

Inclusive business for enterprise development in rural settlements

V2. May 2018

1 Problem statement

South Africa suffers from high levels of unemployment, particularly in the rural areas where the unemployment rate is above 40%. As a result, many rural households are trapped in poverty. The South African government acknowledges the need to create job opportunities outside the main urban areas. To achieve this, the focus is largely on stimulating the agricultural sector and in particular the smallholder segment. But, the composition of rural areas presents a high degree of de-agrarianisation, with a large proportion of rural households not able to engage in agricultural activities. In addition, the large-scale commercial orientation of the agricultural sector questions the role of small-scale agriculture as catalyst for job creation. Alternative sources of income outside of farming are thus crucial to allow rural households to diversify their livelihoods.

Simultaneously, South Africa presents a significant lack of self-employment, one of the avenues for development. Whereas the B-BBEE act stimulates the support of SMMEs, the survival rate of enterprises in this segment are disappointing. Furthermore, the supported entrepreneurs are often based in the main urban centres where it is easier to link these businesses into the existing supply chains of large corporates. As a result, economic activities remain concentrated, both geographically and in terms of large business dominance.

These two aspects lead to the following problem statement:

What architectural structures are needed for sustainable entrepreneur-based inclusive business models and how do corporate entities fit into these structures?

2 Jobs impact

This paper explores a number of inclusive business (IB) models: partnerships that integrate low-income communities into existing commercial value chains. IBs thus incorporate existing commercial business entities. The models researched are designed to specifically operate in the context of rural settlements and thus have the explicit objective to stimulate economic activity, and consequently jobs, in these areas.

These models identify two different entrepreneurial types: business owners and self-employed contractors. As such, jobs are created through three options, business entrepreneurs, staff employed by these entrepreneurs, and self-employed workers that produce goods on contract. The partnership models are designed to be scalable and replicable, generating an overall significant employment impact in the marginalised areas. The basic models are franchising, independent enterprise development fund, joint ventures,

and township outsourcing. These models should be seen as instruments that serve as a foundation to be combined with other tools and instrument that result in unique models.

Drawing on the logic of how the CWP programme was implemented, for the inclusive business models to succeed, a number of elements are critical: an understanding of the communities in which an IB is implemented; and clear partnership arrangements between corporate entities, coordinating/implementing organisations and financial supporters.

3 Theory of change

Corporate entities are motivated to develop models to engage enterprises in rural settlements into their supply chain. This can be triggered for example by the B-BBEE policy framework or by a willingness to be a good corporate citizen. Rural communities are looking for entrepreneurial opportunities but lack the skills and networks to gain entry into commercial value chains.

For corporate entities, engagement with rural communities is an uncertain strategy with the likelihood of lower returns on investment, thus they defer such initiatives. Providing insights into several inclusive business models, and identifying critical elements for the implementation can lower this uncertainty. It is assumed that this will lead to an increase in the initiatives with rural entrepreneurs with a higher success rate than current initiatives.

This proposal serves to identify inclusive business models that, if implemented with care, can lead to the ultimate outcome of sustainable work opportunities in rural settlements through commercial value chain integration.

4 Existing initiatives/experience

A number of inclusive businesses have been implemented in South Africa. The largest and longest running is the Anglo Zimele model that has operated for over 30 years, and which has resulted in thousands of jobs, particularly in the mining areas. It is by far the largest example of inclusive business in the country. Furthermore, a considerable number of diverse and complex models have been established in the agricultural sector, engaging smallholder farmers, landowning communities or farmworkers. Lastly, a range of CSI projects that focus on non-agriculture activities in the rural areas have been implemented, albeit at a small scale. In addition, multiple international examples operate IB partnerships, such as Coca Cola in Tanzania and Danone in Bangladesh. All these initiatives provide valuable lessons regarding engagement of low-income communities into commercial value chains. The research has analysed these initiatives and makes recommendations to grow the number of inclusive businesses, to make them scalable and replicable, and to make them more sustainable, so that the objective of job creation in rural settlements can be achieved.

The most important lesson from past and current initiatives is the need for partnerships. Particularly the engagement of a local organisation that has a thorough understanding of the community is critical to ensure that the IB understands the needs and the internal dynamics of the community and gets the buy-in from the local population. Other partners are required for training and financing of the IB. Another lesson is that the IBs need long-term commitment. A thorough preparation phase is followed by an iterative implementation. Thus, an IB project does not align to the usually short timeframes set for

mainstream business activities. Lastly, crowding out of existing entrepreneurial activities must be prevented.

5 Constituency participation in implementation

The community and business constituencies are critical in a number of roles. Firstly, the community constituency plays a role in identifying the opportunities for their community and should be involved with the selection of members to be engaged in the IB and participate in a collective organisation that might be a part of the IB (joint venture and outsourcing models). Secondly, identification of implementing agents who have a very thorough understanding of the dynamics in each constituency in order to implement a successful IB.

The business constituency's role lies in partnering to identifying business opportunities that align with their supply chain, and the allocation of resources for implementation.

6 Benefits

The benefits depend on the particular model a corporate decides to implement. The table below provides an indication of the kinds of groups that can be included in the IB. Any job numbers and time frames are model and even community specific and hence only serve as a rough guideline.

In all cases, the general advantages of better health, educational options and improved social standing must be included under the other benefits.

Group	Job creation	Other benefits	Time frame for success
Rural entrepreneurs (franchise, enterprise development, joint venture models)	Direct job creation for the entrepreneur him/herself. A growing business will generate further employment opportunities within the supported business.	Skills development: entrepreneur is exposed to commercial network and overall business management through training, mentoring and experience. Linkages: a successful enterprise will generate a local demand for inputs, services and the like.	For entrepreneurs to establish their business and become independent operators takes minimum 3-5 years.
Home workers (outsourcing model)	Direct job creation for selected home workers. The working times are flexible, allowing opportunities	To reach scale, a number of workers must be included. This group can serve to create a tighter community, a support network for the	The preparation phase for such a model takes time as a good understanding of the

Group	Job creation	Other benefits	Time frame for success
	particularly for women with children to become active participants in the (informal) labour market	members, and be a platform to engage in other activities (e.g. savings group).	community skills and dynamics is needed. But, implementation can then be quick and the model is quickly scalable. Positive results can be expected 1-2 years after establishment.

7 Cost and potential sources of funding

As with the benefits, the anticipated costs are model and community dependent. The information in the table below should be seen as an indication of a potential distribution of costs within an IB.

Group	Anticipated costs	Potential sources of funding to implement the project	Time frame for impact
Corporate enterprise	Loan/equity investment Input of supplies/branding material Training/mentoring costs Staffing of coordinating unit	Corporate budget, CSI enterprise development (can be self-funding)	As a general guideline, a minimum of 3 years
Rural entrepreneur	Equity, inputs, working capital, operating space	DFI, commercial bank	As a general guideline, a minimum of 3 years
Meso-organisation / implementing agent	Staffing of coordinating unit	Sponsored by corporate enterprise	Upon implementation
External (commercial) financier	Loan/equity investment	DFI such as IDC, commercial bank, jobs fund	As a general guideline, a minimum of 3 years

Group	Anticipated costs	Potential sources of funding to implement the project	Time frame for impact
Other sponsors	Sponsoring of training, inputs, equipment	CSI budget,	Short time frame for impact – a few months
Home workers	Inputs, equipment	Loan from corporate outsourcer, NGOs, corporate sponsors	From implementation, if no loan funding is needed to establish the required assets.

8 Risks

Some general risks are associated to IBs, in particular lack of commitment and lack of understanding between the partners. Other risks can be identified for more specific models, are applicable to a particular sector or a specific location.

Lack of long-term commitment from the corporate partner. Setting up a sustainable IB that creates on-going employment opportunities requires the corporate partner to change its thinking to a longer term horizon. The rural entrepreneurs will need time to gain skills and the model itself will need adaptation as it develops. The corporate partner needs to be able to adjust to this new arena of doing business. As such, a dedicated team of people, who can operate with flexibility and with less stringent commercial targets needs to be in place. Of importance is financing for at least a period of three years, in which time no returns should be expected. The (offtake) commitment to the enterprise needs to stretch beyond the initial establishment phase to increase the chances of survival for the supported enterprise.

Another risk is the lack of mutual understanding. Before an IB is established, a thorough understanding of the particular location is required: existing enterprises, available skills and resources, internal community dynamics, social challenges of potential entrepreneurs, and the like. Vice versa, the entrepreneurs need to understand that engagement in an IB is not a get-rich-quick scenario.

A smaller IB risk relates to a lack of flexibility. The implementation of an IB is an iterative process and cannot be replicated without adapting specification of earlier implemented partnerships.

9 Risk mitigation

An independent entity dedicated to building inclusive partnerships can build a deep understanding of such initiatives. This understanding extends to understanding sources of external favourable funding such as government grants. Independence provides flexibility.

The risk related to community understanding requires the involvement of a well-established meso-organisation(s) which is familiar with the local people, resources and dynamics. Such organisations can be a for-profit organisation, an NGO, a church organisation or even the Community Works Programme partner. The role of this meso-organisation can be limited to

advisory services, engagement with community development, or tasked with the implementation of the IB.

10 Additional comments

This proposal covers a specific concept to stimulate enterprise development in the form of inclusive business partnerships in rural settlements outside of the agricultural sector. It does not present a specific model, but a number of main structures to engage with rural settlements for integration into commercial value chains. It is based on an analysis of a range of inclusive business models implemented in South Africa, but also in other developing countries. This analysis provides insights into critical elements that need to be taken into account when engaging in such partnerships.