates that South Africa's wage employment elasticity - a measure of the sensitivity of job retention against wage increases - is 0.7%. This suggests that for every one percent increase in wages will result in 0.7% decrease in employment.

In debating the national minimum wage, the context should fundamentally be influenced, and informed, by an understanding of how it might impact on the levels of poverty, inequality and rising unemployment, especially for our young people. References to these challenges are often stated in a single context, yet they are three different economic conditions, which have different – and relative – impacts on each other. Inequality may not necessarily result in poverty or unemployment, but poverty and unemployment might have a strong forward linkage.

Since the national minimum wage will only apply to people who currently have jobs, the unemployed will not benefit. Taking into account the expanded definition and based on Statistics SA findings this means that up to 13 million unemployed South Africans will be excluded from receiving a national minimum wage.

Unleash a culture of entrepreneurship

It should not be assumed that a focus on the regulatory environment would be a sufficient intervention to propel large-scale job creation for the youth. To do so is to simplify a complex set of issues but a step change has to happen to enable more young people to acquire the necessary education and skills to join our country's workforce.

Many studies show that young people have difficulty entering the labour market. This is attributed to identifiable, and often remedial, skills deficits, including a lack of work related skills, lack of experience and testimonials that could get them started on an upward path, and limited opportunities for entry level work that is career orientated. And while we're focusing on educating our youth for the formal workplace, we should also invest in their abilities to be entrepreneurs. With the right investment in encouraging young people to discover and seize economic opportunities, they will create their own jobs and may hire others.

Given the importance placed on the SME sector by the NDP, it stands to reason that the challenge is to ensure an environment that enables SMEs to grow, prosper and employ more people, especially young adults.

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Conditions need to be put in place under which start-ups can flourish and more young entrepreneurs are encouraged to formalise and enter the market-place. It is perhaps with small businesses, and new young entrepreneurs that the “spirit of enterprise” is most readily associated.

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SBP is a not for profit company specialising in improving the environment for doing business. We have worked in Africa and internationally since 1998 providing innovative solutions for policy formulation, better regulation and development in emerging markets. We have a special interest in small business as vehicles for growth and job creation.

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