



POLICY BRIEF

The role of skills and education in predicting microenterprise performance

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Executive summary

In the light of South Africa's high levels of unemployment and relatively small informal sector, enabling and supporting growth of small, medium and microenterprises (SMMEs) in the informal sector are of developmental importance as well as a policy priority. The associated benefits of SMME growth, such as employment creation, enhancement of economic growth, and poverty alleviation, provide further motivation for the prioritisation of this sector.

Given the developmental importance of growth in the informal sector, and of SMMEs more generally, this policy brief examines the determinants of SMME performance in South Africa. Particular focus is placed on the role played by education and skills in driving the performance of firms.

Summary of findings

- Formal education is a key factor driving SMME performance. Higher levels of education are associated with higher returns to self-employment, with returns being greatest for matric, post-matric and apprenticeship qualifications.
- Previous industry experience and practical, work-related training (e.g. apprenticeships) are important sources of skills for owners of firms and key determinants of the performance of firms.
- Marketing, accounting and information technology (IT) skills are positively associated with the performance of firms.
- SMME performance is influenced by a wide range of factors (e.g. access to credit) and, consequently, policy interventions in respect of skills should form part of a wider policy initiative aimed at enabling and supporting SMME growth in South Africa.

The research

Introduction and methodology

In the light of the developmental importance of growth in the informal sector, and of SMMEs more generally, this policy brief provides insight into the determinants of SMME performance in South Africa. Particular focus is placed on the role education and skills play in driving enterprise performance.

We do this, firstly, by using direct and indirect measures of skills to generate a human capital profile of SMME owners across both the formal and informal sectors. Secondly, we use econometric analysis to examine the factors determining enterprise performance along two dimensions: financial performance, and the ability to access market opportunities. The analysis benefits from the use of data from the Finscope Survey (2010), a nationally representative data set providing information on the owners of firms as well as on their firms across both the formal and informal sectors of the South African economy.

Drawing on insights from the analysis, this policy brief provides policy guidance concerning skills development initiatives in the SMME sector.

Human capital profile of SMME owners

The descriptive analysis of the human capital profile of SMME owners across the formal and informal sectors provides a number of interesting insights: Firstly, formal-sector enterprise owners have higher levels of education than their informal-sector counterparts. Two-thirds of informal-sector enterprise owners have less than a matric education. Therefore, skills development initiatives targeting the informal sector need to take into account the relatively low formal education base of owners in the sector.

Secondly, enterprise owners reveal that the main source of the core skill needed to operate their firms is obtained via self-discovery, family, work experience, and on-the-job training; hence, the skills needed by owners to manage their firms are not necessarily obtained via the formal education and training route. This suggests that skills development offerings should be seen as providing secondary skills that complement existing core skills and thus equip the owners of firms to 'do what they do, better'.

Thirdly, using an indirect measure of business skills, the analysis shows that only 13.6% of firms have at least one of the following functions – IT, accounting, administrative, human resource, marketing and legal – within their business (and hence the associated skill). The limited extent to which these core business functions, and hence the associated skill, exist within firms across both the formal and informal sector suggests scope for 'multiskilling' programmes that address these deficiencies.

Finally, when asked what minimum level of education is needed by their employees, half of both formal- and informal-sector enterprise owners specified work-related training or an apprenticeship. Consequently, skills development initiatives need to focus on practical, work-related training programmes.

The determinants of a firm's performance

The econometric analysis examines the importance of skills and education in explaining enterprise performance, while controlling for other enterprise and individual characteristics. The estimates indicate that higher levels of education are associated with higher levels of enterprise performance. Interestingly, the highest returns are associated with enterprise owners whose highest level of education is an apprenticeship. In addition, previous work experience is positively associated with a firm's performance. Again, this emphasises the importance of practical, work-related training.

The indirect measures of skills in the estimations indicate that the ability of a firm to market itself, keep financial records, and keep computerised financial records, and hence the presence of marketing, accounting and IT skills, respectively, are positively associated with a firm's performance.

The results also indicate that other enterprise characteristics, such as being a registered enterprise in the formal sector, having access to formal credit sources, and having black economic empowerment (BEE) supplier status, are positively associated with a firm's performance.

Policy recommendations

In analysing the role played by skills and education in determining SMME performance, a number of skills-focused policy recommendations can be deduced. Although the analysis focused on SMMEs across both the formal and informal sectors, the policy recommendations that follow are geared toward small and microenterprises in the informal sector.

The ability to acquire additional skills is strongly influenced by an individual's formal education base, and the analysis indicates that this base is weak in the case of informal-sector enterprise owners. Consequently, raising levels of education and literacy are important. In particular, the development of 'finishing school' curricula may be an important element of an overall skills development agenda.

Multiskilling is a key element of running a business, especially in the informal sector, and thus the inclusion of a variety of business skills – e.g. accounting, IT and marketing – in a skills development initiative is important.

The analysis points to the importance of on-the-job training (e.g. apprenticeships) and practical, work-related experience. Therefore, 'training with production' may be an important element of an overall skills development initiative. Associated courses need to be high in practical content to keep in touch with industry trends.

Another channel from which to assist in the development of skills in these firms is to provide business-support services, for example assisting firms with registration procedures, acquiring BEE status, submitting tenders, maintaining financial records, formulating and writing business plans, and accessing credit sources.

Finally, there are a variety of factors outside of skills that influence a firm's performance, and, consequently, skills development policy that targets SMMEs needs to form part of a wider policy framework aimed at facilitating the development of SMMEs.



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