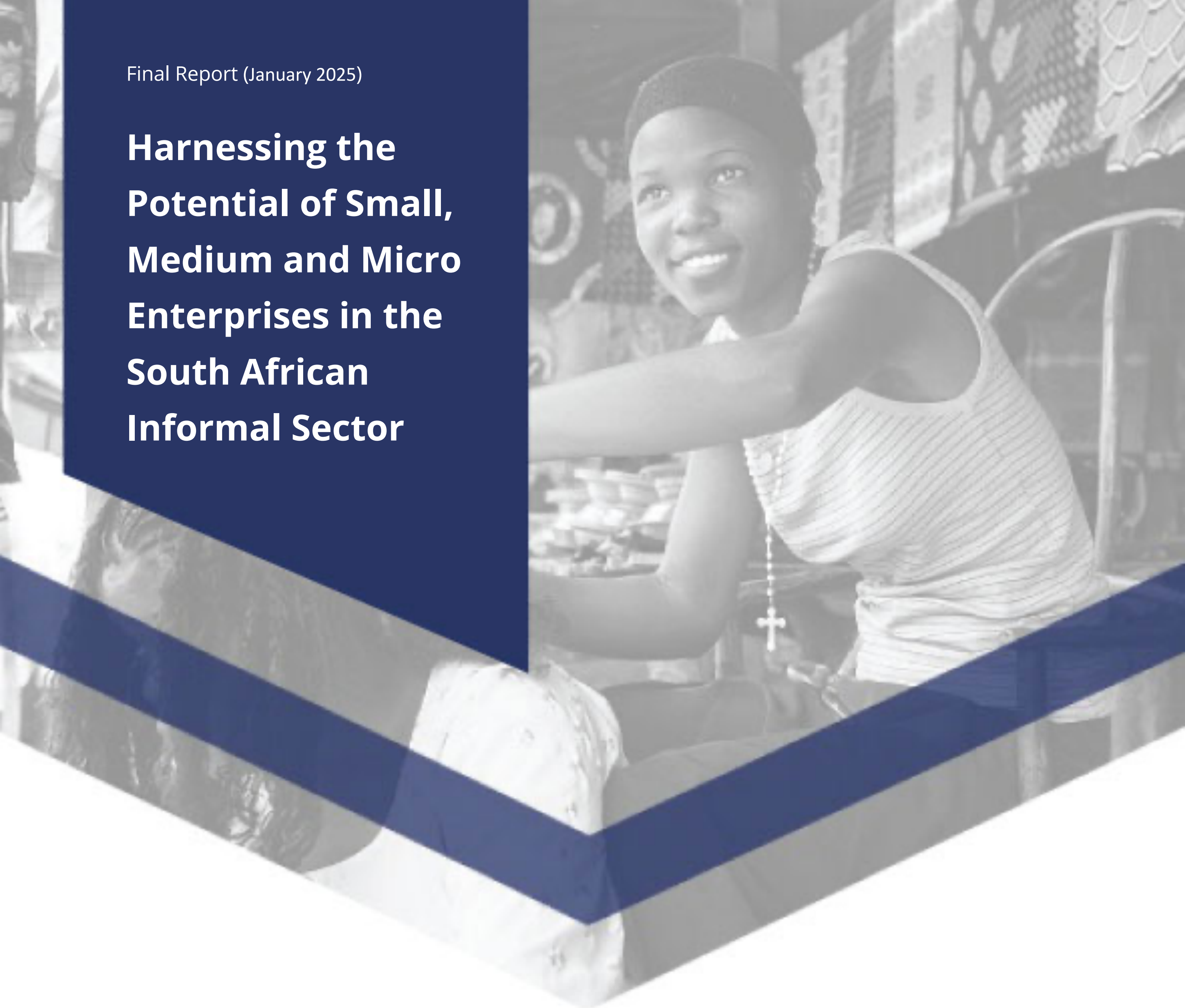
Final Report (January 2025)

Harnessing the Potential of Small, Medium and Micro Enterprises in the South African Informal Sector



Policy recommendations for the informal sector in South Africa

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Acronyms

Acronym	Description
AFI	Alliance for Financial Inclusion
AfDB	African Development Bank
BASA	Banking Association of South Africa
CBDA	Cooperative Bank's Development Agency
CIPC	Companies and Intellectual Property Commission
DSBD	Department of Small Business Development
EMDE	Emerging and Developing Economies
EU	European Union
FIC	Financial Intelligence Centre
FICA	Financial Intelligence Centre Act
FSCA	Financial Sector Conduct Authority
GDP	Gross Domestic Product
GPFI	Global Partnership for Financial Inclusion
IFC	International Finance Corporation
IFWG	Intergovernmental Fintech Working Group
ILO	International Labour Organization
NCR	National Credit Regulator
SALGA	South African Local Government Association
SARB	South African Reserve Bank
SARS	South African Revenue Service
Seda	Small Enterprise Development Agency
Sefa	Small Enterprise Funding Agency
SME	Small and Medium Enterprises
SMME	Small, Medium and Micro Enterprises
SOE	State-owned Enterprises
Stats SA	Statistics South Africa
VAT	Value Added Tax
WBG	World Bank Group

Executive Summary

The objective of this document is to provide recommendations that will be useful to inform future government policy on the informal sector in South Africa[1]. The document is based on a review of global informal sector experience, interviews with South African authorities, financial sector participants and experts, and a combination of qualitative and quantitative research. In a key departure from existing practices, suggested priorities consider that informal businesses are not homogeneous, particularly regarding their owner aspirations and goals, profitability and viability, constraints, and potential for formalisation. The document is primarily intended for use by the Department of Small Business Development (DSBD)[2] as a pathway to harmonising and strengthening informal small, medium and micro-enterprise (SMME) support currently spread across numerous policy documents and agencies.

The informal sector in South Africa is significant (estimated at 23.7% of GDP)[3], however, it is relatively small compared to peer middle-income countries despite the country's substantially higher unemployment rates[4, 5]. This has been attributed to historical and structural reasons, including laws from the colonial and apartheid eras which discouraged entrepreneurial spirit in black Africans[6]. Further, in contrast to a gradual drop in the levels of informality globally (as per cent of GDP), South Africa has seen a slow upward trend, demonstrating the untapped potential of the local informal sector. With its high prevalence among low-income earners, the informal sector presents a unique opportunity to contribute to reduced poverty and unemployment in communities that are often solely dependent on social security payments. A broader economic development policy is needed. However, an integrated government approach to supporting the informal sector is an important starting point.

The sector has had limited structured support due to a siloed and sometimes contradictory approach by government departments and agencies regarding informal businesses. The one-size-fits-all strategy and inadequate business identification and data have hindered progress. While there have been efforts to promote formalisation as a catch-all solution, this approach fails to recognise that businesses typically choose to formalise only when it is in their interest to do so in their development journey[7]. A more effective approach would be to acknowledge the informal sector's contribution as it currently exists and aim to increase efficiency and sustainability while creating simple pathways to formalisation for those minority segments that find it useful and offer the most promising policy option.

Emanating from research and engagements undertaken for this report, 13 key priorities across five areas (pillars) are proposed for further consideration and, in due course, implementation.

Pillar one: Policy approach

Priority 1 – Provide high-level policy direction: To lead and align the government's approach to informal businesses, it is recommended to issue a stand-alone policy statement from the Office of the Presidency that articulates a policy approach prioritising informal businesses. The statement should emphasise the importance of the informal sector and

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[1] Informality in this document follows the African Development Bank (AfDB) definition i.e. those economic activities not subject to government regulation, taxation or protection. This aligns to the ILO's definition i.e. economic activities and units that are not covered or insufficiently covered by formal arrangements

[2] The DSBD is mandated to lead and coordinate an integrated approach to the promotion and development of entrepreneurship, SMMEs and Co-operatives, and to ensure an enabling legislative and policy environment to support their growth and sustainability

[3] ACCA 2017.

[4] Asmal, Bhorat et al. 2024

[5] Cunningham 2023

[6] World Bank. 2018

[7] Levenson and Maloney, The Informal Sector, Firm Dynamics and Institutional Participation, World Bank, 1998

the need for cross-ministerial cooperation, as well as guide and align the actions of all actors in the informal ecosystem towards supporting the informal sector. The messaging should set out the framework for coordination and reporting, anticipated outcomes, and timelines; it should not be seen as discouraging formalisation or supporting enterprises that break the law. The statement should emphasise the need for entrepreneurship and skills development to address past injustices and promote reform to ease informal businesses' compliance with local and national laws.

Priority 2 – Determine a segmented approach for the informal sector: To address the limitations of a one-size-fits-all approach to informal sector support, a segmented approach should be defined for the informal sector to allow for targeted extension of market support services and initiatives. Suggested segments include:

a) A *basic segment* (Segment 1): Survivalist businesses with a turnover of less than R 100,000 annually. These are typically single-owner enterprises with little desire to expand but play an important role in supporting jobs and livelihoods.
b) An *emerging segment* (Segment 2): Businesses with a turnover between R100,000 and R300,000 annually. This segment represents informal businesses with the potential to grow if adequate support is provided.
c) An *established informal business segment* (Segment 3): Businesses with a turnover exceeding R300,000 annually. These enterprises demonstrate viability and potential for employment creation and include high-growth start-ups.
d) An *agricultural segment* (Segment 4) (for consideration): Self-employed individuals in agriculture, small farm owners with employees, and agri-businesses. This segment is distinct, given its unique operating realities.

The basic segment includes a majority of informal SMMEs, with an estimated breakdown of 60:30:5:5 across the segments.

Pillar two: Identification, registration and onboarding

Priority 3 – Pre-registration of informal businesses: Informal SMMEs, to a large extent, do not carry a unique identification, hindering their access to various formal services. Acknowledging that many informal enterprises are unlikely to participate in complete registration or formalisation processes, an intermediate status is proposed through a pre-registration identity system that can serve as the first step towards formalisation and may be used to provide a unique identifier for informal enterprises. Unlike existing single use-case databases, the identity will function across multiple platforms, e.g. to access finance, e-commerce, markets, business development support, and other services. The pre-registration identification system should be on a voluntary basis and delinked from business registration, tax and labour law requirements, with the owner or manager serving as a proxy for the enterprise. The pre-registration is expected to be relevant to all informal SMME segments, with higher uptake among Segments 2 – 4.

Priority 4 – Reshape the SMME registration and licensing process to be more integrated and streamlined: Given that some informal businesses may wish to transition into formal enterprises in their growth journey, it is recommended to review the formalisation process and make it as effortless as possible. A fully integrated business registration system with a one-stop process is proposed digitally, with links to all appropriate authorities, including tax, employment and labour, business support programmes and local authorities. The registration database should be directly available to qualifying entities via a standardised interface. A risk-based approach should be adopted for registration, licensing and inspections, avoiding excessive burden on low-risk businesses while protecting the public interest (health, safety and environment) in high-risk sectors and businesses. Further, the ongoing cost of compliance should be kept low, with increased access to the necessary services and institutions in local geographies or contexts (Priorities 1, 5, 6, 7, 10 and 12). This intervention will mostly apply to Segments 2 and 3.

Priority 5 – Update registration, licensing, finance and other laws and regulations to support informal businesses: To adequately support informal SMMEs, it is recommended to update relevant business registration, licensing, tax and financial sector[8] laws and regulations at the national and sub-national level to provide for a legal framework for the pre-registration status of informal businesses. Other laws and regulations on labour, social security, and immigration should also be reviewed to the extent the business identity system impacts them. The update will focus on recognising informal businesses, assigning a unique business identifier, easing registration, licensing and compliance through risk-based approaches, and promoting accessibility of credit and other services to the informal sector. Implementation practices must also be examined to ensure that enforcement is uniformly applied and aligned to the aspirations outlined in Priority 1. This intervention will impact all four segments.

Pillar three: Access to finance

Priority 6 – Broaden accessibility of financial services to the informal sector: Given the limited ability of banks to provide services to the informal SMME sector, it is recommended to strengthen available alternatives, especially cooperative financial institutions (CFIs), microfinance institutions (MFIs), fintechs and agency networks. These alternative providers face regulatory and other challenges that raise business costs or limit new products. There is also a lack of data in some subsectors. Key measures recommended include:

- Introduce tiered licensing and review compliance requirements in line with a risk-based approach.
- Establish a second-tier cooperative bank and adopt cooperative models in the informal sector.
- Increase data availability in the MFI sector and develop a national strategy for the sector.
- Identify and address the market, legal and regulatory barriers to the increased use of bank retail agents, including reviewing enabling legal and regulatory instruments[9], and availing data and evidence on the sector.
- Leverage the Intergovernmental Fintech Working Group (IFWG) regulatory sandbox and accelerator process to encourage fintech approaches to address financial inclusion challenges in the informal sector.
- Fast track legislative reforms in the National Payment Systems (NPS) Act and the Conduct of Financial Institutions (CoFI) Bill to enhance the supervision of fintechs and non-banks' role in retail payment and credit reporting systems, with interim measures to reinforce the supervision and monitoring of fintechs.

This intervention is relevant to all informal sector SMME segments, with MFIs and cooperatives broadening access at the lower end. At the same time, fintechs and agent networks would focus on the more sophisticated end of the informal SMMEs.

Priority 7 – Redesign public credit support programmes in line with international good practices: Public SMME credit support programmes should be redesigned in line with international best practices to improve their effectiveness by considering consolidating smaller programmes and redesigning programme features. A review should be undertaken to evaluate the quantity and effectiveness of public finance available to the sector, phase out direct lending, use additional intermediaries such as fintech companies, and expand credit guarantee facilities, especially for smaller and informal businesses. New programmes should be piloted, evaluated, and scaled up if effective. A coordination of public credit support programmes and business development services should be enhanced to improve enterprise performance. This intervention will be more relevant to larger informal SMMEs within Segments 2 – 4.

Priority 8: Improve credit infrastructure relevant to informal SMMEs: The lack of readily available credit risk assessment and mitigation mechanisms hampers access to credit by informal SMMEs. Using movable assets as collateral can potentially improve the availability and cost of credit. However, limitations in the legal framework make it difficult to recover assets in the event of a default. The lack of a modern, centralised and computerised movable assets registry also hampers uptake. The law on secured transactions should be reviewed, and an initiative should be

[8] For example on financial intermediaries, financial intelligence, and national payment systems

[9] The Banks Act 94 of 1990, The Financial Intelligence Centre Act No. 38 of 2001, and the Financial Advisory and Intermediary Services Act 37 of 2002

established to introduce a modern registry. In addition, the range and depth of data available from credit bureaus should be reviewed to include more SMME-related data, such as payments data, to improve reporting coverage among small lenders. This intervention is more relevant to larger informal SMMEs within Segments 2 – 4.

Priority 9 – Promote the use of digital payments by informal SMMEs: Digital payments are an essential first step towards financial inclusion of informal SMMEs who primarily operate as cash-only businesses. Innovation, especially around digital payments, is needed to address this situation; however, the landscape is dominated by banks focused on the formal sector. The role of non-bank payment service providers should be supported through reforms to the National Payment System Act to level the playing field between banks and non-banks and promote the interoperability of retail payment instruments. Community-based digitisation projects and financial and digital literacy programmes can complement the supply-side initiatives. Digitisation will be relevant to all segments of SMMEs, particularly those in Segments 2 – 4.

Pillar four: Business support

Priority 10 – Develop new programmes and extend existing SMME support programmes to the informal sector: Given the general lack of government support programmes that target less sophisticated informal businesses (Segments 1 and 2), the development of such programmes should be prioritised. Programmes targeted at Segment 1 should incorporate phased, multifaceted interventions that address various constraints, including basic knowledge, access, and clustering. SMMEs in Segment 2 could benefit from individualised mentoring and grant funding support, while larger informal enterprises in Segments 3 and 4 could benefit from extending existing business development support programmes, where possible. Further support could include integrating these larger informal SMMEs into government procurement, providing social support programmes for enterprises and their workers, and ensuring access to incubator projects.

Priority 11 – Promote financial, digital and business skills among informal enterprise owners: Enhancing business, digital and financial skills among informal sector SMMEs is crucial to their success. Efforts in these areas must be strengthened, particularly for digital technologies, and coordination must be improved. The proposed informal sector coordination platform (Priority 13) or a newly purpose-made coordination platform could be used to actively coordinate skills development activities. This would help align and further strengthen such skills support. It is important to involve key entities with a business development mandate, including the Financial Sector Conduct Authority (FSCA), Cooperative Bank's Development Agency (CBDA), Small Enterprise Development Agency (Seda) and Small Enterprise Finance Agency (Sefa). Additionally, this effort should be closely linked to the National Financial Inclusion Strategy and National Financial Education Strategy processes, which the National Treasury is developing. All segments of the informal sector will benefit from this intervention.

Pillar five: Enabling taxation framework

Priority 12 – Develop a tiered taxation system to cater for the informal sector: Tax is a barrier to formalisation for informal business owners, who typically already pay Value Added Tax (VAT). Due to the size of their businesses, informal SMME owners often cannot absorb additional costs related to other taxes or the associated administrative burden. By reducing and simplifying tax registration and payment and revising thresholds, eventual tax compliance can be more feasible. The approach to tax collection should, therefore, be overhauled to tax-exempt smaller informal SMMEs (Segment 1); introduce a simple, token all-inclusive tax on emerging enterprises (Segment 2), and a higher rate for established informal SMMEs (Segment 3) based on turnover and number of employees. A single payment should be used to limit compliance costs. Efforts should also be made to improve education on tax literacy to sensitise enterprise owners to the various tax elements and their implications for their businesses. The intervention will impact all informal SMME segments.

Governance and coordination

Priority 13 – Establish a formal coordination mechanism to champion and coordinate informal sector support: The above recommendations apply across government ministries, agencies and levels. These recommendations should be implemented in coordination with the relevant authorities, ensuring that the overall objectives of the reforms, the needs of vulnerable segments, and the country's specific context are adequately addressed. The coordination mechanism should be at a sufficiently high level and report directly to the President's office.

It is expected that this holistic approach, when implemented in conjunction with other developmental initiatives, will enable the informal SMME sector to contribute significantly to the economic well-being of South Africa.

Table of Recommendations

	Recommendation	Suggested responsible parties	Time horizon
	Pillar one: Policy approach		
1	Issue a stand-alone policy statement from the Office of the Presidency that articulates a policy approach that prioritises informal businesses.	NT, DSBD, DTIC, Presidency	Short-term
2	Determine a segmented approach for the informal sector to allow for the extension of market support services and initiatives.	DSBD, DTIC, CIPC and NT	Medium-term
3	Implement a pre-registration identification system for all informal enterprises on a voluntary basis and delinked from tax and labour law requirements.	DSBD, DTIC, CIPC and NT	Short-term
	Pillar two: Identification, registration, and onboarding		
4	Reshape the SMME registration and licensing process to be more integrated and streamlined.	DSBD, DTIC, CIPC SARS, FIC and NT	Medium-term
5	Update laws and regulations to accommodate informal businesses, particularly laws and regulations on tax, business registration, labour, social security, and national payment systems.	DSBD, DTIC, CIPC and NT	Medium-term
	Pillar three: Access to finance		
6	Broaden the accessibility of financial services to the informal sector, particularly through CFIs, MFIs, agency networks and fintechs.	DSBD, NT, SARB, FSCA, NCR, FIC	Long-term
7	Redesign public credit support programmes in line with international best practices.	DSBD, DTIC, NT	Medium-term
8	Improve the availability of credit information relevant to informal SMMEs.	DSBD, NCR, NT, SARB, FSCA	Medium-term
9	Promote the use of digital payments by informal SMMEs.	DSBD, Seda, Sefa, CBDA, digital service providers, innovative technology companies	Medium-term
	Pillar four: Business support		
10	Develop new programmes and extend existing SMME support to the informal sector.	DSBD, Seda, Sefa, CBDA, DBSA, FSCA	Medium-term
11	Promote financial, digital and business skills among informal enterprise owners.	DSBD, Seda, Sefa, CBDA, FSCA	Short-term
	Pillar five: Enabling taxation framework		
12	Develop a tiered taxation system to cater for the informal sector.	DSBD, NT, SARS	Long-term
13	Establish a formal coordination mechanism to catalyse informal sector support.	DSBD, Presidency	Short-term

Note: "ST (short-term)" refers to 1–3 years, and "MT (medium-term) refers to 3–5 years.

1. Introduction – An Informal SMME Support Framework for South Africa

South Africa is marked by a persistently low economic growth rate, an increasing level of unemployment and a rising number of people who are directly and often solely dependent on monthly social security payments. This document considers how the informal sector can be strengthened to contribute to addressing this challenge in a meaningful way. Properly enabled, the sector has largely untapped potential that should be harnessed as a viable pathway to job creation: the informal sector contributes around 20% to the Gross Domestic Product in South Africa compared to 40% in Sub-Saharan African countries[10]. While it is recognised that a broader and more inclusive economic development policy is required, the informal SMME sector offers an opportunity to begin to address some areas. A meaningful impact on economic growth and job creation can be achieved if the informal sector can be supported to the extent where its contribution to the national economy aligns with its potential.

This document aims to develop and detail a support framework for the informal sector in South Africa. The document outlines key recommendations that should be used to coordinate activities in the informal sector and to inform future government policy positions in the SMME sector. In so doing, it also provides a pathway to harmonising various informal SMME policy documents and support mechanisms currently spread across multiple policy documents and departments. The suggested policy approaches will ensure that the informal sector can better contribute to the national agenda, particularly regarding economic growth and job creation.

Informality in this document follows the African Development Bank (AfDB) definition: *The informal economy is broadly defined as those economic activities not subject to government regulation, taxation, or protection*. This is not inconsistent with the International Labour Organisation's definition: *All economic activities by workers and economic units that are – in law or in practice – not covered or insufficiently covered by formal arrangements*[11].

The support framework developed here primarily aims to support the ongoing work undertaken by the Department of Small Business Development. However, it is necessary to involve several other authorities whose mandate is to implement specific elements of the recommendations proposed in this document. The intention is that this document will be used by policymakers in unison to create an appropriate policy framework that truly harnesses the great potential presented by the informal sector.

The proposed policy priorities are arranged in five pillars that inform the analysis and suggested recommendations. These pillars reflect the areas of greatest need for reform to facilitate the informal sector in South Africa:

- Pillar 1 – Policy approach
- Pillar 2 – Identification, registration, and onboarding
- Pillar 3 – Access to finance
- Pillar 4 – Business support
- Pillar 5 – Enabling taxation framework.

The document consists of four main sections:

- An overview of the global informal sector in Chapter 2, with a view to understanding global trends that inform the recommended policy approaches.
- An overview of the South African informal landscape is presented in Chapter 3 to present the importance and structure of the sector and key drivers of informality.

[10] IMF (2017).

[11] These definitions exclude all criminal and illegal cross-border activities.

- An analysis of each of the pillars in Chapters 4 – 8 to provide informed insights and a basis for the recommendations. This section includes an analysis of some of the more pressing challenges and constraints facing informal enterprises in South Africa and a set of recommendations that will ensure a cohesive policy approach, pathways to formalisation, and enhanced support to SMMEs that remain informal.
- Chapter 9 presents a brief review of the broader governance issues that need to be considered.

This document was developed by the World Bank Group in partnership with FinMark Trust as part of their efforts to contribute to inclusive growth and employment in South Africa.

2. The Global Informal Sector

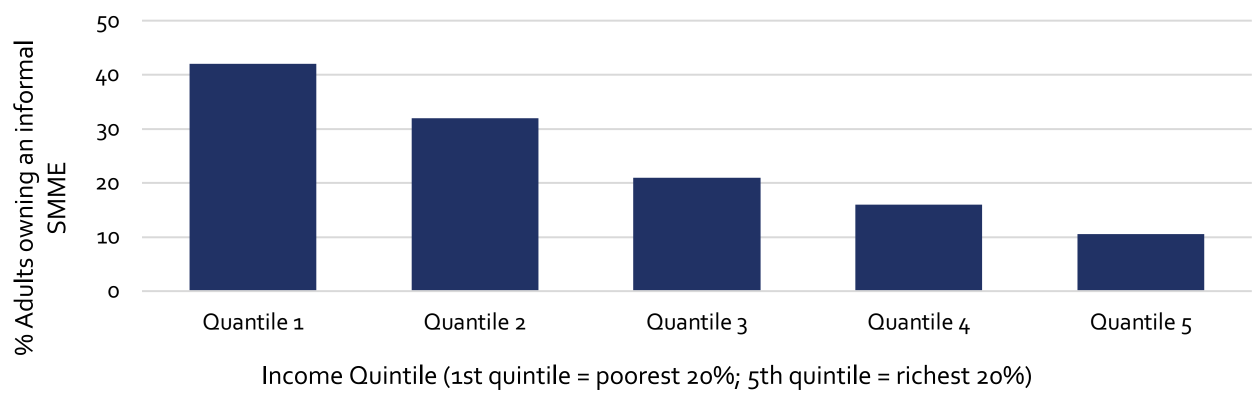
2.1 Overview of the global informal SMME sector

The informal sector encompasses a diverse range of SMME types, varying in size from one-person survivalist-type micro-enterprises to sizable medium enterprises employing scores of people. The diversity extends to varying levels of maturity and length of operation, reasons for starting a business and for operating informally, and the different challenges that vulnerable groups face when operating a business. Policy interventions and initiatives must take these differences into account in the design and implementation of support frameworks to avoid a one-size-fits-all approach.

Informality is associated with the level of economic development and the support ecosystems associated with such development. In general, the higher the level of economic development in a country, the lower the level of informality. Economic shocks can also result in fluctuations in the level of informality, as demonstrated during the Covid-19 pandemic when informality increased, partly because of the higher cost of doing business.

Chart 1 below illustrates the dependence of informality on economic development by plotting the estimated level of informal business ownership against per capita GDP quintiles[12].

Chart 1: Informality is widespread in poorer countries *(adults owning an informal business, using the proxy of per cent who report being self-employed or owning a business with two or fewer employees, by income quintile as measured by country-level GDP per capita % age 15+)*



Source: *Klapper L., Miller M. and Hess J., World Bank Group 2019, Leveraging Digital Financial Solutions to Promote Formal Business Participation*

[12] Klapper, L. *et al* 2019

Given the significant role of the informal economy, the level of economic development should not act as a constraint when considering support for the sector, as a more vigorous and economically contributing sector will directly lead to increased economic development with a greater chance for increased formalisation.

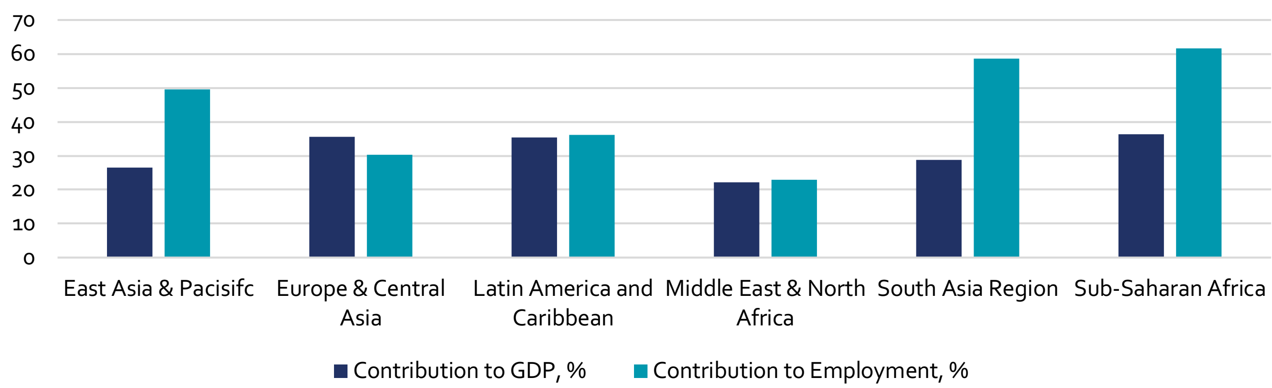
From the perspective of economic and development policymakers, the informal sector presents opportunities and dilemmas. On the one hand, the sector is often characterised by low productivity, uncertain working conditions, low or no tax contributions, lacking in the responsible use of natural resources, and potential competition with formal businesses on an unequal footing. The combination of these factors makes formalisation and stricter governance appear as attractive policy options. On the other hand, the informal sector provides real job opportunities to many people who are unable to find employment elsewhere, especially formal employment. The unstructured basis of employment in the informal sector provides business flexibility, which would otherwise not be possible. Informal businesses also provide goods and services where formal businesses may not. A more comprehensive, nuanced and tiered approach is required to balance the demands of government with the realities of the sector.

2.2 Size and importance of the global informal SMME sector

The contribution of the informal sector to national economies is significant, with around 80.9% of global small businesses being informal[13]. Despite consistent efforts to increase formality in many countries, the level of informality remains stubbornly high. There is evidence that overall global levels of informality have decreased; however, the decrease is not uniform, as informality remains persistently high in some jurisdictions.

The informal sector also makes a significant contribution to the economies of emerging and developing economies (EMDEs), accounting for about a third of GDP[14], with this contribution higher in some countries, particularly in agrarian-based economies. An estimated 82.5% of enterprises in EMDEs are in the informal sector, and nearly 70% of employment in EMDEs (69.6%) is informal,[15] compared with less than 20% in developed countries. Chart 2 below shows the varying levels of the contribution of the informal sector output to GDP (expressed as a per cent of total GDP) and informal employment (as measured through self-employment) to total employment per EMDE region[16].

Chart 2: Contribution of the informal sector to GDP and employment per EMDE region



[13] ILO 2018

[14] Ohnsorge F. *et al* 2021

[15] ILO 2018 *Women and Men in the Informal Economy*

[16] Ohnsorge F. *et al* 2021.

Source: Ohnsorge F. and Shu Yu World Bank Group 2021, The Long Shadow of Informality: Challenges and Policies

As measured over the last three decades, the level of informality has declined in terms of the relative size and percentage of the sector, as well as the percentage of informally employed people. This is a complex phenomenon resulting from multiple influences, with general economic development being one crucial factor. On average, informal output compared to GDP fell by about 7% to the current level of approximately one-third of GDP in EMDEs, compared to an average decline of about 3% in developed economies. The share of informal employment, as measured by self-employment, fell by about 10% in EMDEs compared to a 3% decline in developed economies. These averages do not reflect the wide range of informality levels still evident across EMDEs.

In Sub-Saharan Africa, the output of the informal sector represents 36% of the official GDP, which is the highest of the EMDE regions[17]. Informal employment is also the highest among the EMDE regions. However, there is significant variation within the region. Informality rates in South Africa and Mauritius are significantly lower than in the rest of the region. In line with global trends, informality in the Sub-Saharan Africa region has declined over the last three decades.

2.3 Drivers of informality

The basic root causes of informality are generally accepted to be lack of development and poor governance[18]. The lack of development is the broader concept underpinning the link between informality and poverty mentioned above. Economies at lower levels of development often do not have the capacity to establish and maintain appropriate levels of governance and support, thereby directly reinforcing the link with informality. Insufficient governance, however, is also associated with fragile states and states in political uncertainty, making it a separate root cause.

There are a number of different models that attempt to explain why enterprises choose to remain in or move to the informal space[19]. These models can be categorised as follows:

- **Exclusion model:** Informal enterprises are excluded or dissuaded from engaging with the formal economy because of market rigidities (e.g. minimum wages) and the cost of formalisation – burdensome formalisation cost and requirements, and excessive tax and regulatory compliance burdens once registered.
- **Rational exit model:** The decision to formalise or not is assumed to be a rational business decision based on objective cost-benefit analyses of formalisation for the enterprise and the government's enforcement effort and capability. If there is a quantifiable economic benefit, then enterprises will formalise; otherwise not.
- **Parasite model:** It is assumed that the formalisation decision is primarily related to the quality and thoroughness of regulatory oversight. Enterprises will remain informal if there is a low level of enforcement and if the costs to formalise are perceived to be high. A version of this model is likely to emerge in oversight regimes with noticeable corruption.
- **Dual economy model**: It is assumed that informal and formal enterprises operate in two distinct spheres, with informal activities not impacting formal enterprises. This is based on the idea that informal enterprises exhibit different characteristics, such as largely being small, less productive and run by low-skilled entrepreneurs. As a result, the majority of informal firms are likely to be crowded out over time by more productive firms.
- **The structuralist model**: The informal economy is viewed as a subordinate component to the formal economy, providing low-cost inputs and flexibility to the formal sector. In essence, the two sectors co-exist and are both inherent parts of the national economy.

[17] Ohnsorge F. *et al* 2021

[18] See for example Marusic, A.*et al* 2019

[19] See for example Floridi A., *et al* 2020 and Perry GE et al 2007

The dual economy model is largely a conceptual view of informality, but the other models are likely to co-exist and overlap in most economies. This complicates the task of policymakers, as the different reasons and scenarios need to be considered when formulating policies and interventions.

In addition to the reasons embedded in these models, there are additional issues that should also be considered when formulating policy responses[20]:

- **Poor government services**: In many developing countries, formalisation has no impact on the level of government services. Enterprises operating in rural and poor areas are often subject to poor road and other transport infrastructure, inadequate electricity supply, lack of basic services like rubbish removal, and so on. The cost of registration simply becomes an additional cost with little, if any, benefit.
- **Exclusion and marginalisation:** Certain vulnerable groups, like women, youth and minority groups, are sometimes underrepresented in the formal economy due to social conditions, making the informal sector more attractive to such groups. Policy interventions that explicitly recognise the constraints facing these groups are required to address the situation.
- **Survivalist enterprises**: Poverty and unemployment force many people into starting a micro-enterprise as the only means of generating some income. People in this group typically have little interest in growing the enterprise and would probably abandon the effort if reasonable employment becomes available. This group usually does not consider formalisation as something that is applicable to them. There are also a significant number of survivalist SMME owners who choose to be self-employed rather than to be employed. Many maintain modest strategies as they feel hindered by financial, personal and market constraints, suggesting a role for public policy to better support them in achieving their aspirations[21].

2.4 Global effort towards formalisation

Many governments have attempted to increase the level of formality in their business sectors over the last three decades. Globally, the traditional approaches to increasing formality include:

- Reducing the cost and complexities of registration
- Providing information on the benefits of and procedures for formalisation
- Increasing enforcement
- Reducing and simplifying the tax burden and providing tax incentives, though these appear to have had mixed results[22], with many efforts not being very successful or having only been marginally successful.

While much emphasis has been placed on reducing registration costs, the available results indicate that easing entry into the formal sector has had a limited effect on formalisation, with larger formalisation results coming from reducing the ongoing costs associated with formality or, conversely, increasing its benefits and through greater enforcement[23]. The finding is linked to the root causes of informality, with three primary causes being explored. Firstly, firms remain informal to avoid high entry costs; secondly, they are informal to avoid complying with taxes and other regulatory burdens, meaning that lighter compliance requirements and enforcement would be effective; and lastly, informal firms are used as a survival strategy for low-skilled individuals and are, therefore, too unproductive to ever become formal. An example from Brazil estimated that 9% of informal firms fit into the first category, 42% into the second, i.e. choose to remain informal to enjoy the cost advantages, while 49% are too unproductive to ever become formal. Increasing enforcement could be very effective for the 42% avoiding the formal system; however, a blanket application can

[20] ILO 2016 *Policies, Strategies and Practices for the Formalisation of Micro and Small Enterprises*

[21] Cerkez N., et al (June 2024).

[22] See Marusic A, *et al* 2019

[23] Ulyssea G., 2020

generate adverse effects for the 49% in the last category, who would be forced to simply exit with concomitant job losses.

Other major insights drawn from these efforts are that:

- It requires an actively coordinated effort among all stakeholders over a significant period to enhance the sector. Creating the appropriate environment for enterprise formalisation will take considerable time as it requires the establishment of an enabling environment with strong institutions, laws and regulations, infrastructure and education. In addition, it involves identifying appropriate business incentives for enterprises, such as access to new market opportunities and access to financial and non-financial services[24] for enterprises.
- Informality is unlikely to disappear or become negligible.
- Informality is often the only alternative for the unemployed and those in poverty.
- For many informal enterprises, formalisation seems to be an impractical and unnecessary step.
- Generally, micro-enterprises are the least likely to formalise or obtain benefits from formalisation that exceed the cost of formalisation.
- Some interventions have had some success, such as stricter enforcement of regulations and targeted incentive payments.
- Policy reforms and educational programmes have resulted in a modest impact at best[25].
- Efforts aimed at simplifying registration processes for informal enterprises have had a moderate impact, although the processes still remain somewhat cumbersome.

The International Labour Organization (ILO) has been instrumental in promoting greater formality among its members, especially with the adoption of Recommendation 204 in 2015, by the International Labour Conference. This is referred to as the '*Recommendation Concerning the Transition from the Informal to the Formal Economy*'. The recommendation, with its 12 principles, guides members in their efforts to transition the informal sector and workers to the formal economy[26].

2.5 Emerging policy options for informal sector support and pathways to formalisation

Some of the most informative emerging principles in formulating and implementing formalisation policies and strategies include:

- Reducing informality, but not at all costs or in any possible way. Consider the impact of interventions and adjust these to minimise negative consequences, while treating all actors fairly.
- Making formality attractive rather than only penalising informality. It should be worthwhile for the enterprise owner – formalisation needs to make sense to SMMEs, not only to the government.
- Focusing on formalising labour and economic activity, not necessarily all enterprises. Most micro-enterprises are inefficient and would gradually exit the market as economic development unfolds. Formalisation should be pursued for larger informal enterprises as these can generate growth and employment to a greater extent than survivalist enterprises. This points to targeted approaches towards formalisation, i.e. a segmented approach to formalisation that considers the size and maturity of an informal enterprise.
- Developing and implementing a comprehensive and well-integrated strategy. Isolated reforms are unlikely to bring about a significant impact. The strategy must include interventions that address the complexity and distinctiveness of informality in the country concerned, with alignment across all areas involved in the ecosystem. Where possible, include the benefits of digitalisation and technological development.

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[24] IFC 2013

[25] Klapper, L. *et al* 2019

[26] ILO 2016 *Policies, Strategies and Practices for the Formalisation of Micro and Small Enterprises*

- Considering the behavioural aspects of the informal enterprise owners. There are various psychosocial factors that drive these business owners to remain informal.
- Making the labour market more flexible to adapt to changing conditions while reforming social protection to focus on workers, regardless of their employment status.
- Making the regulatory framework and the justice system more efficient. The regulatory framework should promote business development, market competition and the protection of workers and consumers.
- Rationalising the tax system. The tax system should be as simple as possible and easy to understand[27].
- Expanding and developing an inclusive financial services sector.
- Approaching the informal sector with the understanding that it is not a monolithic group. Rather, it comprises enterprises that differ in size, maturity and reasons for operating (e.g. small enterprises that operate for the sole purpose of household income generation versus larger enterprises that employ other people). Proper context sensitive segmenting and targeting can allow differentiated approaches towards informal businesses, as well as behavioural insights that might lead to different interventions.
- Intervening in the sector through a behavioural lens that acknowledges that informal enterprises function differently, i.e. tailor support initiatives to the specific ways in which informal enterprises conduct their business activities.

There are varying and evolving views on how the informal sector should be regarded, which is why the approach to formality should be flexible. Typically, the policy drive for greater formality is based on assumptions of enhanced sustainability, improved quality of employment and increased contributions to the economy and tax base. In Africa, especially Sub-Saharan Africa, the persistently high informality levels and the reliance most people seeking employment have on informality have led to a slightly different approach. There is a greater emphasis on the developmental aspect of the informal sector compared to other EMDE regions. The focus is more on poverty alleviation and the basic employment aspects of the informal economy than its potential contribution to GDP and tax revenue[28]. This also implies that any effort on formalisation should recognise the continued existence and value of many SMMEs in the informal sector in line with the above policy approaches.

The approach towards providing a comprehensive support framework for informal SMMEs can be informed by lessons learnt in the formalisation effort, which to date has received much focus. These include the need for an all-inclusive and integrated approach, as highlighted in a number of research documents[29]. The effort should include policy interventions in related fields to ensure maximum impact and support. The ILO recommends the adoption of an integrated approach that is "included in national development strategies or plans as well as in poverty reduction strategies and budgets, taking into account, where appropriate, the role of different levels of government"[30]. A national approach, supported by legislation that accepts the role of the informal sector and ensures a coordinated approach, holds promise.

As highlighted below (Box 1), Brazil implemented a comprehensive set of measures, including a simplified tax system, and achieved a significant shift toward formalisation of the working population, led by small and micro-enterprises. In the case of Ecuador, this is done under a single law. The informal sector is acknowledged in the constitution and a unified approach is propagated by the government. Ecuador[31] focused mainly on informality as it relates to informal employment in the formal sector. Constitutional and legal reforms strengthened the rights of informal workers and the obligations of employers. As an example, employers were penalised for not providing coverage for social security. In addition, policies were introduced to make the transition to formal employment more attractive and payments easier.

[27] Loayza, N.V. 2018

[28] ILO 2020

[29] See for example AFI 2021 and ILO 2016, *Policies, Strategies and Practices for the Formalisation of Micro and Small Enterprises*

[30] *ILO 2016, Policies, Strategies and Practices for the Formalisation of Micro and Small Enterprises*

[31] ILO 2014, Notes on Formalisation, Trends in Informal Employment in Ecuador: 2009 – 2012

Ecuador also reactivated labour inspection offices that monitored compliance with affiliation and labour obligations for businesses and homes.

The Philippines offers a slightly different approach where it addresses the onboarding of small enterprises and facilitates the cooperation between stakeholders through two mechanisms[32]:

- The Barangay Micro Business Enterprise (BMBE) Act governs the formalisation of micro-enterprises in the country. Micro-enterprises receive benefits such as tax exemption and market assistance, among others. To facilitate access to finance, the law also covers special credit windows targeted at micro-enterprises as well as incentives for financial institutions that offer loans to micro-enterprises.
- The Financial Inclusion Steering Committee (FISC), the inter-agency body mandated to implement the Philippine National Financial Inclusion Strategy, includes all relevant actors in the SMME ecosystem, including actors in the informal sector. The Philippine Commission for Women, an agency focused on women's empowerment, is also included and provides a focal point for gender-sensitive issues.

[32] AFI 2021

Box 1: Formalisation efforts in Brazil

Brazil has developed an integrated support system and a set of laws and interventions to promote formalisation.

- The Brazilian micro and small enterprise support agency Servicio Brasileño de Apoyo a las Micro y Pequeñas Empresas) (SEBREAE) was established as the main small enterprise development support body, offering assistance in technology development, market access, credit guarantees and local economic development. It is operational throughout the country with representation at municipal level at over 700 service centres.
- The Simples Federal Law 9317 simplified tax regulation for micro- and small enterprises by creating an integrated system for the payment of tax and social security contributions. This was further enhanced through a general law for SMMEs Simples Nacional that simplified all taxes and social security payments to all authorities into a single payment that is simple to calculate and administer.
- A complementary law for SMMEs, Lei Complementar Micro Empreendedor Individual (IME), enables small entrepreneurs and own account workers to register as individual microentrepreneurs. Registration is simple and done through a digital portal, with verification done by the local municipality. The entrepreneur pays a fixed monthly fee covering all taxes and social security payments. Many of these entrepreneurs also receive the conditional cash transfer programme Bolsa Familia, thus establishing coherence between social and formalisation policies.
- The general law covering micro and small enterprises gives registered enterprises sole access to public procurement of goods, services and works up to a predetermined value.
- Banks and other FSPs must advance loans to poor families and SMMEs to the value of 2% of all demand deposits such service providers hold.
- Brazil streamlined its procedures for low-value exports, introducing a simplified customs clearance procedure, Despacho Simplificado de Exportação (DSE), for exports up to a specified maximum value. Exporting SMEs use this procedure extensively.
- Brazil also created a national network for the simplification of business registration and legalisation, known as REDESIM (Rede Nacional para a Simplificação do Registro e da Legalização de Empresas e Negócios). REDESIM aims to streamline and integrate into a single system all registration and licensing procedures related to the start-up, operation and closure of companies, regardless of their size.
- In rural areas, the Programa Nacional de Fortalecimento da Agricultura Familiar (PRONAF) programme supports family-based agriculture by financing small farming projects. In order to access PRONAF credit lines, farmers must open a bank account in a formal financial institution.
- Resulting from the initiatives, there was a significant shift toward formalisation of the working population, led by small and micro-enterprises. The formalisation rate among own-account workers increased by 55.4% and among contributing family workers by 3.5 times. While the SIMPLES Nacional was a key anchor of this success, the achievements resulted from an integrated set of policies that combined enterprise development promotion with access to credit and a more favourable regulatory environment.

Source: *FORLAC and ILO 2014*

3. The South African Informal Sector

3.1 Overview of the South African informal sector

The role of the informal sector

The informal sector plays a significant role in the South African economy. Although relatively smaller than the informal sector in other Sub-Saharan African countries, its estimated size has remained fairly constant compared to GDP, while globally, the informal sector is slowly shrinking (see further discussion of this in Section 3.3 below). The estimated size of South Africa's informal economy (as a percentage of GDP) was 23,49 in 2011 and is projected at 24,19 by 2025. Among the factors supporting the growth of the informal sector include the near-stagnant economic growth (estimated at 2,04% annually as of 2021[33]) resulting in a lack of employment opportunities and regular job-shedding by corporates and formal SMMEs. This is exacerbated by the ongoing energy crisis, the impact of the economic shutdown in response to Covid-19, and the relatively low level of skills of many of the new job entrants, resulting in few matches with available opportunities. The largely stagnant South African formal sector, as well as government at all levels and State-Owned Enterprises (SOEs), continue to provide the bulk of job opportunities in the country.

It is notable that the informal sector's contribution to employment in South Africa (16% of adults) and the share of enterprises that are informal is much lower than in comparator countries of a similar level of development, emphasising the untapped potential of the informal business sector. Asmal and Bhorat et al. (2024), in particular, present an analysis showing that the ratio of wage employed to informally employed to unemployed in Middle-Income Countries globally is around 45:45:10 for every 100 individuals in the labour force. The ratio for South Africa, in contrast, is 50:16:34; while formal employment at 50% of adults is above average in South Africa, other middle-income economies are able to absorb more people into informal employment, resulting in lower overall unemployment (45% of adults are typically absorbed into the informal sector, compared to only 16% in South Africa). Mexico has much more of its working-age population in informal services like hospitality, retail trade, transport, and construction.

This results in South Africa having an unemployment rate that is one the highest among middle-income countries, suggesting that if its informal sector were similar to the average middle-income country, unemployment would be much lower. South Africa's past may partly help explain the relatively small informal sector in comparison to other countries. The suppression of entrepreneurial activity during the colonial and apartheid eras actively discouraged entrepreneurial spirit in black Africans, notably through restrictive legislation such as the Native Urban Areas Act, harsh licensing, strict zoning regulations, and the effective detection and prosecution of offenders[34].

Nevertheless, given the absence of formal employment opportunities, it might have been expected that the informal sector would experience a higher rate of growth as people seek alternatives, but research[35] into this aspect reveals that this is not the case. There are still significant entry barriers into the informal sector, including but not limited to low levels of entrepreneurial spirit, a lack of adequate equipment or infrastructure, a lack of access to viable markets, a lack of basic business and financial management skills, and the absence of knowledge and basic requirements needed to obtain support from organisations that target the informal sector.

The informal sector provides services and goods beyond the reach of the formal sector or government services. This is particularly evident in communities, or part of communities, where such services and goods are needed but are not readily available. The sector, therefore, plays a bridging role in the South African economy, and this is a permanent

[33] https://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?locations=ZA

[34] World Bank. 2018..

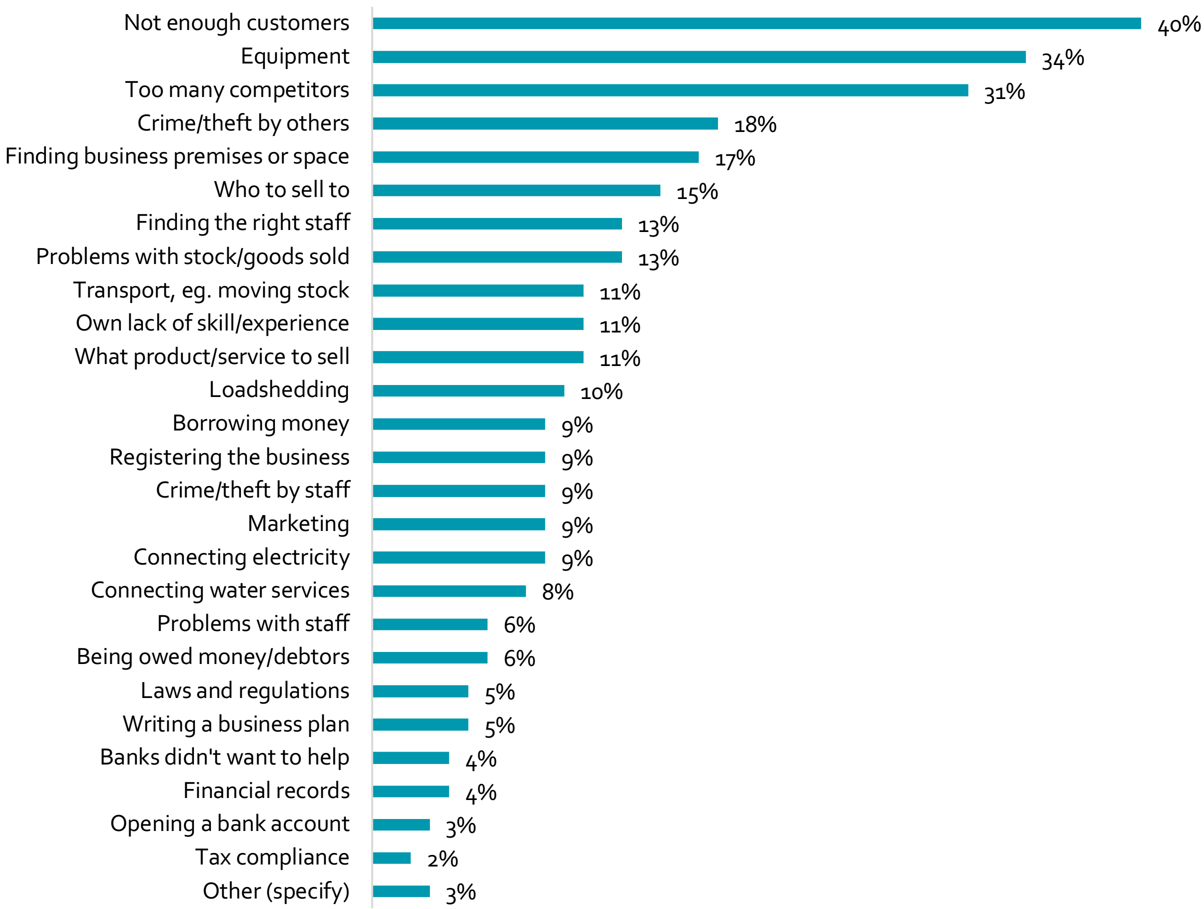
[35] Burger P; Fourie F 2019

feature of the national economy. Supporting the informal sector to improve efficiencies and, where possible, extend its employment capacity would be in the interest of the economy as a whole. In such endeavours, it is important that policymakers recognise the diverse nature of the informal sector and avoid employing a uniform approach to support or simply target greater formalisation.

Challenges facing informal sector SMMEs in South Africa

The informal sector's challenges in South Africa largely reflect the challenges in most developing and emerging economies within the domestic context. These include significant competitive pressures, rudimentary technology access and adoption, lack of social protection for the sector, inadequate physical and digital infrastructure, crime and security concerns, non-standardisation of goods and services, the vagaries of zoning classifications and general lack of business premises, and non-enabling government policies[36]. These challenges manifest in a variety of issues at the business start-up[37] level and often persist throughout the lifespan of the enterprise.

Chart 3: Challenges faced by the informal sector in South Africa



[36] Etim, E. and Daramola O. 2020.

[37] IFC 2020.

Source: *IFC 2020, The MSME Voice: Growing South Africa's Small Business Sector*[38].

Qualitative research undertaken by FinMark Trust[39] within the informal sector largely validates the chart above, and highlights the following issues:

- Challenges accessing financial support (loans, grants, etc.)
- Loadshedding and poor mobile network
- Lack of reliable revenue (e.g. late payment by customers who buy products on credit)
- Lack of customers
- Lack of space to operate (e.g. land and shelter)
- Women business owners often feel more vulnerable to crime
- Migrants must constantly hide from officials
- Water availability is sometimes an issue, e.g. for those selling food, operating salons and car washes.

The challenges faced by informal enterprises relating to access to and usage of financial services are further outlined in Section 6.1, while those related to a lack of access to business support services are further elaborated on in Section 7.1.

3.2 Drivers of informality in the South African context

There are strong drivers for informality in the South African economy, including the lack of real economic growth, as discussed in Section 3.1 above. Other major elements include the quality and level of government services and oversight, as well as criminal activity and the level of law and order[40]. The historical situation with job reservation[41], which forced many skilled artisans and others to operate 'under the radar' has left a lasting legacy of societal acceptance of informality. This is further exacerbated by high unemployment in South Africa, which drives individuals into the informal sector where obtaining job opportunities is less stringent. South Africa has one of the highest reported unemployment rates in the world, with the latest rates depicted in the table below.

Table 1: Employment rates in South Africa Q3 2022[42]

Adults of working age	Number	Percentage
Employed	15,8 m	
Unemployed	7,7 m	32,8% - unemployment rate
Discouraged work seekers	3,5 m	41,5% - expanded unemployment rate

Source: *Stats SA, Quarterly Labour Force Survey (QLFS) Q3:2022*

This compares with the global average of 6,2% estimated by the World Bank and based on ILO figures as of the end of 2021. The unemployment rate in some of South Africa's neighbouring countries, including Lesotho, Eswatini, Namibia

[38] The MSME Voice (IFC 2020 survey) qualitative phase comprised of 45 interviews with business owners across three cities (Johannesburg, Durban and Cape Town) in April/May 2019. The quantitative phase comprised 2,555 face-to-face interviews with business owners conducted between May and September 2019. These included 1,555 formal businesses generated from business lists, and 1,000 informal businesses sampled from across the eight major metropolitan areas.

[39] Research undertaken during June 2023 by TRS on behalf of FMT

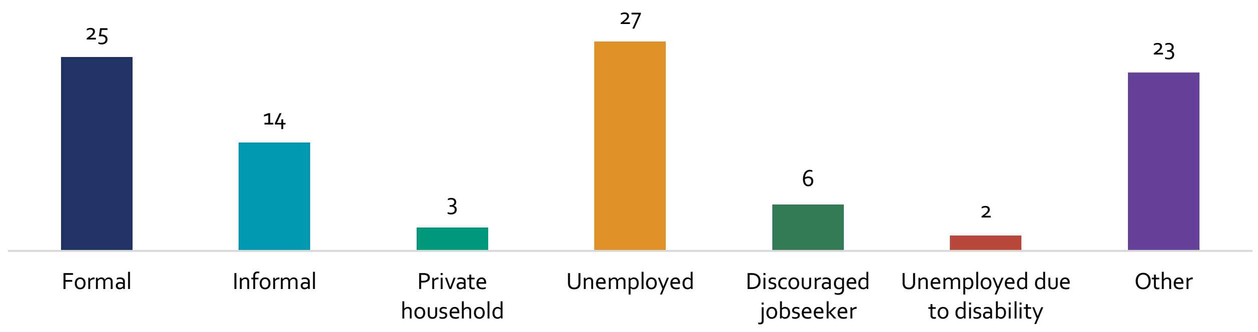
[40] Bowmaker-Falconer, A. and Meyer, N. 2022 & Etim, E. & Daramola, O. 2020

[41] A part of apartheid legislation, the job reservation act limited job opportunities specific races thereby excluding Black, Coloured and Indian people from the majority of employment opportunities.

[42] Stats SA, *Quarterly Labour Force Survey (QLFS) Q3:2022*

and Botswana, is also high, all exceeding 20%. The high unemployment rate is worrying; however, of greater concern are the youth unemployment rates: 59,6% of young people aged 15-24 years are unemployed and 40,5% of those aged 25-34 years are also without employment. Additionally, 34,5% of people aged 15-24 are neither employed, in education nor in training[43]. The employment profile for South Africa, based on FinScope Consumer results, is shown in the chart that follows[44].

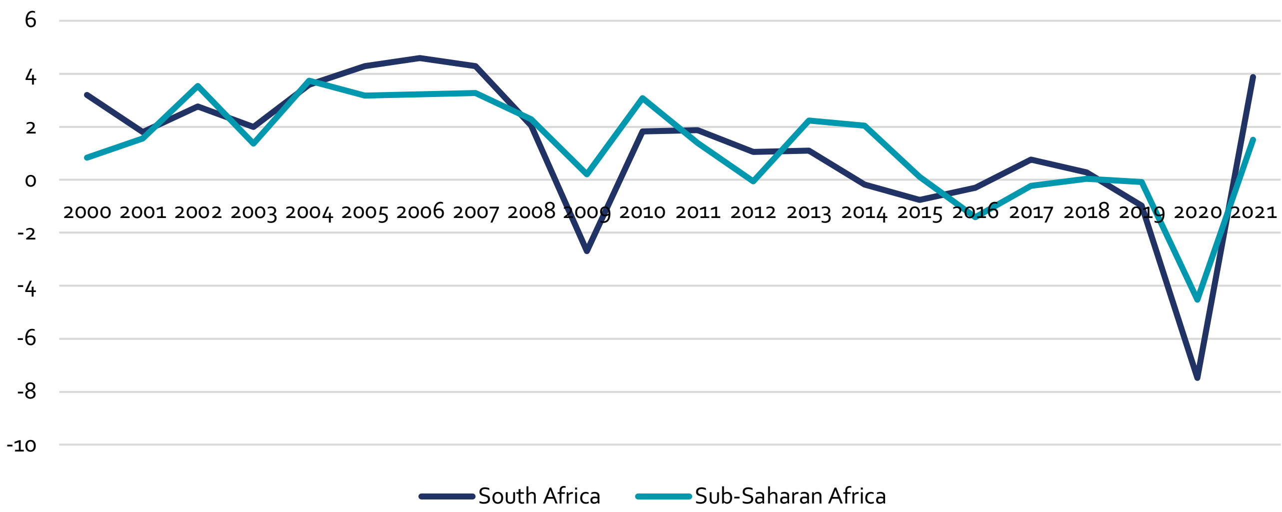
Chart 4 – Employment status of South Africans (% of adults)



Source: *FinScope Consumer 2022 survey results.*

Another factor driving informality in the country is a GDP per capita growth rate that makes it difficult for the economy to absorb the growing demand for jobs. A review of growth trends over the last 20 years paints a pessimistic picture. South Africa's GDP per capita growth rate indicates an overall trend towards lower growth, including periods of negative growth. This is largely consistent with trends in the rest of the Sub-Saharan Africa region[45].

Chart 5: Growth in GDP/capita



Source: World Bank https://data.worldbank.org/indicator/NY.GDP.PCAP.KD.ZG?locations=ZA

[43] Stats SA, *Quarterly Labour Force Survey (QLFS) Q3:2022*

[44] FinScope 2022 survey result

[45] World Bank https://data.worldbank.org/indicator/NY.GDP.PCAP.KD.ZG?locations=ZA

All these factors combined exert pressure on the informal sector to provide opportunities and absorb job seekers. However, as mentioned earlier, this is largely not happening in South Africa. While the sector constitutes a sizable portion of the economy, it is not experiencing significant growth in comparison to GDP, as illustrated in Table 2 below. With the formal sector unable to absorb new job entrants at a rate that would reduce unemployment, new solutions are necessary. From a policy perspective, this requires a more efficient informal sector to accommodate job seekers and provide opportunities, income and experience to participants in the informal sector. Significantly, this will naturally lead to greater formalisation over time, provided the process is structured as a natural progression of SMME development.

Table 2: The size of the informal economy (as a % of GDP) in South Africa and Nigeria[46]

Year	2011	2016	2017	2020	2025 (forecast)	Period Average (2011–2025)
South Africa	23,49	21,29	23,33	23,71	24,19	23,59
Nigeria	50,73	48,37	47,70	46,99	46,11	47,93
Global	23,10	22,66	22,50	22,11	21,39	22,35

***Source**: Etim, E. & Daramola, O. 2020, The Informal Sector and Economic Growth of South Africa and Nigeria: A Comparative Systematic Review*

It is also evident that informality as a per cent of GDP is declining globally, albeit at a slow rate. South Africa, however, is bucking this trend due to the earlier mentioned factors.

3.3 Relative importance of the informal sector in South Africa

Due to its nature, the accurate assessment of the number and size of informal enterprises is difficult to determine. This is best undertaken through regular surveys with a sound statistical basis. According to the FinScope South Africa MSME 2020 survey[47,48], the SMME sector is constituted as depicted in Table 3.

Table 3 Number of enterprises

	Number of enterprises	% of enterprises
Total	3,139,310	
Formal	1,078,209	34%
Informal	2,061,100	66%

As a comparison, the Department of Small Business Development (DSBD) estimated micro and informal businesses at 3,3 million in 2020[49]. Seda estimated that, of the more than 2,6 million SMMEs that existed during the first quarter of

[46] Etim, E. & Daramola, O. 2020,

[47] The 2020 FinScope MSME survey is based on a national representative sample size of about 5000 small business owners aged 16 years or older, at business premises, in public spaces and at household level.

[48] FinMark Trust MSME FinScope survey 2020

[49] UNDP & DSBD 2021

2020, 66.9% (1,748,031) were categorised as informal[50]. The figures are not strictly comparable but are similar and provide a useful basis for planning purposes.

It should be noted that informal enterprises are not homogenous regarding their business structure. According to the FinScope survey, some 5% of informal enterprises operate in a similar fashion to formal enterprises, while the rest of the informal SMMEs have various levels of formality.

In terms of employment[51] in the informal sector, the FinScope MSME survey provides the estimates shown in Table 4 below.

Table 4: Number of employees

	Number of people employed	Percentage
Formal SMMEs	9,128,391	
Full-time	7,778,729	85%
Part-time	1,349,662	15%
Informal SMMEs	5,336,496	
Full-time	4,533,778	85%
Part-time	802,718	15%

The issue of employment creation presents an interesting picture. According to the FinScope MSME survey, 95,8% of informal enterprises (or approximately 1,980,370 enterprises) are micro-enterprises. The majority of these are single-person businesses, although the sector employs 5,336,496 people, of which 4,533,778 are full-time employees. This implies that a minority of informal enterprises offer significant multi-employee opportunities. Fourie[52] observed and interrogated this phenomenon and noted that 'employing' firms can be found in all sectors. For example, these businesses employ more people than those in the formal mining sector, and the propensity to employ is increasing. Less than 7% of the informal sector is made up of self-employed workers who also employ other people in their informal enterprises. These are the enterprises that are likely to continue to provide employment opportunities[53]. It should still be noted that income derived from working in the informal sector is, on average, lower than that derived from formal employment – R 2,757 versus R 3,973 per month[54].

Statistics from Stats SA Quarterly Labour Force Survey (QLFS) estimate that in 2023, approximately 3 million people were employed in the informal sector. This was a significant growth of 31.5% between 2013 and 2023, with a large dip during the Covid-19 pandemic (Chart 6). The economic lockdown and restrictions imposed due to Covid-19 likely had a detrimental impact on employment within the informal sector. The effects of the lockdown were disproportionately felt in the informal sector, leading to a decrease in the number of employed people. For instance, the restriction of

[50] Schirmer, S, and Visser, R. 2021,

[51] The FinScope survey defines employment according to the number of people working in the sector i.e., every business owner plus every employee that earns an income from an informal enterprise on a full-time, part-time or seasonal basis.

[52] Burger P; Fourie F 2019

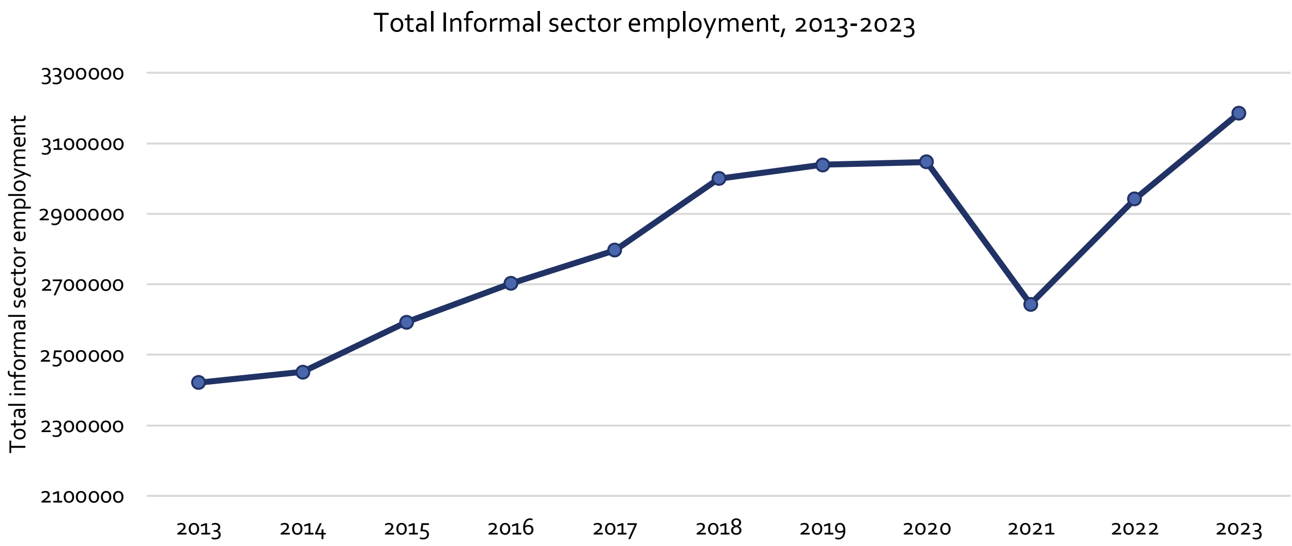
[53] ACCA 2017

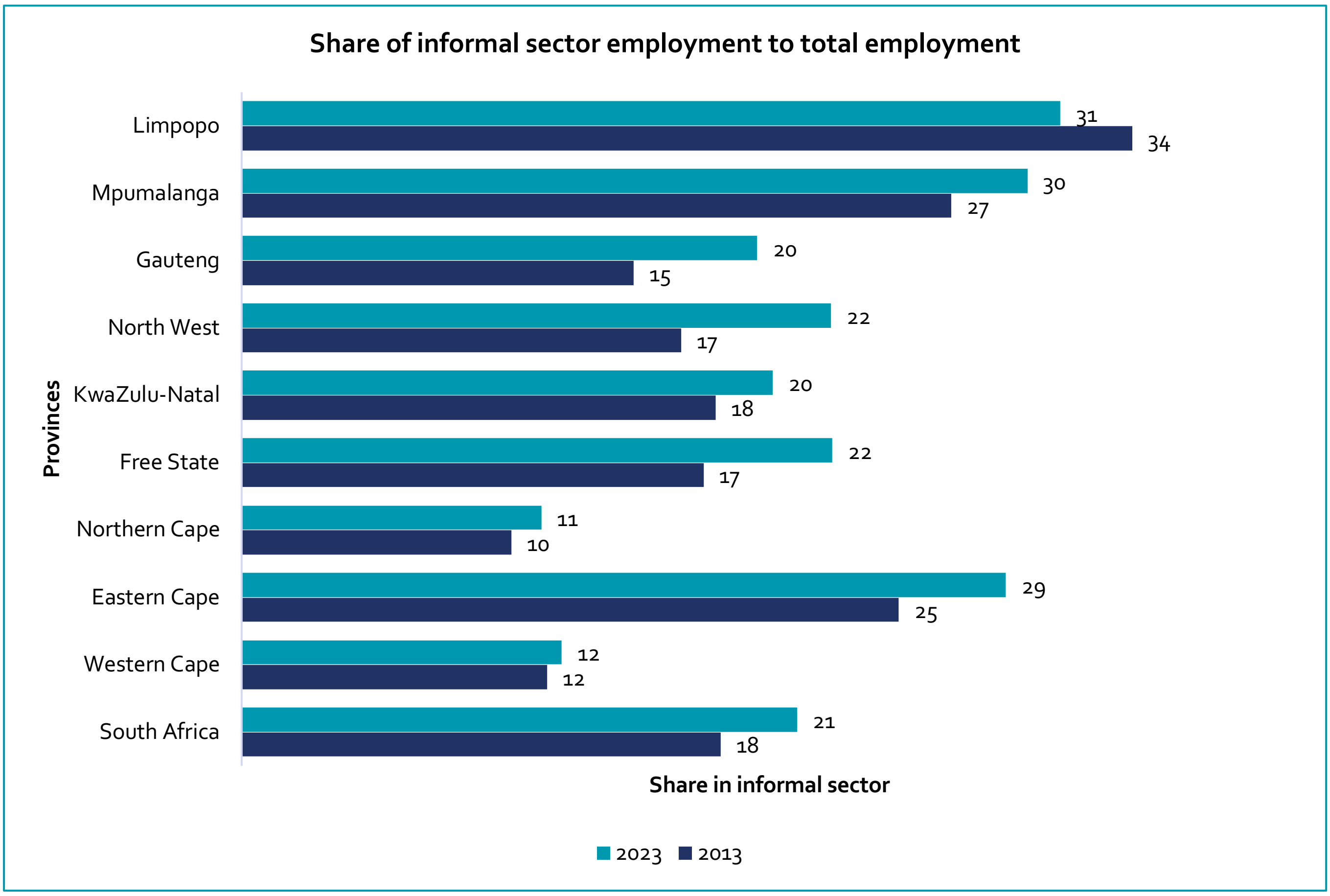
[54] FinScope 2022 survey results

movement during the pandemic's peak limited and, in some cases, eliminated market opportunities for informal enterprises that relied on physical presence for people to purchase products or use their services.

Chart 6 also demonstrates that the informal sector provides 21% of total employment in South Africa, its contribution being highest in Limpopo (31%) and Mpumalanga (30%) and lowest in the Northern Cape (11%).

Chart 6: Contribution of informal sector employment to total employment





More than 20 years of making financial markets work for the poor

Source: QLFS Survey and World Bank Research 2024

It is useful to distinguish between enterprises that are run entirely by the owner and enterprises that employ at least one employee. This is an important distinction to make, given that the challenges faced by these enterprises differ, as do their size, scope and reasons for being established. The FinScope MSME survey estimates that of the total 3.1 million formal and informal enterprises, 809,000 enterprises are owner-operated and, therefore, have no employees, and 1.9 million enterprises employ between one and 10 employees. A breakdown of these enterprises according to gender is shown in Table 5 below.

Table 5: Breakdown of SMMEs by number of employees, disaggregated by gender

Gender	No employees	1-10 employees	More than 10 employees	Total
Male owned	403,268	1,012,003	227,940	1,643,211
Female owned	405,648	920,776	169,674	1,496,098

Of the 809,000 enterprises that have no employees, 663,935 (82%) are informal and survivalist in nature. A majority of these operate by reselling goods in the same form that they bought them from someone else (61%). They were established less than five years ago and started because the owners could not find a job or were retrenched (65%). Many operate from residential premises or the streets.

Although not reporting earnings, the informal sector is estimated to contribute 6% to the GDP through the payment of VAT on goods and services[55].

3.4 Structure and attributes of the informal sector in South Africa

Sectoral and age attributes

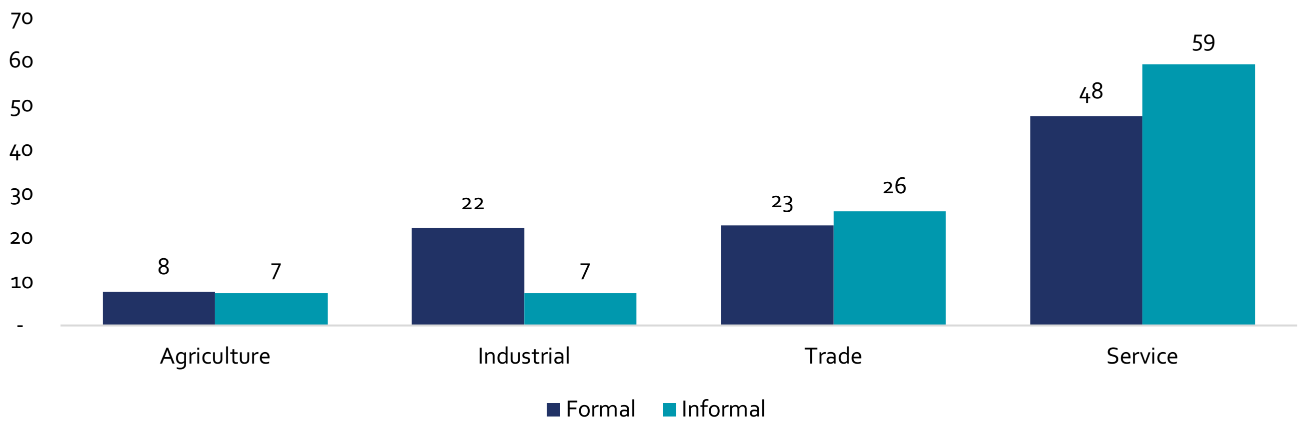
The informal sector contributes to all the main sectors of the South African economy, but there are differences between the formal and informal sectors in terms of sectoral disaggregation. Traditionally, trade (wholesale and retail) dominated the informal sector. According to the latest available data from Statistics South Africa (Stats SA), in 2017, approximately 51,5% of people operating businesses without VAT registration were involved in trade. This percentage has been declining steadily from an estimated 69,6% in 2001. In rural areas, informal-sector agriculture is a key component[56] with an estimated 400,000 to 500,000 people engaged in this sector.

The FinScope MSME 2020 survey presents the following sectoral distribution for formal and informal businesses in South Africa.

[55] Burger P; Fourie F 2019

[56] Burger P; Fourie F 2019

Chart 7 Sectoral distribution of SMMEs in South Africa – % of SMMEs



Considering the spread of informal enterprises across sectors, support programmes could benefit from a sector-based approach that takes into account the varying needs of enterprises based on their sectors.

As mentioned previously, the informal sector is diverse in many aspects. This is also evident in the number of years in business, which indicates business sustainability. Table 6 below depicts the lifespan distribution of all informal enterprises, as estimated in the FinScope MSME survey and categorised by enterprise size.

Table 6: Lifespan distribution of informal enterprises

	Micro (0-10)	Small (11-50)	Medium (51-250)
Less than a year	10,90%	2,90%	0,30%
1 to 2 years	24,60%	8,30%	6,30%
3 to 5 years	34,10%	29,30%	18%
6 to 10 years	16,10%	24,50%	33,70%
More than 10 years	13,30%	34,50%	41,40%

This distribution seems natural, with an increase in time in business as the business size increases.

Organised groups and associations among informal SMMEs

Globally, a number of suggested policy interventions to support the informal sector have raised the potential of groups or clusters to increase the ability to effectively deal with and support members. The FinScope MSME 2020 survey explored the extent to which informal enterprises are currently part of any grouping and revealed a high level of non-involvement in such associations.

Table 7: Incidence of informal enterprise belonging to a group (%)

Type of organised group	Per cent belonging
Labour movement	1%
Women's group	4%
Business organisation	1%
Networking group	1%
Religious group	3%
None	90%

Most informal enterprises do not belong to a group, but this reality does not diminish the potential of forming clusters and groups. However, it does emphasise the need for significant interaction to establish them successfully.

3.5 Vulnerable groups within the informal sector

Gender and youth perspectives

As mentioned above, youth unemployment in South Africa is a growing challenge. The informal sector's role in creating employment opportunities for unemployed young people is continually emphasised in strategy documents such as the National Development Plan (NDP), which envisions that 2.1 million more informal sector jobs will be created by 2030. Youth entrepreneurship is prevalent in the informal sector, as shown in Table 8 below. This indicates the potential to increase youth unemployment through the informal sector.

Table 8: Age breakdown of SMME owners[57]

	Formal	Informal
Total number of owners	959,528	1,656,223
Youth (15-35)	28%	43%
Senior (35+)	72%	57%

The informal sector also provides opportunities for unemployed women, who often consider self-employment a means of supplementing the monthly grants they receive from the government. Table 9 below displays the gender distribution of formal and informal enterprise owners.

[57] FinScope MSME Survey 2020

Table 9: Gender distribution of SMME owners[58]

	Formal	Informal
Total number of owners	959,528	1,656,223
Male	63%	48%
Female	37%	52%

The positive contributions of young people and women as business owners in the informal sector, as depicted above, suggest that further inclusion of these groups is necessary with better support.

A gender-disaggregated perspective on full-time and part-time employment within informal enterprises is summarised in Table 10 below. The informal sector employs a disproportionately higher number of males than females.

Table 10: Gender distribution of employees within informal enterprises

Type	Total workers – Full-time paid	Total workers – Part-time paid	Total paid
Employees in informal SMMEs	4,533,778	802,718	5,336,496
Male	2,936,545	515,916	3,452,461
Female	1,600,108	287,236	1,887,344

Nevertheless, further analysis shows that the percentage of male employees is similar in both the formal and informal sectors, despite the higher percentage of women-owned informal enterprises.

Migrants as SMME owners

South Africa is the migration destination of choice for a growing number of migrants from various African countries, particularly from other SADC countries and an increasing number from the Horn of Africa. Stats SA estimated the total population of foreign-born people residing in South Africa during mid-2021 at 3,95 million[59]. Due to the barriers to entry into formal employment as a result of the labour legislation in South Africa, migrants are more likely to be informally employed compared to South Africans. Stats SA reported in 2017 that 39% of migrants are working in the informal sector. Evidence from a study conducted in Johannesburg (South Africa's largest city) estimates that two out of 10 informal traders are not South Africans[60]. There are misconceptions about informal migrant enterprises, such as squeezing out locals and 'stealing' their jobs; engaging in or promoting illegal activities; provoking locals into acts of violence and looting[61]. These have, therefore, been the object of hostility and exclusionary policies in the country. However, their role in the informal economy cannot be overlooked. These enterprises create employment opportunities, especially for fellow migrant workers and contribute towards the growth of township and rural economies.

[58] Ibid

[59] Statistics South Africa 2021, *Media release: Erroneous reporting of undocumented migrants in South Africa*.)

[60] International Organisation for Migration (IOM) 2021,

[61] See for example: Foreign-Owned Shops: A Vital Cog in Township Economies, South African Catholic Bishops' conference, Dec 2020. https://www.cplo.org.za/wp-content/uploads/2020/12/BP-514-Foreigners-and-township-economies.pdf

4. Policy approach

4.1 Policy, legal and regulatory frameworks relevant to the informal sector

Several legal and regulatory frameworks have influenced the current informal sector landscape. The main drive and underlying assumptions have been to promote greater formalisation, especially through central business registration at the CIPC and tax registration at the South African Revenue Service (SARS). Annexure A includes a list of the legal and regulatory frameworks directly relevant to the informal sector, along with brief descriptions of the goals of each framework. There is currently a shift towards acknowledging the informal sector as a permanent and vital component of the national economy, especially within the DSBD. This framework seeks to continue and strengthen this shift, enabling the future alignment and harmonisation of the various policies and frameworks.

The following key strategies and policies, which are further elaborated on in annexure A, are the core pillars of support for the informal sector:

- The National Informal Business Upliftment Strategy (NIBUS) outlines an implementation plan for supporting the informal sector
- National Integrated Small Enterprise Development Masterplan focuses on an integrated approach across all spheres of government and other stakeholders in advancing small enterprises – formal or informal, and co-operatives
- The SMMEs and Cooperatives Funding Policy provides a framework for strengthening the provision of development finance for SMMEs and co-operatives
- The SMME Access to Finance Action Plan aims to promote greater levels of formalisation and greater access to finance for SMMEs
- The National Financial Inclusion Policy seeks to promote improved and sustainable access to and the use of appropriate and affordable financial services for individuals and SMMEs.

The strategies, policies and interventions by entities in the financial sector have also been crucial in directing the evolution of, and support for the informal sector. The South African Reserve Bank's National Payment System Department (NPSD) Vision 2025[62] as an example, aims to deepen financial inclusion, while an IFWG[63] has been established to facilitate innovation with the potential to impact underserved groups such as those in the informal sector. The National Treasury has recently approved a national financial inclusion policy, further reinforcing these efforts. In addition to this, policies and regulations issued by the FSCA, the National Credit Regulator (NCR), the Financial Intelligence Centre Act (FICA), and the Department of Home Affairs all have significant impact on the informal sector. None of these institutions, however, has a specific mandate for the informal sector.

4.2 Priority 1: Issue a stand-alone policy statement from the Office of the Presidency that articulates a policy approach that prioritises informal businesses.

The analysis in Section 4.1 highlights that the informal SMME sector is addressed through a myriad of disparate policies that lack a central guiding policy direction. This contrasts with the ILO's recommendation for an integrated approach that takes into account the role of different levels of government or the unified approach propagated by the government of Ecuador (refer to Section 2.5 for details). This means the informal sector, to a large extent, operates in a policy

[62] SARB National Payment Systems Department 2018

[63] www.ifwg.co.za

vacuum, except for the drive to formalise, which must be addressed. Formalisation should not be excluded, but a realistic assessment of how many enterprises could and should formalise will, in all likelihood, reveal that it is a relatively small percentage per annum. Even for those enterprises, it is essential that there is a compelling reason to formalise[64]. As mentioned in the introduction, a more impactful approach is to articulate a policy approach that, in addition to promoting formalisation, also recognises and prioritises support for informal enterprises across government and in society.

Such a national, government-wide approach requires a stand-alone policy statement that can be used to guide and align the actions of all government entities and all other actors in the informal ecosystem. It would be most beneficial for this policy statement to come from the Office of the Presidency so that it has weight and emphasis is made on the fact that it impacts various government departments. The policy statement does not necessarily need to be supported by an Act, although that may be considered.

The policy statement should recognise the importance of the informal sector as a key contributor to South Africa's economy and call for the support of informal businesses across all government departments and agencies. Informal enterprises should be positioned as drivers of economic growth and job creation in the country. This policy statement should also call for the establishment of a segmented approach to supporting the informal sector, noting the sector's diverse nature. To prepare for the policy reform process, an assessment of the impact of existing SMME measures and programmes impacting the informal sector to date should be funded and carried out.

Beyond the policy intent, it is important that the presidential statement also provides practical direction on how the key proposals in this framework should be implemented, particularly the institutional setup for implementing these reforms. This may include the details for the coordination mechanism with DSBD and National Treasury mandated to lead the process, expected outcomes at the highest level, the reporting framework, resource allocation, and timeframes. The presidency will be part of the ongoing coordination mechanism.

The message needs to be carefully crafted to avoid the Presidency implicitly supporting enterprises that are breaking the law (by not registering or paying taxes). The statement should emphasise the prevalence of informal institutions and the desire to work together to ensure their support for national development objectives.

Summary of recommendations:

- Put out a stand-alone policy statement from the Office of the Presidency that articulates a policy approach prioritising informal businesses.

4.3 Priority 2: Determine a segmented approach for the informal sector to allow for the extension of market support services and initiatives.

As mentioned in Chapters 2 and 3, the South African informal sector mirrors the global sector in the diversity of the types of enterprises present. The need for targeted approaches towards informal sector interventions was highlighted as a means of responding to the different attributes and requirements of informal SMMEs. This ranges across attributes like business maturity, the size of the business, the characteristics of the business owners, entrepreneurial skills and attitude, the reasons behind the establishment of the business and the desire to grow or develop the business.

This diversity calls for a **segmented approach** to be strengthened in the local context, where there would be sufficient homogeneity in certain attributes within the segments to pursue a set of policies and strategies for each segment,

[64] See for example SBI 2021, page 26

without unnecessarily mispresenting the aspirations of some enterprises in the process. Given the wide diversity in the sector, such segmentation could become quite complex. However, from a practical perspective and in an attempt to achieve broad market acceptance, it needs to be simple enough to enable non-intrusive[65] implementation.

There are multiple ways in which such segmentation can be done. Three or possibly four segments are suggested for consideration and further elaboration[66]:

- A **basic segment** (Segment 1) consisting primarily of survivalist businesses with a turnover of less than R100,000 annually. These are typically single-owner enterprises with little evidence of a desire to expand the business significantly but primarily support the owner's household, with a market focus rooted in the community in which they operate.
- An **emerging segment** (Segment 2) with a turnover of between R100,000 and R300,000 annually. This segment represents informal businesses with the potential to grow if adequate support is provided. Employment may have either taken place or is likely to take place, and the enterprise may have an interest beyond the community in which it operates, either through directly serving further afield or by arrangements with other enterprises.
- An **established informal business segment** (Segment 3) representing businesses with a turnover of more than R300,000 annually. The viability of these businesses has largely been proven, and the enterprise may already, or largely, be operating in a manner similar to formalised enterprises. This segment may also include potential high-growth start-ups, including those without direct employees.
- Consideration could, but need not, be given to an **agricultural segment** (Segment 4). The operating realities and aspects of the required support for these enterprises may be quite different from other enterprises. Subsistence farming should probably be viewed separately.

It is not possible to provide the exact percentages here, but it is estimated that the breakdown of the number of enterprises will be in the order of 60:30:5:5 across the four segments, based on FinScope estimates. It is anticipated that support structures will be established specific to each segment, with specific 'registration' guidelines per segment. Enterprises should be allowed a degree of self-selection and movement between segments.

Summary of recommendations:

- Determine and roll out a segmented approach.

5. Business Identification, Registration and Onboarding

5.1 Business identification registration and onboarding landscape and challenges

Registering a business in South Africa

For an enterprise to be considered as formal, the owner(s) should register their business as a sole proprietorship, partnership, proprietary limited company or public company. The registration process is governed by the Companies Act of 2008 and the Companies Regulations of 2011. The following documentation is required to register a company:

[65] Non-obtrusive in this context refers to implementation that does not require the business owners to adjust their business or business model, but rather that allow them to select the segmentation that is most appropriate.

[66] The National Small Business Act, 1996 (as amended) [[previously Business] Act 102 of 1996] categorises SMMEs by size (micro, very small, small, and medium) depending on sector. in most sectors "micro" is defined as enterprises with turnover below R200,000, while "very small" ranges from R200,000 – R1 million in some sectors and much higher in others. This effectively categorises most informal SMMEs as "micro" or "very small".

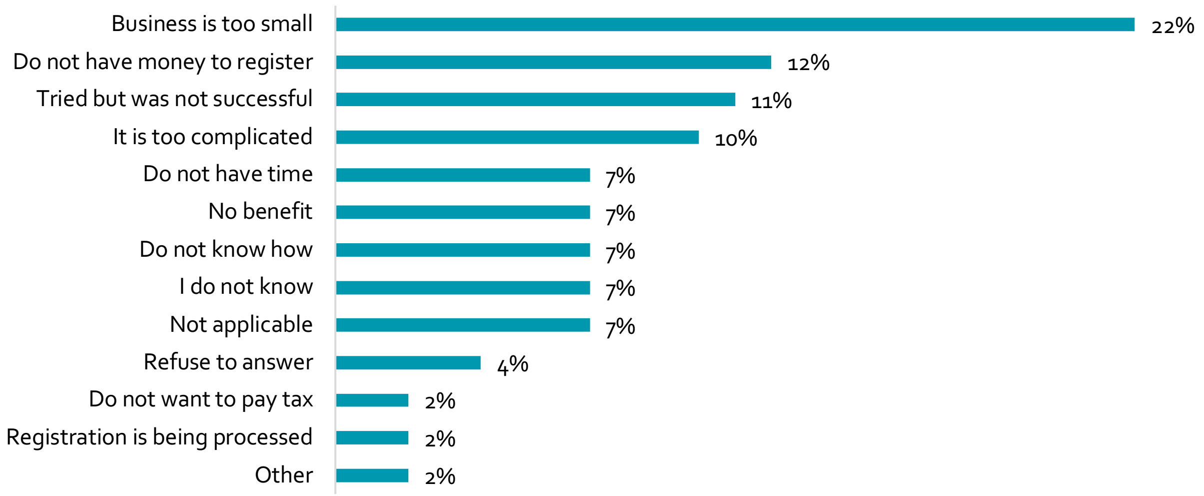
- Notice of incorporation which includes the type of company, incorporation date, financial year-end, company name, director numbers and registered address
- Memorandum of incorporation, which includes the founder's details, the amount of share capital, and the number of directors
- Administrative documents available from the Companies and Intellectual Properties Commission (CIPC) website
- Certified copies of the owner's identity document (ID) and those of the initial directors and incorporators
- The valid reservation document for the business name, if one has already been reserved
- Fees for the registration (between R125 and R475).

The business registration process in South Africa is seen as onerous due to the associated cost of registration, which is high for some smaller enterprises, as well as the perception that registering a business automatically leads to taxation. For these reasons, informal enterprise owners often do not see the benefit of registering their businesses.

Challenges to business formalisation

A deeper understanding of why informal business owners choose to remain informal is important since it puts into context the issue of business registration from the perspective of the informal SMMEs. The FinScope MSME survey 2020 lists a number of reasons, as highlighted in Chart 8 below, ranked from the highest to the lowest percentage.

Chart 8: Reasons for remaining informal

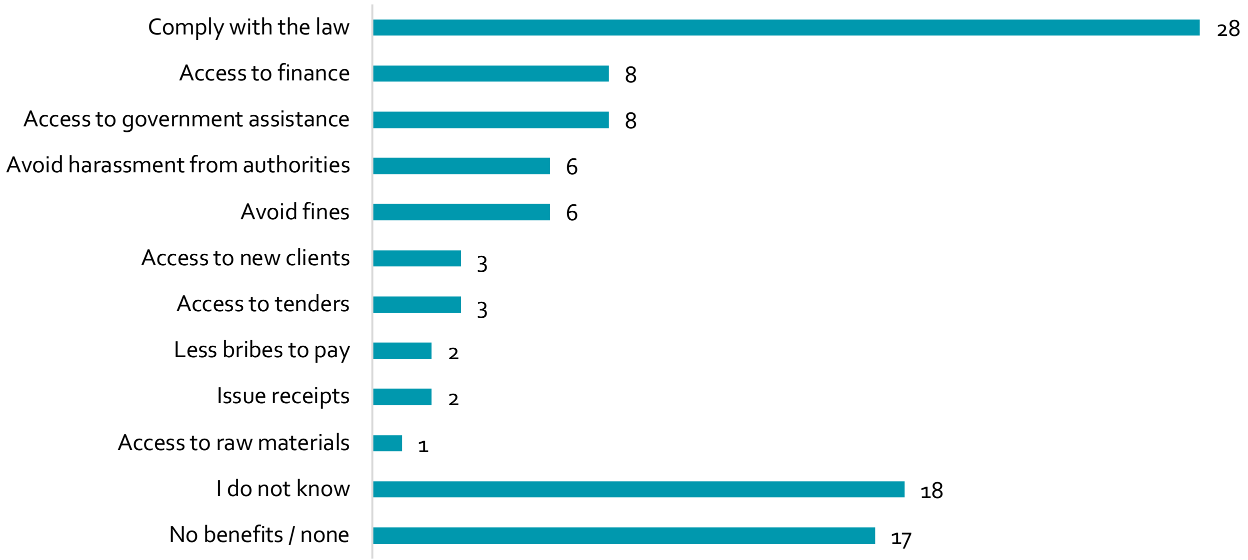


The FinScope findings point to a lack of knowledge and awareness about the process and its benefits, and a perception of high costs and complexity in formalising. There was no significant difference between women and men or between youth and people over the age of 35 in the responses above. Other evidence suggests that entrepreneurs put forward five general reasons for operating informally: avoiding public authorities, greater flexibility, family management, minimising risk, and the lack of incentive for undergoing the process of formalisation[67]Error! Bookmark not defined..

[67] Investisseurs & Partenaires, 2019, Formalising SMEs in Sub-Saharan Africa

In general, it seems that informal business owners do not view formalisation as something desirable or necessary to comply with. This perspective is somewhat mitigated when considering how informal business owners view formal businesses.

Chart 9: Benefits of a registered business – as viewed by informal business owners (%)



A reasonable percentage of the informal businesses referred to some of the business benefits associated with being formal, including access to finance and government assistance. However, most either do not know the benefits of formalisation or simply see formalisation as a compliance function or means to mitigate some of the prevalent negative attitudes towards informal businesses.

Registering a business is the first step towards formalisation. Making this process as efficient and user-friendly as possible is, therefore, a major consideration. The complexities of the business registration process, especially for start-ups and informal enterprises wanting to register, can be daunting. These difficulties are often quoted as one of the reasons why enterprises do not formalise. In South Africa, 9% of informal business owners quote this as the case. It is possible that the owners experiencing these difficulties are largely those who would like to register, meaning that many enterprises that are in a position to formalise are discouraged by the registration process.

Some countries have been addressing the issue of streamlining and simplifying the registration process in a variety of ways. Such efforts have included restructuring the business registration and related processes into a single, simplified interaction. In some instances, the tax system has also been simplified to the extent that enterprises only have to make a single payment for all taxes (see Section 8.1).

In South Africa, the company registration process has been digitised by the CIPC, with significant time savings for those who want to register. However, the time and cost to register a business in South Africa takes longer than most countries – and ranks 136th out of 190 countries on the ease of starting a business in the erstwhile World Bank's Doing Business index[68]. The South African average business registration process takes 45 days, compared to the sub-Saharan average of 22 days. The process also involves four different departments and agencies, with seven different procedures used. Although the total cost is not high for larger SMMEs (a few hundred rand), the lengthy and disjointed process is a constraint for those SMMEs wanting to formalise[69]. This is further compounded by the different types of taxes to be paid (Section 8.1), sector-specific requirements and the additional requirement of local (municipal) registration[70].

[68] Now discontinued, with archives available at: https://archive.doingbusiness.org/en/doingbusiness

[69] IFC 2018

[70] Obtaining a business license in Johannesburg, for example, requires an inspection and approval from five Government departments – IFC 2018

In addition, there is a need to reregister a business at the local authorities if the business changes or adds to its scope of operations. If the existing registration is not amended, the process starts from scratch[71]. Zoning requirements are set at the local level, and any changes to such zoning regulations must be adhered to. Local compliance is administered by metro police officials or local police, and business owners have mentioned this as an additional challenge.

Informal enterprise owners can register their businesses with municipal authorities to obtain permission to operate in a specific area provided for by the municipality. This registration is not linked to the CIPC database and does not change the legal status of informal enterprises.

5.2 Priority 3: Implement a pre-registration identification system for all informal enterprises on a voluntary basis and delinked from tax and labour law requirements.

Unique business identifiers have now been successfully rolled out in a number of jurisdictions to facilitate the provision of services and sharing of information[72]. The identifiers are typically used across both the public and private sectors, as well as in legal and financial documents, to uniquely identify the entities involved. Legislative reform is often required, particularly to allow the creation of the dedicated register and a new public entity to run it (if required), as well as to facilitate the collection, use, and sharing of information. Among others, the Philippines Business Number (PBN), administered by the Philippines Business Registry (PBR), was introduced in 2010 and has been issued to 1.5 million sole proprietors[73]. Similarly, Rwanda introduced a unique business identifier in 2010, based on the tax identification number (TIN).

While these examples are targeted at formal SMMEs, a few jurisdictions have gone further in an attempt to accommodate informal businesses. In July 2020, the Indian Government launched the Udyam registration portal to simplify registration of SMMEs. The free, online process is based on self-declaration, and upon registration, the business receives a permanent identification number and a registration certificate[74]. To respond to the large number of informal micro-enterprises that are not registered for tax, the complementary Udyam Assist Platform[75] was launched in January 2023. The platform issues a Udyam Assist Certificate which enables informal sector SMMEs to access markets, financial services, and government schemes[76]. Support is also provided by designated (accredited) financial service providers (FSPs) to transition SMMEs on the Udyam Assist platform onto the Udyam registration portal. So far, the platform statistics show that the Udyam Assist platform has onboarded over 22 million informal SMMEs.

Lesotho is another jurisdiction envisaging an informal SMME database[77]. Recognising that a majority of businesses are informal and that there is limited data on them, the Lesotho Business Licensing and Registration Act of 2019 mandated the registration of informal businesses with the Ministry of Trade, which will enable increased access to business support and disaster relief mechanisms.

A large proportion of SMMEs in South Africa are similarly informal, as discussed in Chapter 3. Section 5.1 addressed the impediments to formal registration. By definition, informal enterprises are not registered, meaning that, to a large extent, a unique identification does not exist. While some agencies, such as the DSBD, provide a database that can enable access to their services, this is not an ID system that can be used systematically. This hinders access to business

[71] As informed by officials from the City of Tshwane in June 2023

[72] World Bank. 2016.

[73] World Bank. 2016.

[74] ILO 2021

[75] https://www.sidbi.in/udyam-assist-platform

[76] Small Industries Development Bank of India (SIDBI), 2023, Annual Report 2022-23

[77] Kingdom of Lesotho Ministry of Finance and Development Planning, National Financial Inclusion Strategy 2024 – 2028, 2024 (forthcoming)

services, as the only form of identification, if available, would be the personal identification of the owner. As with other initiatives, an integrated approach is necessary, recognising that informal enterprises are unlikely to participate in 'full registration' for identification purposes due to the same reasons they avoid formalisation. Simplified, intermediate or temporary statuses offer a way to overcome this dilemma[78].

It is proposed that a **'pre-registration' identity system** is created for all informal enterprises on a voluntary basis to provide a unique business identifier for informal SMMEs, and to function as a first step to promoting the inclusion of informal businesses in formal and crisis support processes. Such a system could be used to identify enterprises, in the same way that individual IDs are used. This would be useful in access to finance, including grant funding, and in tracking the enterprise consumption that the DSBD would like to establish. It could also serve as the first step of such an undertaking.

Currently, the owner or manager of an enterprise typically acts as the proxy for the informal enterprise. The official recognition of the enterprise as a juristic person begins only when registration details are available and the business structure is known. At this point, access to financial services, support services and access to markets and market initiatives, like supply-chain development, can commence. The intention of the pre-registration process, supported by the segmented approach, is to provide market support and participation to a larger number of enterprises without imposing a one-size-fits-all structure on all informal enterprises, especially in instances where it is not necessary.

The pre-registration system should be designed in a way that serves as the first step towards formalisation if the enterprise chooses this path. It should be acknowledged that some enterprises may remain 'informal' indefinitely. Although certain segments may generate some contributions to state revenue (see Table 11 below), this initial business ID should not imply registration with SARS or the Department of Labour and Employment. It is suggested that the administration of the ID be jointly handled by the DSBD and CIPC, keeping the process as simple as possible. For example, it could include a business name, the ID of the owner(s), the segment category as proposed in Section 4.3 above, the business sector, contact details (and an address if absolutely necessary), as well as the number of employees. A pragmatic starting point for establishing this could be the current registration details at the municipal or local level.

In establishing the pre-registration system, globally emerging approaches should also be assessed to ensure that the new system benefits from innovations elsewhere while remaining relevant locally. One such approach is to use a decentralised business identifier for informal businesses[79], for which a working group under the World Wide Web Consortium (W3C) is developing the Decentralized Identifiers (DIDs) standard. Emerging technologies like these can help make information more secure in light of data privacy and cybersecurity concerns, streamline interactions between businesses and the government, and eliminate the need for physical presence and the use of paper documents.

While pre-registration is entirely voluntary, informal SMMEs can benefit from it by acquiring a formal identity, which allows them to access the formal sector. The broader economy also benefits; firstly, by encouraging the move towards formalisation; secondly, by being in a position to provide certain support to the businesses in aid of job creation; and lastly, by collecting information on an important sector that is currently largely invisible.

Tax and labour law requirements should continue to be managed by the relevant authorities independently of the database. The determination of whether tax is due will rely on the various parameters outlined in the tax code, which should be as updated to align with the proposals in this framework. This determination will not depend on pre-registration status or classification within the pre-registration database. The tax updates should be designed to exempt most SMMEs in the 'basic segment' from taxation while imposing a nominal tax on most of those in the emerging segment. The combined proposed recommendations under the segmentation model (Section 4.3), legal framework

[78] Klapper, L. *et al* 2019

[79] Vranic G and Marusic A., 2021.

(Section 5.4) and tax (Section 8.2) should be implemented so that pre-registered informal businesses are treated as follows:

Table 11: Proposed implications of a pre-registration system on business status

Segment	Legal status	Access to finance	Access to BDS	Access to 'formal' markets	Cost/tax
	Status quo	Limited – as is	Limited – as is	Limited – as is	Nil
	New legal status as an informal enterprise	All basic financial services required for a business	Full access Focus on financial management and sustainability	Improved – dependent on business maturity	Nil
	Status quo	Limited – as is	Limited – as is	Limited – as is	Nil
	New legal status as an informal enterprise	All basic financial services required for a business	Full access Focus on financial management, growth and employment	Improved – full access as per formal enterprises but dependent on business maturity	Fixed amount covering all statutory costs
	New status – 'pre-formal'	Unlimited – as for formal	Full access	Improved – full access	Single payment but with VAT and UIF calculated on realised figures
	Status quo	Limited – as is	Limited – as is	Limited – as is	Nil
	New legal status as an informal enterprise	All basic financial services required for a business	Full access Focus on financial management, growth, employment and agri-specific services	Improved – full access as per formal enterprises but dependent on business maturity	Single payment, but with VAT and UIF calculated on realised figures

The following key points should be noted with regard to the segmentation model proposed above:

- The enterprise identity scheme is aimed at Segments 2 and 3 (and Segment 4, if it materialises). It will need to remain voluntary and should not exclude Segment 1, in order to encourage the more viable enterprises to consider formalising. If the ID process is coupled with 'local' registration, the processes can be integrated.
- Enterprises without an ID will largely remain in the same situation as they are currently. It is anticipated that Segment 3 enterprises will register.
- 'Access to markets' in this table refers to state procurement and formal supply chains.

Summary of recommendations:

- Implement a pre-registration identification system for all informal enterprises on a voluntary basis and without linkage to tax implications.

5.3 Priority 4: Reshape SMME registration and licensing process to be more integrated and streamlined

It is important for any informal sector policy support to consider the needs of SMMEs across the lifecycle. While less developed SMME segments (the majority of Segments 1 and 2) will benefit from increased business support to build their productivity (e.g. digitalisation to reach their customers), some of the more advanced informal SMMEs in Segments 2 and 3 will need to formalise to continue growing their operations, despite the higher costs associated with formality. These more advanced SMMEs should, therefore, in addition to other support, be enabled to transition from informal to formal status as part of their natural evolution, where this becomes useful[80]. The increased awareness about formalisation and a streamlined process for formalisation are crucial aspects of the policy support mechanism.

Many countries provide an online portal or facility for company registration. In Estonia, an e-residency service is offered, which allows individuals to establish and manage companies online from anywhere in the world. The registration process can be completed entirely online and usually takes only a few hours. There are several other instances of the use of digital onboarding in the registration process. In Guatemala, business registration increased by 40% after the introduction of e-registration. Similar reforms in Jordan and Sri Lanka had modest positive impacts on new business registrations[81].

Progressive company registration domains should involve fully automated real-time company registration, integrated company registry data, and emerging technologies for predictive analytics and fraud prevention[82]. The latter is crucial as the simplification of company registration and the elimination of in-person interactions require improvement in fraud prevention and detection. The World Bank further recommends the following key regulatory policies to be considered for a modern data-driven company registry[83].

	Key policies	Description
1.	Mandated interoperability and data sharing between involved stakeholders	Data quality relies on data sharing between involved stakeholders in the company registration procedure
2.	Authorise a single authority for initiating, processing, and completing the company registration	A single authority should be designated as the single point of contact, responsible for deciding on the company registration and managing the integrated company register.
3.	Unify payments of administrative fees into one centralised payment	A single authority should be designated to receive a single digital and integrated payment for the company registration.
4.	Define minimum data requirements for the company register	All input and shared data in a company register must be clearly defined, including mandatory and optional input data.
5.	Allow free public access to company register data	The company register data should be published online and allow free searching or browsing of individual company data.
6.	Simplify requirements for articles of incorporation	Articles of incorporation can be standardised by defining the minimum content that will allow automated validation of data entries and avoid any attachments to applications for initial company registration or registration of changes.
7.	Establish an easy but secure framework for a digital ID	Lowering the requirements for digital signature and defining a single sign-on digital ID facilitates public access to the online services of a company registry.
8.	Implement a unique business identifier	A unique business identifier should be assigned at the initial company registration and shared across the

[80] Levenson and Maloney, The Informal Sector, Firm Dynamics and Institutional Participation, World Bank, 1998

[81] Klapper, L. *et al* 2019

[82] World Bank. 2022. Data-Driven Company Registry: Guidance Note. Equitable Growth, Finance and Institutions Insight; Equitable Growth, Finance and Institutions Insight - Trade, Investment and Competitiveness. © Washington, DC. http://hdl.handle.net/10986/37948 License: CC BY 3.0 IGO."

[83] World Bank 2022. Data driven Company Registry.

		government to facilitate interoperability and business data sharing[84].
9.	Reduce constraints for company naming at registration	Clear rules regarding company names should, in most cases, enable automated name validation without human intervention. Alternatively, simpler rules should be applied, such as the validation of a company name not being a requirement for company registration.
10.	Initiate a mandatory process of public-private dialogue and collaboration	When drafting the Law's revisions and developing digital systems, involve the different actors through public consultations to prevent future opposition to the changes.

These principles align with international best practice on interoperable digital public services, such as the European Interoperability Framework (EIF)[85], ensuring a high quality of public services and collaboration.

The registration process at CIPC has significantly improved over the last few years; however, the overall process is still cumbersome and not on par with international practices. The CIPC's introduction of an online business registration function has eliminated the need for queuing at the commission and the manual capturing of customer information. However, customers still need to have all the necessary documents on hand for automated registration, which requires prior engagement with other agencies. This means the process is not yet fully centralised, acting as a deterrent to formalisation for enterprises that want to formalise, as most in the established informal business segment (Segment 3) will. It is suggested that a fully integrated process be established that includes the following:

- A one-stop process, completely digital, with assistance available if required.
- Links to all appropriate authorities, including local authorities, should be in place. All required business registrations should, therefore, be completed as part of the process, with local support staff involved where necessary for support and/or verification purposes.
- A link to and registration with SARS should be included.
- A link to and registration with the Department of Employment and Labour should be included.
- A link to sector-specific business support services and information on compliance issues applicable to the sector(s) in which the enterprise operates should be provided.
- The registration database should make data immediately available and directly accessible to qualifying entities via a standardised interface. This will enable FSPs to quickly establish business relationships with registering entities.
- The cost of registration should be reduced to zero or near zero, as the benefits of having a fully registered business far outweigh any potential registration revenue.

In addition to streamlining the registration, growing firms are more likely to willingly comply with formalisation (i.e. tax and regulatory) requirements if it increases their access to necessary services and institutions[86]. Such services are wide-ranging but may include governmental programmes such as pensions and healthcare, public risk pooling mechanisms, the legal system, property rights, the banking system, certifications, and trade organisations. Making these and other government services more easily accessible to small businesses within their local geographies and contexts is important to encourage increased compliance. This represents a significant deviation from traditional enforcement-only approaches.

[84] World Bank. 2016. "Implementing a Unique Business Identifier in Government: Guidance Note for Practitioners and Nine Country Case Studies." World Bank, Washington, DC. License: Creative Commons Attribution CC BY 3.0 IGO

[85] European Commission. 2017. The European Interoperability Framework (EIF). Adopted March 2017. Available at https://ec.europa.eu/isa2/eif_en/

[86] Levenson and Maloney, The Informal Sector, Firm Dynamics and Institutional Participation, World Bank, 1998

Compliance requirements should also be streamlined (as suggested in Priorities 1, 5, 6, 7, 10 and 12), to ensure that SMMEs looking to formalise face fewer impediments and barriers to formalisation. Further, a risk-based system in registration, licensing and inspections should be considered. Such an approach can be tailored to avoid imposing an excessive burden on low-risk businesses, while still protecting the public interest in terms of health, safety and the environment through appropriate control of high-risk businesses.

Summary of recommendations:

- Reshape the SMME registration and licensing process to be more integrated and streamlined.

5.4 Priority 5: Update registration, licensing, finance and other laws and regulations to support informal businesses.

To adequately support informal SMMEs, relevant business registration, licensing, tax and financial sector laws and regulations at the national and sub-national levels will need to be reviewed to provide a legal framework for the pre-registration status of informal businesses. The update will focus on identifying informal SMMEs and the utilisation of these identifiers in easing access to services and compliance through risk-based approaches. Many countries have already issued, or are in the process of issuing, unique business identifiers, primarily to expand the tax base. The World Bank[87] describes these efforts through nine case studies, including examples from the Philippines, Rwanda and Jordan. Brazil has a similar scheme, allowing micro-enterprises and own-account workers to 'become visible' without the obligation of paying full taxes[88]. India is exploring the use of such an approach to extend services to informal SMMEs, as discussed in Section 5.2.

Introducing a new business identity system will need to coincide with a review of the current regulatory environment to accommodate the new status of identified businesses within the segments outlined above. In addition, regulations that control access to finance, access to markets and access to business support services will need to be adjusted to accommodate the new cohort of legitimate informal enterprises. Consideration should also be given to ensuring that requirements for informal businesses are reviewed and, where possible, to ease compliance.

Five main areas of reform are envisaged:

- The Companies Act of 2008, the Business Act No.71 of 1991 (including the 1993 amendment) and related regulations should provide a legal framework for the pre-registration status of informal businesses. This would allow informal businesses to operate using the unique business identifier and ease the registration and issuance of municipal licenses and permits.
- Revisit the Financial Sector Regulations Act of 2017 and the National Credit Act to ease the requirements for accessibility of credit and other financial services to the informal sector, and to widen the range of credit information. The review should also include regulations related to financial intermediaries, financial intelligence, and national payment systems to better cater to the needs of the informal SMMEs. In this regard, the Global Partnership for Financial Inclusion (GPFI), a G20 working group, recommends the following[89]:
    - Ensure an integrated identity framework.
    - Adapt and upgrade the regulatory frameworks in the financial sector.
    - Establish a robust and secure digital identity infrastructure in the financial sector.
    - Foster the development of private sector-led services by leveraging legal identity infrastructure.
    - Monitor new developments and approaches to identity.

[87] WB 2016

[88] ILO 2019

[89] Global Partnership for Financial Inclusion 2018

- Reform the Secured Transactions framework to enable the development and use of a modern, simplified registry for movable property. The framework is currently anchored on the dated Security by Means of Movable Property Act 57 of 1993.
- The Protection of Personal Information Act of 2020 to ensure that the pre-registration identification database is used responsibly by entities involved.
- The Tax Income Act of 1962, the Tax Administration Act of 2011, the Labour Relations Act of 1995 and the Basic Conditions of Employment to recognise the unique business identifier and to accommodate and ease compliance requirements for the informal sector.

Further, given the implications of other laws, such as the Immigration Act, which may clash with the business identity system proposed above, it may be necessary to revisit all impacted legislation and regulations. If the business registration system is limited to South African citizens only, a large proportion of informal businesses that are migrant-owned will remain unidentified and unaccounted for.

Implementation practices may also need to be examined on an ongoing basis to avoid instances where the enforcement of regulations and bylaws is interpreted by individual staff rather than the responsible department. This will not only ensure uniformity but also allow for any easing of requirements to be effective across the country.

A summary of the main pieces of legislation that are likely to be impacted by recommendations in this report is included as Annexure E.

Summary of recommendations:

- Update laws and regulations to accommodate informal businesses, particularly laws and regulations on tax, business registration, labour, social security and national payment systems.

6.1 Financial services for informal businesses landscape and challenges

Access to financial services is often cited as a major barrier for enterprises in the informal sector. These enterprises are not considered juristic persons, which is why FSPs traditionally avoid establishing a business relationship with them. In many instances, the enterprise owners have a personal account or use personal financial services; however, this relationship does not recognise the business aspect of the enterprise and is, therefore, limiting.

Access to finance landscape

Selected financial inclusion indicators are displayed in Table 12, (based on the FinScope MSME survey). These reflect a situation that is largely expected, where formal enterprises have a higher level of financial inclusion than informal enterprises. The higher prevalence of cash in the informal sector is evident, as is the noticeably lower uptake of insurance. The latter confirms the view that the insurance product set particularly is insufficiently tailored to and adapted for the informal sector.

Table 12 Levels of financial service usage by SMMEs

	Formal	Informal
Bank account	97	75
- Business account	46	8
- Personal account	50	67
Payments made		
- Cash	48	84
- Digital	57	11
Payments received[90]		
- Cash	81	98
- Digital	58	15
Insurance		
- Business insurance	37	3
- Personal risk insurance (owner)	34	6
Credit		
- From banks	20	7
- From friends/family	5	3
Other sources negligible		

It is worth noting that many informal retailers offer loans to clients to pay for purchases. By doing so, they function as FSPs, albeit informally. More than 50% engage in this practice.

Supply-side challenges

The main constraints faced by FSPs in serving the informal sector were explored in discussions with the Banking Association of South Africa's SME committee and follow-up interviews with both the committee members and with fintech firms operating in the informal enterprise sector. Although the financial services industry generally acknowledges the importance of supporting the informal sector, the current requirements set out by FSPs make it almost impossible for informal enterprise owners to obtain services.

The basic eligibility requirements for a business bank account include proof of the enterprise's registration with the CIPC, valid identification evidence, and verification of a physical address. The enterprise's banking transaction history is also required for access to credit facilities. When proof of registration with the CIPC is unavailable, as is the case for all informal enterprises, banks offer accounts for sole proprietors if the applicant meets all of the aforementioned

[90] These figures should be interpreted in light of the reality that clients of the enterprises may sometimes deal in cash and sometimes digitally. For example, 98% of the clients of informal SMMEs sometimes pay in cash, but 11% sometimes pay digitally.

requirements, except for proof of registration with the CIPC. In this scenario, the enterprise does not qualify as a separate legal entity from the sole proprietor. Three of the four banks engaged offer low-cost business bank accounts, which are subject to the requirements outlined.

Among other methods, all the banks use digital client onboarding. There was a widely held view that products should address needs that are not only limited to the informal sector but that address the needs of a broader customer base. None of the banks showed interest in or engaged with undocumented foreign nationals, citing the Immigration Act as a deterrent. Additionally, none of the banks reported leveraging other support programmes that target the informal sector. There appears to be a lack of industry-led focus within the banking sector to extend the financial infrastructure in a way that caters to the specific needs of informal enterprises. The banks mentioned efforts to promote business education and financial education, especially among potential business banking clients who did not meet the onboarding criteria. However, this education is not explicitly steered toward informal enterprises.

Regarding access to finance and access to credit, some banks mentioned offering lending options based on digital payment turnover. This method is easy and convenient for informal retailers and service providers as repayments are deducted from incoming digital payments. However, given the relatively low usage of digital payments in many communities, this results in small loans suitable only for operational expenses. There is no incidence of sharing such information, which essentially results in closed-loop digital lending products. The banks appear to share implied concerns about the financial and business capacity within the informal market, although some noted that this is less of a concern in certain sectors. The persistence of cash and inadequate support services were common concerns expressed.

Constraints for FSPs when trying to serve informal enterprises can be summarised as follows[91]:

Documentation and identification:

- Lack of proper documentation identifying the business, leading to the owner acting as the proxy for the business at best
- Addresses that change or are hard to use due to the nature of many informal businesses
- Difficulty in verifying information due to the absence of official records
- Uncertainty associated with being an informal enterprise, including changes in ownership, location or ceasing to exist without formal reporting, increases the risk for FSPs.

Financial records and viability:

- Insufficient financial record-keeping making it impossible to assess the financial state and viability of the business
- Insufficient or non-existent business plans, hindering the assessment of the future prospects of an enterprise.

Management and operational skills:

- Insufficient or unproven business and operational management skills, increasing the risk of business failure.

Digital connectivity and verification:

- Limited digital connectivity, hampering the use of the digital economy to improve business efficiency and reach. This does not refer to network coverage, as it is typically, with exceptions, not a major constraint.

Collateral and affordability:

[91] This section is largely based on a discussion with the BASA SME Committee on 9 March 2023 and subsequent discussions with individual members of the Committee

- Lack of realisable collateral to secure lending, especially movable collateral without a legal and operational framework; therefore, it is not considered.
- Inability to afford finance due to the assumed risk profile, resulting in relatively high interest rates jeopardising the enterprise's ability to service loans.

Risk perception and approach:

- The risk-based approach, rather than the rules-based approach, often results in FSPs being cautious in serving informal enterprises. This aspect is further elaborated below.

These constraints often prevent informal enterprises from meeting FSPs' minimum requirements to responsibly establish a business relationship.

Demand-side challenges

Among the issues that constrain the use of financial services by informal enterprise owners is the lack of financial capacity, which is a major challenge. Other factors include:

- Insufficient financial and digital capabilities that often lead to non-beneficial biases in the use of financial services. For example, there is a general distrust of banks often characterised by the phrase: 'They eat your money' that results in informal enterprises remaining in a cash-based system. There appears to be little knowledge of, or appreciation for, low-cost entry-level banking products.
- On the part of many informal enterprises, there is a seeming preference for informal lenders (*mashonisas*) when the need arises. This appears to stem from the convenience and familiar repayment arrangement, notwithstanding the high interest rates of 30-50%[92] *per month*.
- A lack of knowledge and a perceived lack of affordability regarding insurance, particularly asset-based insurance, and insurance providers' business models that do not align with the informal sector realities.
- A lack of appreciation of the advantages of digital payments while the realities and costs inherent to the cash-based informal economy result in limited digital payment adoption. Issues around perceived and hidden costs of digital payments and fear of 'being tracked', including for tax, add to the resistance.
- A possible lack of appreciation of the role that cross-border payments could play for some informal enterprises, particularly in markets where goods are obtained or sold across borders.

These barriers are compounded by additional nuances that should be kept in mind when formulating policies and support programmes:

- **Preference for non-bank funding:** As mentioned, there is push-back against the use of banks and a greater acceptance of smaller credit providers, including unregistered credit providers in the community commonly referred to as '*mashonisas*', despite the high interest rates being charged. It would appear that the possibility of collateral to support access to loan funding is not well-established, meaning the possibility of a movable asset registry is not widely known. There is also an expectation that state grant funding should be made available to individual enterprises in addition to loan finance.
- **The need to receive value immediately**: The immediate transactability of cash is one of the reasons why the sector is still cash-dependent. The need to be able to immediately use payment receipts to buy goods or for household expenses makes using current digital payment systems impractical, as a value across different banks will only reflect the next business day, at best. There is also a significant distrust of digital payments, as these funds could be 'reversed'.

[92] Black Sash 2021

- **The need to offer and control credit to customers**: Informal enterprises, like other micro- and small enterprises, offer credit to their client base when it is required and the customer is known. Given the very thin profit margins of informal enterprises, this is a major risk to them, although necessary to 'stay in the market'. Some supporting mechanisms to make this easier for the business owners would be helpful.
- **The ability to handle payments and payment receipts seamlessly at no cost:** Informal business owners are aware that control over payments from customers and to suppliers is necessary to have an idea of 'where the business is'. The assumption that 'cash is free' and that banks and other payment service providers charge excessively emphasises the need to handle this on a no-cost basis.

Vulnerable groups such as women, migrants and young business owners are also owners of informal enterprises, and they often face additional challenges:

- Women may face challenges regarding control over finances due to the unequal decision-making power within some households. Social norms have traditionally placed men in charge of household finances, which undermines the social acceptance of women's roles as business owners and affects their access to resources required to start and operate their own businesses.
- Undocumented foreign national business owners, even those with identification documents, encounter difficulties in accessing basic financial services if the documentation is not South African. Moreover, they or their businesses often become targets of xenophobia.
- Young business owners often lack the necessary experience and a supportive environment to guide and assist them in establishing and developing their enterprises. This lack of experience and support often leads to misinformed decisions when starting a business, impeding the growth potential of these businesses.

Women in particular are overrepresented in the informal sector and some countries are including gender-specific measures in their formalisation and financial inclusion strategies. Ghana's National Financial Inclusion Development Strategy included a gender objective by integrating the Village Savings and Loan Association (VSLA) into the formal financial system. Women make up a majority of VSLA members in Ghana. The Gambia introduced preferential measures and special incentives to encourage business formalisation, focusing on women and youth. This involved promoting the role of women-owned enterprises and strengthening legislation to guarantee land ownership for women. Similarly, Nepal revised its Industrial Enterprises Act, which exempts micro-enterprises from taxes but also provides a 35% registration fee reduction for women to encourage women-headed enterprises to formalise[93].

Enabling the financial sector to appropriately serve the informal sector

A number of financial sector entities have been crucial in directing the evolution of and support for the informal sector:

- The South African Reserve Bank's **National Payment System Department** (NPSD) has outlined its strategic direction based on its Vision 2025[94] document. The strategy mentions expanding financial inclusion and the payment system, including facilitating innovation and exploring appropriate frameworks to authorise non-banks to directly access payment systems, a process that is already in operation.
- The **IFWG**[95] has been established where all regulators participate to facilitate innovation. A regulatory sandbox approach is available if fintech firms that, after registration, wish to further explore a concept in a controlled environment with the approval of regulators. Some fintech firms with the IFWG focus specifically on serving excluded groups and informal enterprises.

[93] AFI 2021

[94] SARB National Payment Systems Department 2018

[95] www.ifwg.co.za

- The **FSCA** has a strong focus on financial education and financial inclusion. Their mandate involves financial education and encouraging the provision of appropriate financial products to SMMEs, and the involvement of Seda in expanding business and financial knowledge among SMMES, including informal SMMES, is part of the implementation of this mandate.
- The **National Credit Regulator** (NCR) administers the National Credit Act and carries the mandate for the responsible development of the credit market, as well as ensuring compliance with the Act. Through the Minister, they prescribe maximum interest rates for the various categories of credit. The primary focus of the NCR is to ensure compliance with the rates and reporting requirements outlined in the Act, including the prescribed maximum interest rates (Annexure F). Addressing the operations of unlicensed credit providers is not mentioned as one of their main tasks, nor is there an emphasis on the specific clientele of these credit providers. As a result, the NCR does not have a specific focus on informal SMMEs.

Authorities have an important role, particularly in ensuring that various relevant laws and regulations do not limit informal enterprises' ability to access financial services, especially credit. Of particular importance are the National Credit Act, the Financial Intelligence Centre (FIC) Act and the Immigration Act, as amended.

The National Credit Act (2005) has the twin objectives of developing the market and providing the legal framework for the protection of the consumers of credit. Essentially, this Act focuses on market protection and market conduct. Market protection is enabled through a variety of mechanisms described in the Act. For business owners in the informal market, the following are of particular significance:

a) The requirement that credit providers rigorously assess affordability. Failure to do so could incur significant penalties and may lead to the scrapping of any debt incurred.
b) The establishment of developmental credit, *inter alia* aimed at the provision of credit for the establishment of small enterprises. This requires additional registration to advance such credit, with the NCR validating that such providers have the resources and processes to deal with developmental credit. Any registered credit provider can apply for such registration.

The effect of the first requirement has seemingly led to a contraction of advancing credit to lower-income individuals (and enterprises), as the perceived risk for credit providers is deemed prohibitive.

The legal acknowledgement of the need for developmental credit is an indication of support for micro- and small businesses in general. This development is supported by separate (higher) limits on interest that can be charged[96] and the exemption on some of the more onerous credit provider reporting requirements of the regulator. Despite this, developmental credit has only made a modest impact in the market with little, if any, growth currently. None of the credit providers interviewed mentioned this as a specific focus area. This seems to be reflected in the outstanding gross loan book per credit category as shown in Table 13[97].

[96] See Annexure F in this document

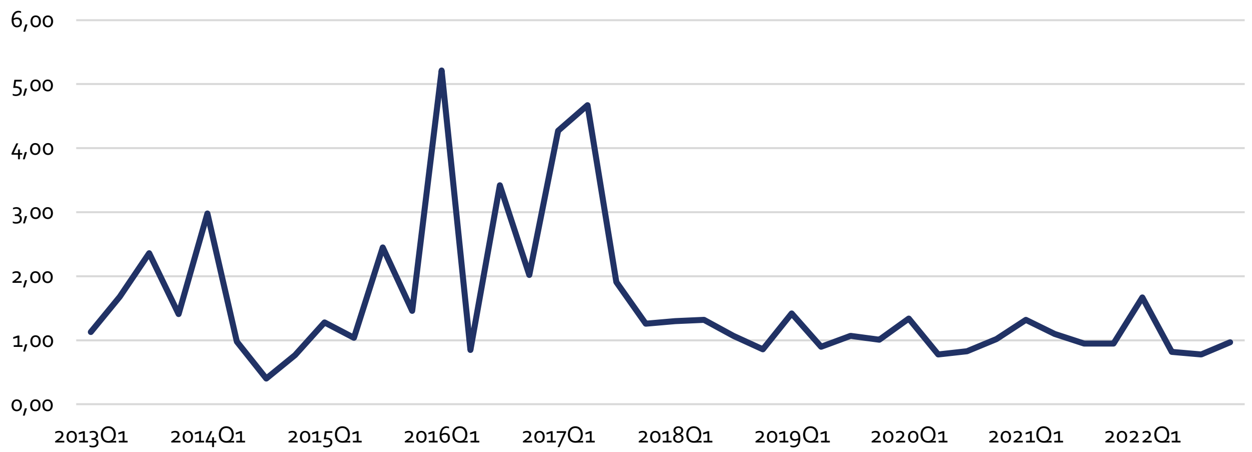
[97] NCR 2023

Table 13. National Credit Regulator's gross loan book as of Q4 of 2022 – Rand values in millions

Credit type	Outstanding book	% of Outstanding book
Mortgage	1,184,338	52,33
Secured credit	493,472	21,80
Credit facility	304,207	13,44
Unsecured	221,506	9,79
Developmental	57,555	2,54
Short-term	2,230	0,10
Grand total	**2,263,308**	**100,00**

The uptake of developmental credit over the last 10 years is shown in Chart 10 below. There is an observable dampening in the relative uptake over the last five years[98].

Chart 10: Developmental credit granted as % of total credit granted



Source: NCR

The Immigration Act (2005) comprehensively deals with the status, processes to be followed and obligations towards undocumented foreign nationals[99]. In particular, the provision of any services that will aid or enable an undocumented foreign national to establish a business in any form is prohibited in Section 42. The wording of this section is given in Annexure B. Generally, FSPs interpret this as prohibiting them from providing financial services to such individuals and; therefore, do not engage this market at all.

The Financial Intelligence Act requires that:

[98] NCR 2023

[99] *An illegal foreigner is defined as an individual who is in the county in contravention of the Act, i.e., who does not hold a valid visa or permit.*

- Accountable institutions must establish and verify the identity of their customers
- Follow a risk-based approach to customer due diligence[100].

The first requirement presents a challenge if a South African ID is not available. South African IDs can be verified relatively easily at the Department of Home Affairs, but IDs issued by other countries, like foreign passports, cannot be verified as easily. There are no digital verification processes in place with foreign authorities, making verification cumbersome and risky. This is another reason why many FSPs prefer to avoid foreigners without South African documentation whenever possible.

The second requirement directly impacts people and enterprises with limited identification information. If all information, such as proof of address, source of income, etc., is not available, the person may be considered 'risky', which could limit the availability of services to them. Many people operating in the informal sector fall into this category. The recent grey-listing of South Africa by the Financial Action Task Force (FATF) has further exacerbated the situation in this sector.

For juristic persons, the identification requirements generally followed by credit providers include:

- Business registration documents
- Proof of business address
- Identification of key individuals
- An authority to act on behalf of the entity (if required).

This explains why informal enterprises have no other practical option but to use the business owner, a natural person, as a proxy for the business.

Extending financial inclusion efforts to owners and workers in the informal sector is a natural progression of the financial inclusion gains of the last decade in EMDEs. Where necessary, a tiered and risk-appropriate approach to deal with know-your-customer (KYC) requirements may be followed, enabling users to access and use such services without providing the full set of information. This was done in Angola for the *Bankita* programme[101], specifically designed to attract people from the informal sector.

6.2 Priority 6: Broaden accessibility of financial services to the informal sector

Appropriate and beneficial financial services that are accessible to the informal sector are crucial for its development. Financial sector policymakers, regulators and FSPs share the responsibility of ensuring this goal is achieved. FSPs must ensure that they understand the sector and its complexities and are aware of the sector's needs, including those of vulnerable groups within the sector. They need to develop products and services that are attractive to the market, incorporating innovative pricing and service models.

The authorities must ensure the establishment of an enabling environment, define an adequate array of FSPs, and create a supportive environment capable of serving the sector. Authorities can play a particularly crucial role in creating an enabling environment for the informal sector by ensuring that different classes of FSPs are able to operate in the

[100] *From the FIC website: Implementation of a risk-based approach to customer due diligence, which relies on institutions determining the risks that the customer poses to the institution and its products in terms of money laundering and terrorist financing. Based on this the institutions are able to apply lighter or heavier touch customer verification and identification measures.*

Customer due diligence (CDD) refers to the knowledge that an accountable institution has about its client and the institution's understanding of the business that the client is conducting with it. The level of identification and verification can be determined in line with the client's risk profile

https://www.fic.gov.za/Resources/Pages/Legislation.aspx#:~:text=The%20FIC%20Act%20is%20one,country%20safer%20for%20all%20citizens.

[101] AFI 2021

sector. This may include enabling regulation for financial cooperatives, as was done in Ecuador[102]. Coupled with a solid regulatory framework and oversight, applying risk-appropriate levels of capital requirements leads to increased trust in and use of the financial system.

Existing financial sector footprint

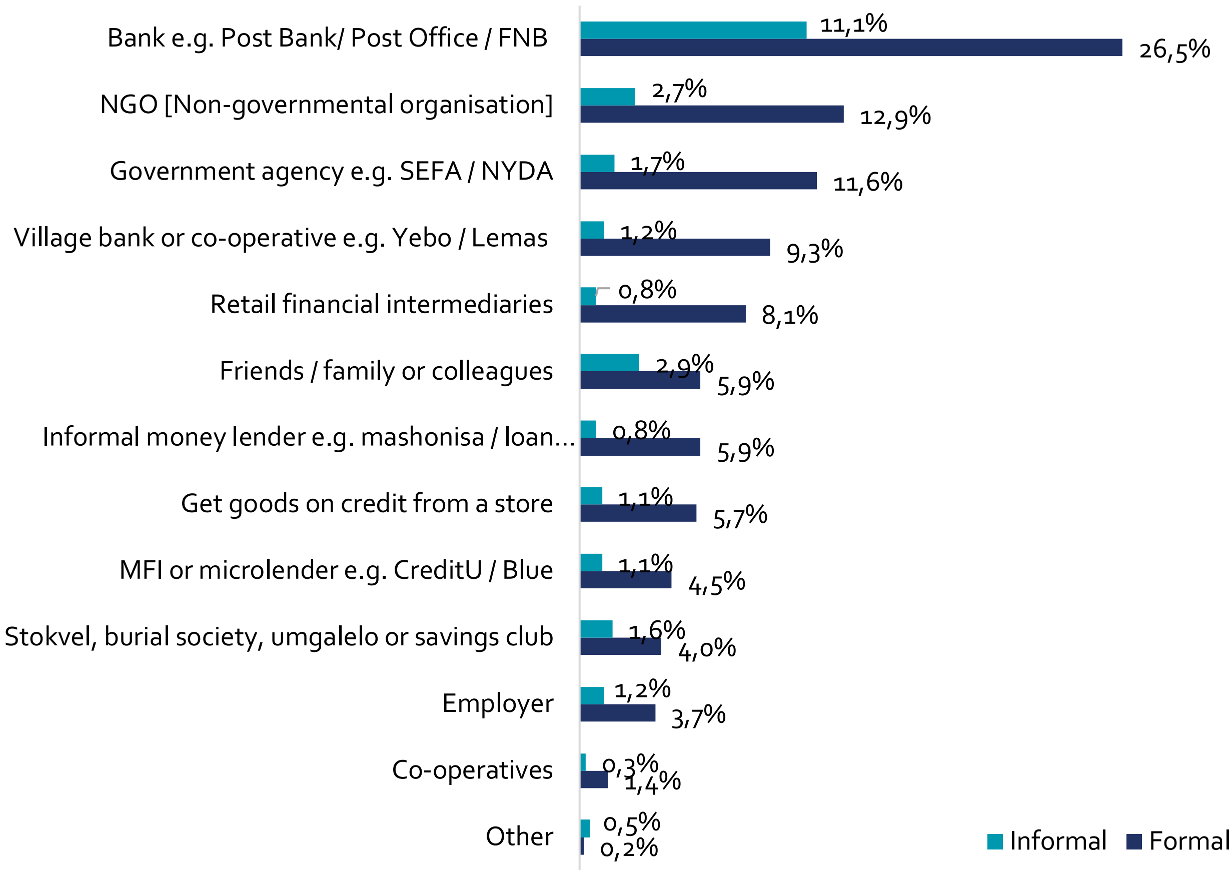
Informal SMMEs require a variety of services from formal FSPs. Among the most important are credit and payments, while insurance and remittances are also essential to many of these businesses. The array of providers with the potential to serve the sector needs to be fully leveraged, including by extending the reach of bank services through appropriate models such as agency networks and fintechs and empowering non-bank providers as microfinance institutions (MFIs), cooperative financial institutions (CFIs), and fintechs whose business models have the potential to serve the informal sector.

In terms of credit, informal SMMEs need short-term working capital to pay suppliers and employees, and finance to make investments in assets like machinery, equipment or inventory. Formal finance to the informal SMME sector credit market is estimated at upward of R1.5 billion[103], typically from MFIs, suppliers and government institutions. However, the sector also accesses finance from a spectrum of other sources, including informal sources such as friends and family, *stokvels* and informal micro-lenders or *mashonisas*. The FinScope MSME survey result below shows the sources that both formal and informal SMMEs commonly use to source finance. Formal SMMEs source funds from formal sources, such as banks and government agencies while informal SMMEs are dependent on informal sources. It should be noted that substantial finance is also provided to individuals, but this funding is used for business purposes.

[102] AFI 2021

[103] IFC, The unseen factor, 2019

Chart 11: Sources of SMME finance based on South Africa FinScope MSME 2024



Stymied role of microfinance institutions (MFIs)

MFIs are licensed under the National Credit Act, and in excess of 2,000 are registered with the NCR[104]. The sector focuses on the underserved low-income market, mainly with unsecured short-term credit, competing with informal credit providers, such as *stokvels* and *mashonisas*. MFIs are important credit providers to survivalist entrepreneurs and informal SMMEs who often struggle to meet typical requirements for funding from larger players. They apply a mix of lending models – including group loans catering to the business market's low end.

The MFI sector is divided between developmental finance (not-for-profit) MFIs represented by the Development Microfinance Association (DMA) and for-profit MFIs represented by Microfinance South Africa (MFSA). An estimated 1,400 MFIs belong to the MFSA[105], while the DMA has a further three members (the Phakamani Foundation, the Small Enterprise Foundation and Thuthukani Financial Services)[106].

Data on the sector is fragmented and difficult to obtain. While MFIs provide statutory data to the NCR as well as to the South African Credit and Risk Reporting Association (SACRRA), this data is not separately published. Interviews with the DMA indicate that developmental MFIs focus on the business (informal SMME) market, while the for-profit members' focus is largely on the consumer market with payslip loans. As of October 2024, the DMA members had

[104] https://www.sahiffund.co.za/documents/SAHIF-THOUGHT-PAPER_THE_STATE_OF_HOUSING_MF_SA_NOVEMBER- 2021.pdf

[105] https://www.mfsa.net/

[106] https://www.dmasa.org.za/our-members/

210,000 active clients and a loan portfolio of R560 million[107]. Loans are primarily group loans, with only a small proportion of individual loans. Most of these clients were female (90%), rural or peri-urban (85%) and on average, take loan sizes of R4,200. The group model has been effective at ensuring repayment, and the Portfolio at Risk (PAR, >30 days) is about 5%. In the for-profit sector, MFSA represented members with between five and seven million customers in 2018.

An estimated 3% of adults in South Africa accessed loans from MFIs in 2021, compared to 2% in Zimbabwe, 2% in Lesotho, and 4% in Malawi, according to the latest FinScope surveys in those countries. The limited impact of MFIs in South Africa (and, to some extent, the region) has been due to various reasons, especially high operating costs while being dependent on small loan sizes.

Among the challenges, MFIs in South Africa face difficulties in meeting customer due diligence requirements of FICA due to a lack of identity documents and proof of address among customers. There are also high levels of indebtedness (including mixing formal and informal credit) and the use of loans by customers for consumption rather than productive purposes, increasing the risk to serve[108]. Competition from informal providers and interest rate caps serve to constrain profits, and although MFIs offer lower interest rates and longer repayment periods than informal providers, these benefits are not always obvious to potential borrowers. Given their market focus, MFIs also face high costs of financial literacy training, high staff turnover, and a lack of adequate controls to prevent fraud. Disbursement and collection utilises bank infrastructure, resulting in high costs especially in light of the MFI's high volumes of small loans.

The relatively high cost of regulatory compliance in South Africa is also notable[109]. Formal MFIs are subject to the same set of regulations as banks, including FICA, the Protection of Personal Information Act, the National Credit Act, caps on interest rates and data submission requirements, which are onerous. A potential solution may be to develop a 'compliance lite' regulatory framework for MFIs, based on a tiered licensing model[110]. This could help address specific regulatory issues on compliance and business model, as well as around FICA/KYC requirements where MFIs currently have to meet similar requirements under the NCR as banks do. The introduction of a standardised record-keeping and reporting system can further reduce the cost of compliance and reduce the risk of over-indebtedness in the sector.

There is a general absence of global development MFIs in South Africa. This is partly due to cost and licensing requirements[111]. To maintain their standard business models in South Africa (for example, to take deposits or provide payment services), they would need to apply for a full banking licence. This is onerous, given the limited scope of their activities. A tiered licensing framework could allow global development MFIs to play a larger role in the country.

National Treasury's strategy to diversify the financial services sector should, therefore, be actively harnessed for the informal sector by enabling and supporting the development of tiered licenses in consultation with the Prudential Authority housed within the SARB. This will have the benefit of strengthening the viability and business case for MFIs and enable greater market participation. MFIs are often well-placed to engage and finance the informal sector.

Access to wholesale funding has been cited as a challenge, particularly a lack of patient capital and access to revolving facilities, which can allow smaller MFIs to build a track record and scale. Given the relatively low risk of such narrow-range providers, due consideration should be given to setting appropriate capital adequacy ratios to enable their cost of funds to be as low as possible.

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[107] Interview with DMA held on 18 October 2024

[108] IFC, The unseen factor, 2019

[109] Skowronski, G. 2010.

[110] IFC, The unseen factor, 2019

[111] National Treasury, South Africa Financial inclusion Policy, 2023

The untapped potential of the financial cooperatives sector

Financial cooperatives in South Africa are regulated under the Cooperatives Banks Act of 2008 and are authorised either as cooperative bank institutions (CBIs) or cooperative financial institutions (CFIs). The sector is yet to make a significant impact, and as of 2019, it had only an estimated 30,000 members, with 31 registered CFIs and six licensed CBIs[112]. The number has remained relatively flat (0.7% annual growth) over the past decade and is lower than in small neighbouring countries (Eswatini has 50,000 members and Lesotho has 76,000 members) and far below peer countries such as Kenya (7.7 million) and Brazil (10 million). In terms of the adult population served by financial cooperatives, South Africa ranked last out of 118 countries at 0.08% in 2019[113]. The sector had R433 million in deposits as of November 2019 and nearly 60% of the deposits are concentrated in just three institutions.

The 2008 Cooperative Banking Act established the CBDA under the National Treasury, which focuses on the training and development of CBIs.

Recent diagnostic work by the World Bank identified factors that constrain the development and growth of the CBI sector in South Africa. These include: (i) lack of public awareness; (ii) lack of desire for growth among some existing members and institutions; (iii) competition from banks and stokvels; (iv) lack of product diversity (e.g. payment services) and digitisation; (v) limited investment in core financial management and IT systems; (vi) difficulties in the hiring and retention of managers and staff with critical skills in retail financial services; (vii) lack of access to the national payment system; and (viii) difficulties securing a credit provider license from NCR[114].

In March 2021, the sector convened a National Indaba, which recommended the establishment of a second-tier cooperative bank as a high priority to serve the sector. The cooperative bank would facilitate access to national financial infrastructure, which is critical for CFIs and CBIs, as it reduces the need to access it through competitors. The second-tier bank is also expected to intermediate funds among CFIs and CBIs on a wholesale basis, helping to address their liquidity needs. Additionally, it would help broker technology solutions to groups of CFIs and CBIs to achieve scale.

A further challenge prioritised by the sector is the current regulatory approach, which results in comparatively high compliance costs, particularly regarding borrowing, non-earning assets, liquidity and capital. Recalibrating this framework with a lighter, risk-based regulatory approach could help spur growth.

At a customer level, the low awareness and penetration of financial cooperatives in South Africa remains a key challenge. Promoting the formation of cooperatives among informal enterprises is therefore essential, especially because cooperatives have consistently been mentioned in South African policies as an attractive option to harness entrepreneurial efforts in a cooperative and shared manner. This has evolved into expectations that cooperative financial institutions could equally play a greater role in financial service provisioning within the communities they serve. To date, this expectation has not materialised to the extent expected.

It is recommended that this approach be revived with a focus on informal enterprises. The concepts of pooling resources and knowledge are very relevant in the informal space, given the lack of business skills and inadequate availability of resources to establish and grow an enterprise. The cooperative approach, on its own, is unlikely to completely solve the problem, but it is likely to put enterprises that would benefit from a cooperative model on a firmer footing. Supporting the formation of cooperatives among informal enterprises will enable them to move to economies of scale far quicker

[112] Natarajan,H; et al. 2022. South Africa – FSAP Technical Note on Financial Inclus,ion. Note: A CFI must have at least 200 members and R100,000 in shares to be registered. A Cooperative Bank must have R5 million in deposits and meet more stringent prudential requirements.

[113] 2018 Credit Union Statistical Report, World Council of Credit Unions.

[114] World Bank, South Africa Financial Sector Assessment Program, Technical Note, July 2021.

than would be possible as individual enterprises[115]. Combining cooperative development among enterprises with further and focused development of CFIs will likely impact the cooperative and informal sectors positively. The DSBD's SMMEs and Cooperatives Funding Policy for South Africa mentions the possible incorporation of the CBDA within Sefa, which could be used to drive CFI development aimed at SMMEs.

Underdeveloped agency networks

The full extent of the retail agent network in South Africa is not fully understood as the authorities do not currently collect the relevant data on agents used by banks. Bank agent networks can play an important role in supporting financial inclusion, especially in rural areas, increasing convenience by being closer to customers and operating flexible hours that match local preferences. Agent networks can also help increase understanding and usage of bank services and provide an opportunity for agents (who are usually SMMEs) to earn commissions and create cross-selling opportunities. Convenience is an important aspect because, although technology and other enhancements have improved financial access in South Africa, access is still limited in rural areas due to customer distance from urban centres, preference for personal interactions, and a lack of financial education. According to the FinScope Survey 2015, the median time for adults in South Africa who live in rural areas to get to a bank branch is 54 minutes.

The retail agent network accounts for a significant share of financial access points in many countries. For example, in Brazil and China the number of banking retail agents is roughly equivalent to that of ATMs, while in Colombia and Indonesia the banking retail agents vastly outnumber other bank retail channels[116]. Similarly, in countries dominated by e-money issuers, such as Ghana and Zambia, non-bank e-money issuer agents typically outnumber bank channels. The use of small 'spaza' shops as agents is not common in South Africa when compared to other Sub-Saharan African markets, and their use can help extend services closer to the informal sector.

Kenya is a relevant example of how an African country has been able to leverage agency banking to extend the reach of banks into communities. Underbanked clients were not inclined to access banking services. As a result, the Central Bank of Kenya initiated the development of Agent Banking Guidelines for commercial and microfinance banks in 2010 and 2012, respectively. The Banking Act was amended, and the agent banking model has since enabled commercial and microfinance banks to expand into areas they would otherwise not have reached. Between them the commercial banks and five microfinance banks (MFBs) contracted 53,833 and 2,068 agents, respectively[117].

The current use of the agency banking model in South Africa is limited, partly driven by a lack of interest from banks to increase their physical footprint. Banks have been closing branches in affluent areas and, without outside influence, are unlikely to consider expansion into peri-urban and rural areas using the agency model. Further, a study undertaken by FinMark Trust[118] cited a perceived lack of clear guidance from the regulatory authorities on agency banking in South Africa, which has led to a cautious interpretation of the regulations. The Banks Act allows the use of agents; however, FICA and the Financial Advisory and Intermediary Services Act 37 of 2002 (FAIS) are perceived to be restrictive[119]. To address these bottlenecks, it is recommended that the development of institutions that can serve informal markets be prioritised (such as through tiered licenses) while also implementing a scoping study to assess whether the instruments in place allow for the required growth in agent networks, for example, by being accommodating of agent and low-income customer onboarding through tiered e-KYC. Improved coordination across regulators, including the FIC, will also

[115] DSBD 2017, *Small Businesses and Cooperatives in South Africa*.

[116] IMF Financial Access Survey (2020)

[117] National Treasury. 2023. South Africa Financial Inclusion Policy.

[118] Hawkins, P. (2012).

[119] National Treasury. 2023. South Africa Financial Inclusion Policy.

be needed. Greater use of retail agents can help foster a deeper ecosystem for digital financial services to be used by the informal sector.

Further steps to strengthening the agency model in South Africa include the development of data and evidence, particularly on the extent of the current agency network.

The potential of fintechs in the informal sector

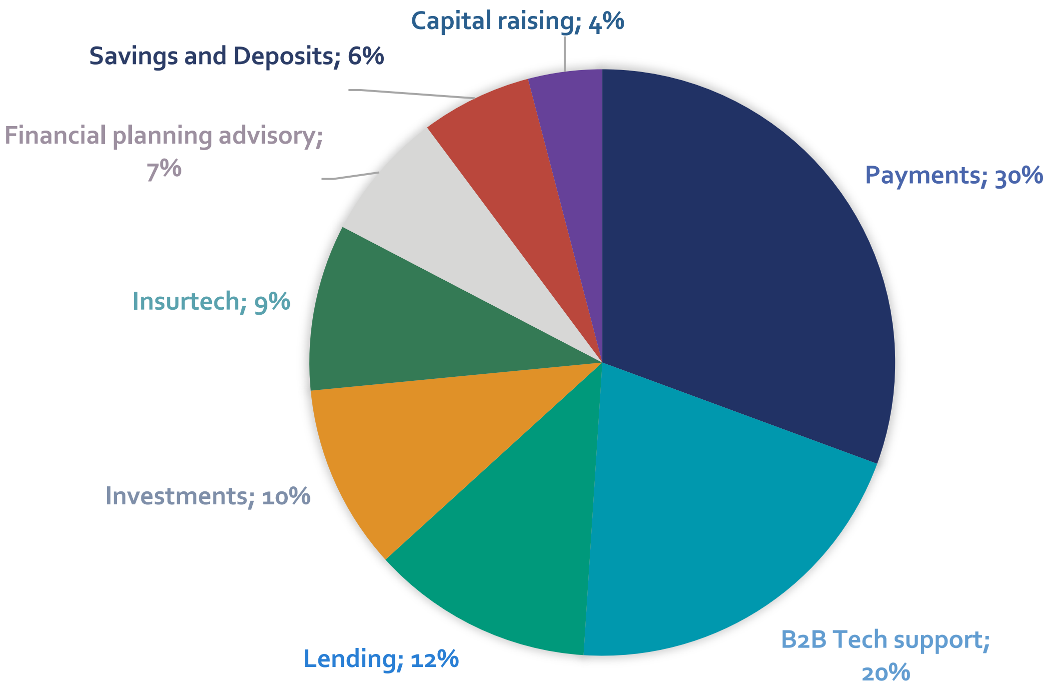
Digital financial services are an important tool for extending financial services in the informal sector. Digital payments and digital access to credit, savings and insurance can all meet important needs in the informal sector, while digital platforms in combination with digital financial services can enable informal enterprises to connect with global value chains[120]. Consideration should, therefore, be given to the role of fintech companies in supporting informal enterprises' access to and use of financial services. Fintech firms offer, for instance, alternative credit scoring that expands access to credit to individuals and entities that cannot obtain credit from traditional FSPs. Another potential offering is marketplace and peer-to-peer lending, which can make a positive impact on the underserved and unbanked market to which most informal enterprise owners belong.

The IFWG, in its 2019 fintech landscape study, identified 227 active fintech companies in South Africa, indicating a relatively small but growing fintech market. Activity is focused on five segments that represent close to 80% of fintechs: payments, B2B technology support, lending, insurtech and investments[121]. Payments represent the most active segment, with entrants focusing on merchant payments and mobile point of sale (POS) services due to regulatory constraints. Unlike many other Sub-Saharan African and emerging market countries, direct provision of payment services to payers is deemed a banking activity as it requires the handling of customer funds. This has stymied mobile money development and forced fintech companies to rely on third-party payment processors (TPPPs) and system operator (SO) licenses to access retail payment systems.

Figure 1: Fintech segments in South Africa

[120] Klapper, L. *et al* 2019

[121] Elliot L et al. 2021. South Africa – Financial Sector Assessment Program: Background Note – Fintech (English). Financial Sector Assessment Program (FSAP) Washington, D.C: World Bank Group



Source: Elliot L et al. 2021.

Leading telecom companies (MTN and Vodacom) relaunched their mobile money services in 2020 in partnership with banks, each exceeding 1 million customers within three months of launch, with offerings ranging from person-to-person (P2P) transfers, bill payments, in-person and e-commerce merchant payments to international remittances. Commercial banks have also continued to invest in digital channels, including various physical and virtual payment cards and mobile and internet-based payment applications.

Fintech lending is offered through four main products: balance sheet-based online lending, POS financing (cash advances to merchants), marketplace lending, and asset financing. South Africa is leading other African markets in marketplace lending, connecting consumer and business borrowers to lenders; however, growth has been constrained by the lack of a clear regulatory framework. Notable players in this space include RainFin, which serves corporate institutions, and PeerFin, a peer-to-peer lending platform. Equity crowdfunding is also still in the early stages of development but is also hampered by the lack of regulatory clarity. The total amount of financing provided to the SMME sector by fintech firms is not known, but a recent report estimates it at over R500 million[122].

A key challenge is that fintechs have primarily focused on relatively affluent and digitally savvy consumers[123], resulting in less attention to the informal sector. Fintech products helping to bridge the gap between the informal economy and digital financial solutions include handheld POS devices, mobile apps and payment cards. These digital solutions are significantly impacting the largely cash-based economy of the informal sector. Additionally, some fintech payment service providers use a risk-based approach in compliance with the amended FICA to onboard foreign nationals using foreign passports, with a 'best effort' approach in terms of document features and ongoing risk management.

The IFWG was formed in 2016 to catalyse the development of the sector, working through three innovation structures: (i) a Regulatory Guidance Unit providing guidance to firms; (ii) a regulatory sandbox allowing participants to test products in a real-world environment; and (iii) the innovation accelerator providing a collaborative, exploratory

[122] IFC, The unseen factor, 2019

[123] Genesis Analytics, 2017.

environment to work on emerging innovations. Among the aims of the working group is the use of fintech to address the needs of underserved and marginalised segments. The working group has launched initiatives to better understand fintech developments and to coordinate the sector. However, not much attention has been given to encouraging the industry to address specific financial inclusion challenges, like SMME finance and the lack of reliable digital ID. The IFWG sandbox and accelerator process should be used to actively encourage finding fintech solutions to underlying issues hindering financial inclusion in the informal sector, and coordinating efforts with the fintech industry to harness their potential. A detailed analysis of what more can be done to leverage fintech approaches, coupled with special calls and cohorts for fintechs focused on those challenges could be employed.

At a policy level, the role of fintech in payments is constrained by laws that limit competition. There are plans to address this through the NPSD vision document and the position paper on revisions to the NPS act, which propose remedial actions. However, implementation has been slow. In addition, critical financial infrastructure is owned by banks and incumbents, which poses a challenge as the role of fintechs expands. The retail payment systems, the credit reporting system, the gateway for ID verification services and fraud reporting repository are all controlled by banks. Key institutions include the Payment Association of South Africa (PASA) and BankServ in the payments space, the South Africa Credit and Risk Reporting Association (SACCRA) and the South Africa Fraud Prevention Services (SAFPS) in credit reporting, and the South African Banking Risk Information Centre (SABRIC) for access to ID infrastructure. Fintechs should be enabled to contribute to the future development of the infrastructure, pricing and governance. Non-banks' role in the governance of these bodies should be considered as part of the legal reform, through mechanisms such as shareholding, board of director and board committee composition and market consultation.

More broadly, slow implementation of the Conduct of Financial Institutions (CoFI) Bill, amendment of the NPS Act, and fintech initiatives under the IFWG means that several fintech developments like crowdfunding, online lending, crypto assets, open banking, alternative data and non-bank payment service providers remain either unregulated or inadequately regulated. Implementation should be fast-tracked while also considering how best to cover regulatory gaps in the interim, particularly in the context of barriers preventing entry of fintechs in some segments, effective regulation of fintechs in other sectors, and a regulatory framework for open banking.

Various products and solutions that have taken off in other parts of the world remain nascent in South Africa–largely due to the regulatory barriers limiting financial innovation[124]. Penetration in payments and lending–the two leading

Summary of recommendations:

Diversify informal sector providers, particularly through CFIs, MFIs, agency networks and fintechs:

- Promote the development of the MFI, CFI and CBI sectors by introducing tiered licensing and reviewing compliance requirements in line with the level of systemic risk they introduce.
- Support the cooperative sector to establish a second-tier bank and promote the adoption of the cooperative models by the informal sector.
- Support the development of the MFI sector by promoting data availability in the sector and developing a national strategy for the sector.
- Identify and address the market and legal/regulatory barriers for greater use of bank retail agents, through a scoping study focusing on greater use of formal and informal retail stores, the enabling legal/regulatory instruments (Banks Act, FICA, FAIS), and availing data and evidence on the sector.
- Leverage the IFWG regulatory sandbox and accelerator process to actively encourage fintech approaches to be adopted for addressing the financial inclusion challenges in the informal sector.
- Fast track legislative reforms in the NPS Act and CoFI bill, including enhancing the supervision of fintechs and non-banks' role in retail payment and credit reporting systems, with interim measures to buttress supervision and monitoring of fintechs.

[124] Genesis Analytics, 2017.

fintech segments globally and of high relevance to informal SMMEs locally–is low in comparison to other countries[125]. Government can, through the working group platform, start to address the barriers in a collaborative manner, building on the initiatives launched to date. The proposed intervention will align with the envisaged larger role for fintech companies in existing and new public credit programmes (discussed under Priority 7), and increased adoption of digital payments in the informal sector (Priority 9).

6.3 Priority 7: Redesign public credit support programmes in line with international best practices

Several agencies, including the Industrial Development Corporation (IDC), the Department of Trade and Industry (DTI), the Department of Science and Technology (DST), and the Department of Small Business Development (DSBD), which oversees Sefa, manage national government financing for SMMEs. A 2019 World Bank report estimated that there are more than 52 government programmes targeting SMMEs through these institutions, ranging in annual commitment sizes from less than R100,000 to R50 million[126]. In FY2018, these programmes had an estimated annual budget of about R18 billion and supported more than 46,000 small businesses. There are close linkages between the government programmes, with good leverage on the capabilities of the IDC and Sefa. For example, Sefa is an implementing agency for the DSBD while also a wholly owned subsidiary of the IDC. It has two reporting lines – to the DSBD and the IDC. The IDC manages several funds on behalf of the DTI and several other state agencies, while Sefa similarly manages a programme on behalf of Transnet.

The government programmes include both direct and wholesale lending, and guarantees. Most of the finance is provided through debt finance, and of the total budget in 2019, 48% was in debt finance, 35% in grants, and 17% in blended products that combine either debt or grant financing with equity[127]. The DSBD and IDC provide mostly debt finance; whereas the DTI and the Technology Innovation Agency (TIA) mostly provide grant finance. Further, while the largest proportion of the financing—nearly 80%—is channelled through the IDC, the vast majority of beneficiaries are reached via Sefa's wholesale lending channel (see Table below). This points to the opportunity to leverage Sefa's indirect channels to expand the reach of government schemes towards the informal sector. Sefa would be best positioned to work with intermediaries in the informal sector, providing the needed impact.

Table 14: *Fund disbursement through selected government vehicles*

	Value of Funds Disbursed to MSMEs at end of FY18 (R)	# of MSMEs in Portfolio
IDC	1,563,000,000	581
Direct Lending - Sefa 12	118,720,736	116
Wholesale Lending - Sefa 13	1,194,306,031	45,024
TIA	89,700,000	85

Source: World Bank, Financing Small Business in South Africa – a snapshot of Government programmes, 2019

Sefa provides financing directly and indirectly through bank and nonbank financial intermediaries, with direct financing ranging from R50,000 to R5 million. Sefa's indirect lending support ranges from R500 to R5 million, utilising intermediaries to disburse small amounts. The total Sefa loan portfolio in the 2019/20 financial year was R1.9 billion, 63% of which was wholesale lending[128]. Sefa also manages a small guarantee programme (R248 million in 2019/20

[125] BIS working paper number 887 – Fintech and BigTech Credit – Sep 2020 and CPMI Red book statistics - https://stats.bis.org/statx/srs/table/CT6a

[126] World Bank, Financing Small Business in South Africa – a snapshot of Government programmes, 2019

[127] World Bank. Financing Small Business in South Africa: A Snapshot of Government Programs. 2019.

[128] Small Enterprise Finance Agency (Sefa). Annual Report. 2020

guarantees issued) administered by its Khula Credit Guarantee Fund. The objective of the scheme is to issue partial credit guarantees to SMME lenders where access to finance is impeded by the lack of collateral. The reach of the Khula Credit Guarantee scheme has remained relatively limited, with high default rates close to 43%[129]. In 2019/20, Khula guarantees issued were .005% of GDP, compared to 4% of GDP for the SME fund in Korea.

A R200 billion Covid-19 loan guarantee scheme was initiated in 2020 as emergency support for SMMEs. Despite demand from SMMEs for access to finance, only R18 billion in loans were approved by banks and taken up by small businesses under the Covid-19 loanguarantee scheme by the time it closed in June 2021.

The effectiveness of public support programmes is generally unclear in the absence of published data on Non-Performing Loans (NPLs) and monitoring and evaluation frameworks that include rigorous assessment of their effect on productivity and employment. In addition, the available resources are small in comparison to what is available from the private sector. The IFC's Unseen Sector report estimates formal funding to SMMEs in South Africa at about R230 billion[130] compared to the R18 billion availed by the government. The government, therefore, needs to focus its resources on enabling private financial resources to flow to priority segments and should consider how to leverage its scarce but sizable public resources to catalyse or mobilise private resources. This implies phasing out direct lending programmes and exploring wholesale or credit guarantee schemes that can facilitate small business lending.

In addition, with more than 50 public programmes available to support SMMEs, streamlining these could improve their efficiency and effectiveness. Authorities should consider consolidating smaller programmes and redesigning programme features, especially for guarantee programmes and those involving direct credit, in line with international best practices. There is also a need to improve the coordination of public credit support programmes to enhance their performance. Authorities could consider allowing new non-bank players, including fintech companies, to become intermediaries for the public credit programmes, enabling them to deliver credit to specific SMME segments that might be better reached by such players.

Sefa should, in conjunction with the NCR, act as the champion and supporter of development finance for providers in the informal sector, particularly CBIs and MFIs. As the reporting requirements for such loans are less onerous than for 'ordinary' loans, this should have a beneficial effect on the institutions' willingness to extend this line of credit.

Summary of recommendations:

Redesign public credit support programmes in line with international best practices to improve their effectiveness:

- Consider consolidating smaller programmes and redesigning programme features, especially for guarantee programmes and those involving direct credit, in line with international best practices (size, lending criteria, other parameters, and intermediaries to increase outreach and additionality).
- New programmes should be piloted, except in crisis circumstances, evaluated and scaled up if proven effective.
- Improve the coordination of public credit support programmes and business development services to enhance firm performance.
- Consider allowing fintech companies to tap the existing MSME credit programmes of the government to deliver credit to specific MSME segments that might be better reached by fintechs.
- Consider phasing out direct lending programmes

6.4 Priority 8: Enhance credit infrastructure relevant to informal SMMEs

South Africa has 44 registered credit bureaus, six of which are primary bureaus, while 38 are niche and reseller bureaus, including non-traditional providers such as CredoLabs, which produces digital scorecards based on mobile data. The

[129] Credit Guarantee Roundtable: A Dialogue to Explore the Application of Credit Guarantees: Khula Credit Guarantee. June 18, 2020

[130] IFC, The Unseen Sector: A Report on the MSME Opportunity in South Africa, 2018.

credit bureaus hold data for over 60% of the adult population (25.2 million consumers as of December 2019). Data is sourced primarily from among the 7,700 registered credit providers, as well as from sectors such as insurance and post-paid mobile phone contracts. Credit bureaus also source data from the national business registry, courts, the deeds office and the South African Fraud Prevention Service.

There are two primary legislations that cover credit information sharing: The National Credit Act 34 (2005), enforced by the NCR, and the Protection of Personal Information Act (2013), enforced by the Information Regulator. Two voluntary associations support the sector, i.e. the Credit Bureau Association (CBA), representing registered credit bureaus and SACRRA, representing members who share credit and risk performance data of their customers.

While relatively well developed, the sector is consumer-focused. The omission of business credit information reflects the sector's historical development in South Africa, which predated its formal regulation. The existing infrastructure is not designed for businesses, and the layouts and standards for information sharing are designed for individuals rather than business entities. When credit information for small businesses is shared, it typically associates the credit with the individual business owner rather than the business entity. This critical gap is recognised. Although SACRRA has made efforts since 2011 to facilitate business credit information sharing, this has not yet been achieved. The lack of readily available credit risk assessment and risk mitigation mechanisms is one of the major reasons for limited access to finance for SMMEs [131]. Inadequate credit bureau data collection in the SMME sector worsens due to poor record-keeping by SMMEs and the lack of appropriate assets to serve as collateral.

The use of movable assets as collateral, in particular, has the potential to improve the availability and cost of credit by providing greater flexibility in terms of assets that can be used to secure loans. This is especially important for informal SMMEs whose capital is usually in the form of movable assets such as livestock, inventory, raw materials and equipment. However, while the South African legal framework provides for immovable as well as movable security to be used as collateral, in practice, lenders are reluctant to use movable collateral. Credit providers cite difficulties in the perfection of interests in movable property (which relies on a court process or mutual agreement between parties) and the lack of a centralised and computerised nationwide movable assets registry that would make it easier to track and detect double use of assets to secure loans. A National Treasury diagnostic study into the issue found that existing options – including pledges, notarial bonds, cessions, hire purchase agreements and retentions of title – do not provide sufficient legal certainty, while registry and enforcement frameworks are reported as being complex and outdated in various respects[132]. The diagnostic found deficiencies in the existing legal framework, including in the definition of concepts and terminology, a fragmented approach that overlooked underserviced business sectors, and incomplete integration with other laws.

It is therefore recommended to reform the law related to secured transactions to introduce a modern, simplified legal framework governing security interests in movable property[133]. This can support a modern registry for security interests in movable assets. By operating electronically, the modern collateral registry system can be made accessible to all users, including lenders, borrowers and third parties. Widening the use of movable assets (including accounts receivables, inventory, machinery, equipment and others) as collateral gives more flexibility to SMMEs, especially small and informal firms that have difficulties accessing traditional lending. It will also widen the risk mitigation mechanisms available to credit providers. This should be complemented by awareness building, business knowledge and financial literacy interventions for SMMEs.

Traditional credit data sharing should also be improved from the current largely voluntary and consequently limited data collection approach. This may require legal reform since, unlike consumer credit agreements, the National Credit Act of

[131] National Treasury, South Africa Financial inclusion Policy, 2023

[132] National Treasury, South Africa Financial inclusion Policy, 2023

[133] Secured Transactions Collateral Registries: Diagnostic for the Republic of South Africa, World Bank on behalf of National Treasury, 2015

2005 has a limited scope for the sharing of credit data on businesses. The credit information sharing infrastructure and standards for information sharing should also be reviewed. Further, mandating an increased range of SMME-related data collection by the bureaus by incorporating alternative data sources for SMME data into credit reports, notably payments data, could be useful for larger informal SMMEs to create a recorded history. An IFC diagnostic study suggested that useful alternative data for SMMEs could include information from bank accounts (e.g. related to account activity and balances), supply chain data and key indicators from merchant payments solutions[134]. The latter would be especially relevant for informal SMMEs.

Lastly, while the NCA requires registered credit providers to submit data to credit bureaus, as of February 2021, only 30% of registered credit providers reported to credit bureaus[135]. While this is increasing, further enforcement effort is needed, and the potential development of an automated and user-friendly data submission platform. Enhancing the participation of small lenders in the credit bureau can help generate increased data for informal sector SMMEs. The NCR should continue to prioritise registration of small credit providers as these account for a significant share of lending (by number of loan accounts) among low-income South Africans.

These improvements will assist credit providers in expanding their services into the informal SMME sector.

Summary of recommendations:

Improve the availability of credit information relevant to informal SMMEs:

- Reform secured transactions law concerning SMMEs to anchor a modern, simplified legal framework governing security interests in movable property.
- Establish a modern movable assets registry that operates electronically and is accessible to all users, including lenders, borrowers and third parties.
- Widen the range of SMME data available from the credit bureaus by improving reporting coverage among small lenders and incorporating alternative data sources into credit reports.

6.5 Priority 9: Promote the use of digital payments by informal SMMEs

Digital payments can serve as an important first step towards the financial inclusion of informal SMMEs, and of communities that make use of their services. Yet, structural realities in South Africa mean that a large part of the country operates in an informal economy where cash remains the dominant means of payment. MasterCard research shows that around 90% of South Africa's informal enterprises run as cash-only businesses, even though a significant proportion (51%) report they have encountered strong customer interest in paying by card[136]. Finmark Trust's research on the state of digital payments in two South African townships (Tembisa and Hammanskraal)[137] shows that the use of digital payments among informal enterprise owners remains relatively low. In Tembisa, only 11 % of informal enterprises make use of digital payments despite 66% of these enterprise owners having a bank account. In Hammanskraal, 82% of informal enterprises are banked, but only 28% make use of digital payments. Although these areas are not nationally representative, understanding the barriers that prevent the use of digital payments and finding solutions to these could be useful in providing better support for the informal sector as a whole. The barriers preventing the use of digital payments in these communities include, but are not limited to, the following factors:

- Even though digital solutions are present in the sense that POS ownership is moderate, the usage of these devices remains low.

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[134] IFC. Diagnostic: Alternative Data Landscape in South Africa. July 2021

[135] Natarajan,H; et al. 2022. South Africa – FSAP Technical Note on Financial Inclusion

[136] MasterCard 2023.

[137] Finmark Trust, 2024

- Enterprise owners perceive the cost of acquiring POS devices as high.
- Enterprise owners do not see the benefits of digital payments for their businesses, and they have negative perceptions of them, e.g. that digital payments are unsafe.
- Most suppliers of goods accept only cash, and employees are mostly paid in cash, making the presence of cash on a day-to-day basis a necessity.
- There is a lack of digital and financial literacy as well as capability among enterprise owners.
- There is a lack of trust in and dissatisfaction with formal financial services and products.
- Unstable connectivity caused by inconsistent electricity supply, limited access to fibre networks and high data costs prevent the use of digital payment methods.
- Although bank account ownership is high among South African entrepreneurs, it is low for migrant-owned businesses, especially those that are undocumented.

Promoting digitalisation among informal enterprises in such township areas could be achieved through community digitalisation programmes that create an open digital ecosystem that integrates payments in the community with the wider financial system, supported by wider social and economic upliftment efforts:

- Financial and digital literacy for both enterprises and consumers, ideally through targeted and ongoing training interventions aimed at providing community members with an understanding of the basic functions of financial products and services available to them (with a focus on digital financial services).
- Community mobilisation through the building of trust and acceptance of the value of digital payments. This should also include the promotion of existing digital payment solutions.
- Mobilisation of FSPs to provide digital payment solutions that include value-added services such as the purchase of electricity or airtime. This would incentivise customers to pay digitally and make a case for digital payments for enterprise owners.
- The digitisation of transport costs, especially taxi fares, which are the most frequently paid in cash, so that the need to carry cash is reduced.

Digitalisation, especially for the more sophisticated informal SMMEs, could be of significant benefit in growing these enterprises and improving their competitiveness. The adoption of digital payments should be used as an entry point to promote the broader use of digital financial services, which can help address access to finance challenges – this being the most significant challenge for informal enterprises in their business endeavours[138]. Access to finance is hindered by the lack of credit information on enterprises seeking loans, insufficient financial information on their current position, and either a lack of collateral or 'hidden' collateral, as informal enterprises do not disclose their financial situation to any authority. By promoting the access and use of digital transactional services and creating an enabling environment where this information can be shared, together with appropriate identification of the enterprise, this problem can be addressed. Credit applications may then be processed on an informed basis.

Wider use of digital platforms is also crucial. The Covid-19 lockdown and the resulting disruption in supply chains emphasised the need for increased adoption of web or mobile technology for informal business owners' business operations. This should go hand in hand with enterprise digitalisation efforts, where feasible, for improved productivity. The National Treasury's Community Digitisation project should be harnessed to incorporate lessons learned and to develop new beneficial engagement models to enhance the adoption and use of digital services in the informal sector going forward.

E-money offerings have the potential to pave the way for more sophisticated digital solutions, yet, to date, they have had limited market uptake in South Africa. A key driver is that the payments landscape is currently dominated by banks through the Banks Act (No. 94/1990), which limits deposit-taking and the provision of payment services to banks, mutual banks, and CBIs. The result is that only these institutions can offer payment services to payers in an unrestricted manner,

[138] *ILO 2016, Role of Finance in Driving Formalization of Informal Enterprises*

while 'non-banks' are forced to participate only after being sponsored by a bank. This raises competition-related issues that impact innovation, as well as pricing.

Increased competition in the provision of payment services is vital for innovation. The development of regulation that ensures a level playing field for all participants offering similar services, therefore, needs to be prioritised, with particular attention to fintech, mobile money and other non-bank firms. This approach will help both banks and non-banks to invest in new business models, boosting competition and innovation and ensuring lower costs for end-users[139]. Importantly, increasing acceptance of digital payments among SMMEs' customers will also support the broader adoption of digital payments in the informal sector.

To this end, the SARB has proposed legislative reforms. Envisaged changes will allow non-banks to issue e-money, process domestic remittances, offer payment services independently, and have access to the clearing house and a settlement account at SARB. These reforms need to be fast-tracked and accompanied by provisions to allow the non-bank entities to appoint agents and to apply tiered due diligence on customers, agents and merchants[140].

A further challenge in the payments ecosystem is that existing e-money offerings are closed-loop offerings. Many of the wallets use proprietary standards, and this needs to be addressed through open-loop systems and mandated interoperability.

Lastly, with the increasing usage of digital services, a range of related issues must be addressed to ensure that such use is in the interest of the user, is fair and undertaken in a secure manner. This is particularly relevant in the informal sector, given the vulnerability of many business owners. The GPFI recommends a policy framework to address this, as follows[141]:

- Financial consumer protection
  - Adapt oversight arrangements and capability for financial consumer protection.
  - Enhance disclosure and transparency.
- Financial literacy
  - Foster data collection, coordination and identification of new core competencies in digital financial literacy.
  - Strengthen the delivery of financial education for DFS and support its evaluation.
- Data protection
  - Enhance secure and effective consent models.
  - Enhance access, rectification, cancellation and opposition (ARCO) rights.
  - Address data security.

Summary of main recommendations:

Promote the use of digital payments by informal SMMEs:

- Promote digital payment ecosystems in communities, with digital payments as an entry point.
- Enact reforms to the National Payment System Act to provide a direct role for non-banks in the provision and governance of payment services.
- Develop and issue regulations prescribing retail payment instruments and open banking interoperability.

[139] SARB, The National Payment System Framework and Strategy Vision 2025

[140] Natarajan,H; et al. 2022. South Africa – FSAP Technical Note on Financial Inclusion

[141] Global Partnership for Financial Inclusion, 2018.

7. Business Support

7.1 Business support for informal enterprises landscape and challenges

Business development services landscape

The level of business and financial knowledge of business owners is fundamental to ensuring sustainable SMMEs and reducing the risk of business failure. For this reason, the government has set up Seda. Support for the informal sector predominantly comes from the DSBD, although its implementing agencies – Seda and Sefa – are involved. The DSBD has set up various programmes to support the development of small businesses in general, including the Informal Micro Enterprises Development Programme (IMEDP), which aims to empower and develop informal traders to become skilled and adequately equipped to manage their businesses.

The DSBD also runs programmes around:

- Localisation, supply chain development and supplier development partnership programmes for SMMEs
- Incubation and digital hubs roll-out
- Young entrepreneur development in partnership with NYDA and Seda)
- Cooperatives in partnership with Sefa
- Mentorship with Khula Enterprise Finance and others.

Other government departments also deliver a number of programmes targeted at mostly formal SMMEs, while local authorities provide some training, although this seems to be aimed at achieving compliance with regulations rather than developing business skills. Financial institutions have also put in place platforms for prospective SMME business owners to build business skills and financial literacy.

A summary of the programmes offered to SMMEs, including informal SMMEs, is provided in Annexure C. The basic eligibility requirements for most of these programmes include online registration (e.g. on the DSBD's national SMME website) or full CIPC registration. A South African identity document is also required.

Informal enterprise awareness and use of business support services

Generally, awareness and utilisation of available business support services in the SMME sector are low. Although it is somewhat higher for formal enterprises, the difference is not significant, and the use of these services by informal enterprises is often negligible. The table below shows some of the key players in this space:

Table 15 Awareness and use of business support services

Organisation	Awareness by formal enterprises (%)	Awareness by informal enterprises (%)	Use by informal enterprises (%)
Business Partners Limited[142]	11,0	4,0	2,0
Banks	7,0	3,0	0,4

[142] Business Partners Limited provides business loans and support services to viable SMMEs.

National Federated Chamber Of Commerce (NAFCOC)[143]	3,0	1,0	0,0
Department of Small Business Development (DSBD)[144]	7,0	3,0	1,0
Department of Trade and Industry and Competition (DTIC)[145]	10,0	4,0	0,1
Small Enterprise Development Agency (Seda)[146]	7,0	3,0	0,3
Sector Education and Training Authorities (SETAs)[147]	7,0	3,0	0,3
National Youth Development Agency (NYDA)[148]	5,0	4,0	0,0

While some of these are exclusively for formal SMMEs, the lack of awareness among both formal and informal SMMEs is clear. It is concerning given that the lack of business and managerial skills is often cited as one of the major reasons for the relative lack of sustainability and growth among SMMEs in general and informal SMMEs in particular.

Non-financial business-related challenges

Apart from challenges in accessing financial services (See Chapter 6), informal enterprise owners face significant challenges on multiple fronts. These result from various structural realities and deficiencies in the economic and social fabric of society. Among these challenges are the following aspects:

Infrastructure

- Access to markets in general, with access to supply chains as part of the issue. Insufficient access leads to constraints in business growth and sustainable revenue. It also implies that enterprises need to be prepared for market expansion, which includes ensuring product or service quality as well as some standardisation measures.
- Practically all enterprises in South Africa share the common challenge of reach, quality and reliability of the public logistics network, which is problematic and becoming increasingly so. While large corporates can, to some extent, overcome this with alternative arrangements, smaller and informal enterprises particularly are largely dependent on the public system.
- The inadequate electricity system is hampering business operations for all enterprises. Larger enterprises and many established formal SMMEs can mitigate this lack of service delivery by providing alternative

[143] Nafcoc is an independent and non-profit business support organisation primarily, but not exclusively, serving the black community.

[144] DSBD is a South African government department established in 2014 to lead and coordinate an integrated approach to the promotion and development of entrepreneurship, Small, Medium and Micro Enterprises (SMMEs) and Co-operatives, and to ensure an enabling legislative and policy environment to support their growth and sustainability.

[145] DTIC is a South African government department established in 2019 to develop and roll out policy interventions that promote transformation and competition issues through effective economic planning, aligned investment and development policy tools.

[146] Seda provides non-financial support to small enterprises and cooperatives.

[147] SETAs contribute to the raising of skills, to bring skills to the employed, or those wanting to be employed, in their section. They have to do this by ensuring that people learn skills that are needed by employers and communities.

[148] NYDA is a South African-based agency established primarily to address challenges faced by the nation's youth.

energy, but informal enterprises often lack the resources to do the same and, therefore, have to suspend business operations when there is no power.

- Access to and usage of facilities or business premises where goods and services can be offered is often a constraint, leading to the erection and use of temporary structures of dubious quality in some cases. Municipalities and metros are mandated to allocate land and erect basic structures, but it would appear that these processes are sometimes inadequate or too slow to meet the needs of enterprises. The allocation also does not always match the market flows that enterprises would like to tap into.

Competitive landscape and market access

- The structure of the South African economy, where several large corporates provide consumer goods and services in a largely efficient and convenient manner. This restricts small enterprises from certain activities that are often the engine for sustainability in other markets. Informal enterprises are, therefore, restricted to finding niches within value chains where they can compete. For example, selling bread rather than having small enterprises involved in all aspects of the bread value chain.
- Most informal enterprises operate in a competitive space. Enterprises in the same industry segment tend to follow similar business models with similar input and operational costs. The ability to differentiate based on price is limited, with margins needing to match competing enterprises' price structures. Municipal business sites often group similar types of businesses together, which is convenient for price-sensitive consumers but increases competitive pressure for the enterprise owner. Like practically all enterprises in South Africa, the reach, quality and reliability of the public logistics network are problematic and becoming increasingly so. While large corporates can, to some extent, overcome this with alternative arrangements, smaller enterprises and informal enterprises are largely dependent on the public system.

Managerial and technical skills:

- Business skills among informal enterprises are often not at the level that a business requires. This includes basic business skills like accounting, cash flow analysis, inventory management, pricing and marketing. It also includes sector-specific skills, depending on the sector in which the enterprise would like to engage.
- The cost of operating a business is often underestimated and can be a real block to establishing a business, given that most informal enterprises operate in a highly competitive environment. The costs include labour, transport, registration and compliance costs for local business registration (where applicable), energy, input costs, network data and servicing costs.
- In general, there is a low level of adoption of digital technologies for the enterprise by business owners. While the level of smartphone ownership or access in South Africa is relatively high, the use of digital services that such devices enable to advance the enterprise is low. This reflects a gap in digital literacy beyond basic personal use and a lack of appreciation for how the judicial use of digital technologies can benefit business development.

Addressing non-financial challenges for the informal sector

Business development services, or business support services, are necessary for the entire SMME landscape, not only the informal sector. Support for the informal sector, including formalisation policies, should explicitly address the issue of business development and the role of the various stakeholders in this process. Specifically, business support services targeting the informal sector should include basic financial literacy, business management skills, including the management of competition, innovative ways to expand a business and or diversify products and services, and knowledge of the relevant entities that can provide support to informal enterprises. This is best achieved through a comprehensive approach that is coordinated.

Many of the existing SMME support programmes are relevant to larger informal SMMEs (especially those in Segment 3). However, available programmes often carry participation criteria that end up implicitly excluding informal SMMEs.

Prohibitive conditions may, for example, include formal registration, minimum requirements in terms of enterprise age, size or profitability, requirement for a credible business plan, or a requirement to travel to regional branches for the programme[149]. Another key challenge is that the programmes are not well-coordinated across departments, leaving some potential beneficiaries unserved, for instance, informal SMMES. Pre-registration (Priority 3) and better coordination to eliminate gaps would help improve access of larger informal SMMEs to these programmes.

Smaller survivalists and emerging SMMEs that form a majority of the informal sector face a more significant challenge. Most of the public programmes in place are not designed to serve these SMMEs in Segments 1 and 2. Programmes designed for survivalists and small informal SMMEs should, at the onset, recognise the multiple constraints facing them and respond with multidimensional economic inclusion programmes customised to the local context. A recent review of such programmes globally shows that governments typically bundle multiple interventions, which result in a greater impact on income, assets, and savings relative to standalone interventions[150]. Bundled interventions typically include cash transfers, skills training, coaching, market links, and access to financial services. Non-economic facets are also important. A study in Niger showed the value of including well-designed psychosocial components in such interventions to complement traditional training[151].

Survivalists and emerging South African informal sector SMMEs face a long list of constraints that can be best addressed through phased, multi-intervention programmes. These should consider, among others, basic financial literacy, business management and entrepreneurial skills, social well-being, and the potential use of incentives, as many beneficiaries are uncertain of the returns they may get from the training[152]. The training should be flexible, delivered by providers already active in the communities, in local languages, and be geographically accessible. The geographic location of where the training is delivered can be a significant barrier, particularly for women and girls.

At the upper end of the small informal SMMEs (Segment 2), new programmes can emphasise certain aspects such as mentoring, business planning and business plan competitions, and seed funding via grants rather than loans. The Kenya Youth Employment Opportunities Project (KYEOP) can provide a useful model here[153].

Further, there is a growing recognition that a greater degree of self-organisation could improve the market position of informal enterprises. It appears that such an organisation is in a nascent phase at best, but there is an appreciation that costs could be reduced through bulk purchases and coordination of logistics. Sharing business insights is also a possibility, although the question of how this would co-exist with the competitive nature of most businesses is unclear. Informal businesses can also join informal trader associations, which provide a platform to address issues that are commonly experienced.

The use of informal clusters to enable access to business support and self-organise enterprises for greater efficiency is attracting increasing interest[154]. Clusters can be defined in different ways, such as geographic location or type of enterprise. These clusters serve as a channel to deliver interventions that support informal businesses. They reach many businesses through a representative body, communicate market opportunities and other support actions, and facilitate moves to a more formal status.

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[149] Cunningham, Wendy, ., Ngarachu, M. & Lekezwa, I., 2022.

[150] Andrews, C. et al. 2021.

[151] Bossuroy T. et al, 2022.

[152] ILO 2023.

[153] https://youth.go.ke/projects/

[154] Marusic, A. *et al* 2020

7.2 Priority 10: Develop new programmes and extend existing SMME support to the informal sector

As mentioned earlier, existing support programmes hardly cater for survivalist (basic) informal SMMEs, and new programmes should be developed under the leadership of the DSBD to cater for this market segment. For Segment 1 and 2 SMMEs, new programmes are suggested incorporating the following:

- For Segment 1, phased, multi-intervention programmes including basic financial literacy, business management, entrepreneurial skills, social well-being, and incentives to encourage uptake.
- For Segment 2, mentoring, business planning and business plan competitions, and seed funding via grants rather than loans.
- Flexibility, use of local languages, geographical accessibility, and self-organisation (clustering) to improve efficiencies, e.g. bulk purchases, logistics, and access to business support.

It has already been noted that while they might be appropriate for larger informal SMMEs, most formal programmes exclude informal sector enterprises either explicitly, through the set requirements, or in their design, with informal enterprises receiving very little if any, support. Apart from the provision of business premises and the corresponding local business registration, local authorities are seemingly more intent on compliance than on support, leaving informal enterprises to fend for themselves. Part of the efforts to bring the informal sector into the main economy should, therefore, be to facilitate their participation in formal support programmes.

For the larger informal SMMEs, it is suggested that efforts be focused on the following:

- Review participation criteria and coordination to enable their incorporation in supply chain development initiatives, both by the public and the private sector.
- Review participation criteria to ensure inclusion in government procurement targets and programmes.
- Extend formal support to informal enterprises and workers involved in those enterprises. At the enterprise level, this should include emergency support measures such as those implemented to deal with the Covid-19 lockdown.
- Accelerate access to incubators and skills development programmes and workshops that upskill entrepreneurs in their area of focus.

Although the focus of this framework is on the enterprise, it is important to address social protection for individuals, as this will make entrepreneurship more appealing. Currently, own-account workers, including those operating single-owner enterprises, are excluded from the benefits of the Unemployment Insurance Fund (UIF). This situation needs to be addressed, with the principle that eligibility for support should not be linked to the requirement that an individual must register as an enterprise. It is not suggested that the full benefits of the UIF should apply in the informal sector, but the principle must be that appropriate support is provided.

The limited support for the informal sector extends to emergency response and social protection, which is currently prejudicial to informal enterprises and the workers in these enterprises. The lack of financial support for informal enterprises during the Covid-19 lockdown is a case in point. The fact that workers are dependent on an employment contract before being eligible for unemployment insurance benefits from the UIF is another example. Also, social grants would typically exclude someone with an informal enterprise from receiving any grant, though many women in this position need child support grants.

Organisations representing informal enterprises generally have a low profile, resulting in little real support for informal enterprises. This could be due to many reasons, not least of which is the policy vacuum in which informal businesses find themselves. The alternative to self-organise seems to be underdeveloped, leaving informal enterprises largely on their own in navigating the business landscape.

Summary of recommendations:

- Develop new programmes and extend existing SMME support to the informal sector, including:
  - Increased inclusion of larger informal businesses in existing business development programmes by adjusting the criteria and requirements and improved coordination across these programmes.
  - Active inclusion of larger informal SMMEs in government procurement targets and programmes, supply chain development initiatives, and incubator and upskilling programmes and workshops.
  - Extension of formal support to informal enterprises and workers involved in those enterprises, e.g. emergency support.
  - Creation of new multifaceted programmes targeted at the low end (Segment 1 and 2) of the informal SMME sector, including support for clustering.

7.3 Priority 11: Promote financial, digital and business skills among informal enterprise owners

As mentioned, improved digital and financial literacy are clear requirements for informal enterprise owners to progress. This is true for the digitisation of their businesses but also for general business operations and the realisation of opportunities. With more informal enterprises encouraged to join business development programmes, digitalisation components can be enhanced within the programmes and coupled with digital and financial literacy. Cooperation with digital service providers and with the providers of digital literacy programmes is therefore essential. Seed funding, possibly from Sefa but also from the Development Bank of Southern Africa, may well be necessary to kick-start this programme. Such a programme should make use of the extensive range of fintech firms already operating in the country and typically with the entrepreneurial drive to engage in new challenges. Resources from the financial sector should also be leveraged to deliver financial education. The high priority placed by SMMEs on access to finance, coupled with the ready use of *mashonisas* by informal enterprises, provides a stark example of why increased financial literacy is required.

Currently, the FSCA has the policy mandate for improving these skills, with CBDA, Seda and Sefa also responsible for certain elements of business development, including Seda incorporating the use of digital skills, particularly within the business context. There is an ongoing process to merge the business development elements of CBDA, Seda and Sefa, and this will help to improve coordination in the sector. Nevertheless, there is a need for a more concerted effort to coordinate efforts, in the context of the informal sector in particular but also in the context of the National Financial Inclusion Strategy and National Financial Education Strategy, both currently in the development process led by the National Treasury.

In addition to public sector players being involved in the broader coordination process, there is room for new, innovative technological companies to support the improvement of the digital capacity of SMMEs. These companies could assist in improving the overall operational and marketing efficiencies of informal enterprises through their range of services, which cover business management, financial literacy, financial management, and knowledge on how to gain access to markets, to mention but a few.

It is proposed to step up the effort to coordinate and align existing efforts and to catalyse new ones, and this should happen as part of a national coordination platform from an oversight perspective, with localised support coordination being supplied by the local support staff in conjunction with the four organisations mentioned. All efforts should be available to all small enterprises, irrespective of the status of the enterprise or the segment within which the enterprise finds itself. It is important to note that this cannot be a once-off exercise but calls for an ongoing commitment.

Part of the implementation of skills improvement should include regular market assessments of the efficacy and impact of such training, with adjustments where necessary.

Summary of recommendations:

- Strengthen, coordinate, and align existing efforts to improve business skills currently being conducted by the FSCA, CBDA, Seda, and Sefa; closely link the process with the National Financial Inclusion Strategy and National Financial Education Strategy processes under the National Treasury.

8. Enabling Taxation Framework

8.1 Tax framework for informal SMMEs landscape and challenges

SMME tax requirements in South Africa

The administrative compliance burden of accounting for and paying taxes separately is not insignificant for micro- and small enterprises. This involves separate payments for various taxes. Some of these separate payments have since evolved into turnover tax which replaces income tax, VAT, provisional tax, capital gains and dividends tax. Most informal small and micro-businesses would fall under the turnover tax category, which covers enterprises with a turnover of less than R1 million per year. In this case, the first R335,000 of the enterprise's annual turnover is exempt from tax, and thereafter the enterprise is expected to pay 3% of its annual turnover in tax[155].

Depending on the type of the business, the following tax options may apply:

- Value Added Tax (VAT), which is an indirect tax on the consumption of goods and services
- Pay As You Earn (PAYE), which is employee tax that is deducted from employees' salaries as advance income tax payments
- Customs, which are duties or taxes on imported products
- Excise duties and levies, which are for high-volume daily consumable products or luxury items
- Skills Development Levy (SDL), which is for employers to develop employees' skills
- UIF, which is for short-term relief for employees in the event of unemployment.

As mentioned in the reasons why informal enterprise owners operate informally (Section 5.1), there is a perception that registering a business automatically leads to taxation. Tax compliance is a significant deterrent to formalising because informal business owners already pay VAT on the goods that they sell and are often unable to absorb any other additional costs. There is also a lack of understanding of tax law that leads to the assumption that all registered businesses are eligible to pay tax, regardless of their turnover.

In addition, for improved compliance by informal SMMEs, it is also important that the public services, in their respective areas of operation and interest, are sufficiently useful to justify taxation. While enforcement is an important determinant of compliance, increased benefits for the enterprises may help improve compliance[156].

[155] South Africa Revenue Service (SARS) Small Businesses – Taxpayers, available at: https://www.sars.gov.za/businesses-and-employers/small-businesses-taxpayers/

[156] Levenson and Maloney, The Informal Sector, Firm Dynamics and Institutional Participation, World Bank, 1998

Global approaches to taxation of informal sector SMMEs

In many countries, taxation is one of the main reasons enterprises remain informal. Simplifying tax registration and compliance is therefore of paramount importance to encourage more informal enterprises to formalise. Coupled with reasonable tax thresholds, this approach makes the path to eventual tax compliance more enticing.

- As described in box 1 (Section 2.5), Brazil has established, refined and simplified its tax system in the context of a broader reform process, and achieved some success in this journey. Other jurisdictions have extended the use of the tax system to influence enterprise behaviour for the benefit of informal enterprises. For instance, Uruguay promoted the use of digital payments at merchants by doing away with tax on the transactions. A similar approach was adopted by Rwanda during the peak of the Covid-19 epidemic, but for mobile money transactions, which are prevalent in the informal sector.
- Indonesia introduced a range of tax incentives to support SMMEs and the move to formalisation. This included a business tax of 1% of turnover for micro-enterprises, further reduced to 0,5% in 2018. Additionally, they reduced or exempted social security contributions for certain SMMES, together with reduced or exempted VAT and tax holidays for specific sectors. Despite these incentives, participation in the informal economy remains significant[157,158,159].

8.2 Priority 12: Develop a tiered taxation system to cater for the informal sector

Tax collection is a real concern for informal business owners. It is recommended that the approach to tax collection is overhauled to ease requirements for smaller players in the sector. The proposed tax reform will ease compliance for all informal sector SMMEs, whether pre-registered or not. Pre-registering will allow SMMEs on the database easier access to support for tax compliance. Where informal sector businesses are independently pursued by the tax authority, the outcome would depend on the tax law rather than pre-registration status.

The tax reform should be executed with the following objectives anchoring the selection of various thresholds and parameters:

- Ignore tax collection for the basic segment.
- Levy a simple all-inclusive tax on all emerging enterprises with a business ID. This should be not much more than a token contribution to the state's revenue. A fixed amount is proposed, with allocation to municipal fees, income tax, VAT and the UIF done on an ex-post basis.
- Introduce a higher rate, but still not punitive, for the established informal business segment on the same basis, except that VAT and UIF contributions could be based on real turnover and actual employees. A single payment should still be used to limit compliance costs for such enterprises. This will enable enterprises in the segment to 'ease into' full compliance.
- Rationalise and simplify the graduated entry into the tax system once full registration takes place.
- Education on tax literacy should be rolled out to sensitise enterprise owners to the various elements of tax and what implications these have for their businesses.

Summary of recommendations:

- Develop a tiered taxation system to cater for the informal sector.

[157] Lasarti, R.A. 2023

[158] Shonozaki, S. 2022

[159] PWC, 2023

9. Governance and Coordination

9.1 Collaboration and coordination

The mindset of involved policymakers needs to be aligned

Engaging the informal sector in a holistic and supportive manner is a significant opportunity to deepen economic participation for many people in South Africa who are currently marginalised or excluded from the main economy. The informal sector is already making a real contribution to employment and the economic life of areas where they operate, despite a largely non-existent or porous supporting net for such enterprises. If this situation is addressed in a manner that optimises their contribution and creates pathways to directly participate in the formal or mainstream economy, then it should have a substantial effect on the country's economic prospects.

Approaching support for the informal sector with the main purpose of trying to formalise as many enterprises as possible is bound to lead to a contraction of the sector without any real impact on the formal sector. Maintaining the status quo and tweaking a few support mechanisms is also unlikely to result in increased employment. A more promising and pragmatic approach appears to be to accept that the informal sector has the potential to contribute to the economic well-being of the country and to create employment if it is appropriately and sustainably supported and enabled. Such an approach does not exclude some formalisation; however, this will then largely be a continuation of the development of enterprises that have achieved some level of maturity.

Compliance-driven orientation in dealing with the informal sector creates a divide between the authorities and the enterprise owners, with evident mistrust towards the government in general. It is also likely to lead to the exit of many survivalist SMMEs. An alternative would be to deliberately move towards a supportive environment with the expectation that enterprises will, over time, achieve greater compliance because they will perceive it to be in their interest to do so. This approach should also include allowing the business owners to select support measures that they consider most appropriate.

The implementation process is suggested to be inclusive, with activities allocated to the most relevant organisation or agency, monitoring these implementations and making adjustments based on the monitoring, if necessary. Programme management and disciplines are relevant in this context. Additional specific issues that need to be considered in this respect include:

- The need for consistent data definitions and the use of demand-side data to inform the implementation and monitoring[160].
- Include non-traditional organisations in the guidance and implementation – representative organisations of informal enterprises, NGOs involved in the informal sector, religious groups, etc.
- Increased engagement with the corporate sector to gain their insights and buy-in for interventions.
- Whenever necessary and possible, invest in more evidence and monitoring[161].

Policy impact matrix

The informal sector policy support has been designed with consideration to the needs of SMMEs across four segments and along their lifecycle, emphasising increased business support and basic skills in earlier stages (Segments 1 and 2) and more advanced support in Segment 3. For example, to acquire and use a unique identity while still remaining

[160] AFI 2021

[161] ILO 2016, Policies, Strategies and Practices for the Formalisation of Micro and Small Enterprises

informal, or access to existing support programmes. The proposed set of recommendations each emphasises some segments more than others across the informal SMME spectrum and is further outlined in Annexure G.

Policymakers need to remain cognizant of the intended impact of each policy action, and to follow through by ensuring the involvement of all relevant institutions, as well as monitoring whether the intended results are achieved.

Aligning solutions to the country's context

Duplicating successes from other countries is rarely possible without carefully considering the necessary adjustments to improve the likelihood of success. This localisation process must consider established practices within the country, both in terms of government cooperation and state support for enterprises, as well as general business practices. Legal matters such as land ownership and tenure, labour laws, and other relevant issues need to be identified for adjustment, where necessary. Societal norms will significantly influence the acceptance of initiatives and should be carefully considered.

Segmentation holds much promise and has been deployed to tailor interventions and support, matching the needs more precisely than a one-size-fits-all approach can achieve. In this setting, country context also plays a major role. The suggestion made in Section 4.3 of this report can be further built upon based on further research and data.

Ensuring that the needs and aspirations of vulnerable groups are also being addressed in a progressive and inclusive manner is crucial for sustainable economic development. The policy implementation for the informal sector needs to initiate discussions and reach agreements with, among others, the Department of Women, Youth and Persons with Disabilities, as well as financial regulators, that these groups are adequately catered for in developmental efforts and the establishment of new services.

Improving supporting infrastructure

Informal enterprises require basic services in order to conduct their operations, and some of these issues fall outside the immediate scope of this document. The following basic infrastructural support is critical to informal businesses:

- Improvement in the transport infrastructure and arresting the degradation of road and rail networks. This has a major impact on the costs for all enterprises, disproportionally so for most informal enterprises.
- The problems with the supply of electricity and the rising cost of the service are well-known and ongoing. Where feasible, support should be given to practical alternative energy sources, particularly solar energy[162].
- Coordinated, supportive and fair business premises and zoning arrangements for all enterprises, including informal ones, are required at the national level, with consistent implementation at the local level. Implementation should be based on the needs of consumers likely to visit such premises.
- Improvements in digital infrastructure and decreasing the cost of accessing digital networks will require cooperation with the relevant departments, regulatory authorities, and providers.

Key government strategies around these issues need to be influenced to explicitly take the needs of the informal sector into account, such as the modernisation of transport and financial infrastructure or dispute resolution mechanisms, among others.

[162] See for example SolarNow, https://www.solarnow.eu/about-us/

9.2 Priority 13: Establish formal coordination mechanisms to catalyse informal sector support

It is paramount that efforts to positively impact the informal sector are aligned that policies and interventions are actively coordinated, and that key stakeholders at national, provincial and local government are involved appropriately. There is sufficient evidence that single and or uncoordinated interventions typically have little or no impact or lasting effect.

Such coordination requires a national platform, preferably supported by a single overarching policy clearly articulating the acceptance of and support for the role of informal businesses, as mentioned in Pillar 1. While the platform or group should not be cumbersome, all the main actors need to be incorporated and participate in the national platform. Ideally, it should be chaired by the DSBD. The mandate needs to be agreed upon among the stakeholders and relevant cabinet clusters; however, it should essentially be the steering committee deciding on and overseeing interventions in support of the policy and following the pillar structure proposed here, as amended. Although the focus should be national, the oversight of this platform needs to cover all levels of government, including direct oversight of the supporting structures at the local and district levels. Coordination efforts could also consider including international agencies and organisations in informal sector support to allow for the alignment of interventions.

There appears to be insufficient coordination between various officials from all three levels of government, as well as from state agencies, in the support and oversight of the informal sector. The roles of these officials, often within the same level of government, are overlapping and causing some confusion in the market. This situation results in officials on the ground lacking the developmental knowledge and skills to effectively deal with or support enterprises. An ideal solution would be to have one, or at least a limited number, of officials on the ground, representing multiple levels of government and multiple organisations. Skills and expertise can then be established and developed at a central level with identifiable support at the local level – a centralised expertise and decentralised support approach.

In developing such an approach, the following will have to be considered:

- Who takes responsibility and administers the decentralised support staff? Practically, this should be the local authority or the DSBD, or a combination of these. Given that a national and consistent approach is required, at least a joint responsibility is recommended, with the DSBD specifying the role and managing the links to the 'centres of expertise' while the local authority administers the staff. The national forum referred to above should oversee the process.
- Do the support staff also act in an oversight role, or are these two roles separate? In general, an approach to the sector should reflect a supportive and developmental policy attitude. A case can, therefore, be made that the roles are merged so that enterprises know they deal with one entity that is primarily there to assist them in 'doing business'.
- The existing roles and level of responsibility between the various levels and organs of government have to be maintained as far as possible.
- Clusters (mentioned above) could further play a major role in providing a ready avenue for the decentralised support to work with and to self-administer support initiatives.

Unlocking the potential of the informal sector in a holistic way to the benefit of all role players and, indeed, to the economic well-being of the country as a whole is a mammoth task. A coordinated structure as envisaged above should, therefore, be put in place. The coordination mechanism should be at a sufficiently high level and have direct reporting to the President's office. The central coordination mechanism should be complemented by working groups, particularly in the areas of policy (led by the DSBD and National Treasury), segmentation and development of unique business identifiers (DSBD, DTIC, CIPC and National Treasury), financial sector development and adjustments (DSBD, National Treasury and the financial sector regulators), business support (DSBD, Seda, Sefa, COGTA, SALGA, provincial authorities, FSCA and National Treasury) and tax (DSBD, National Treasury and SARS).

The recommendations are summarised in the Table in Annexure D.

Summary of recommendation:

- Establish formal coordination mechanisms to strengthen and align informal sector support.

Annexure A: Legal and regulatory structures and policies relevant to informal SMMEs

Name of policy/regulation	Objective and relevance to the informal sector	Impact on the informal sector and or formalisation
National Development Plan (NDP)	Create 11 million new jobs by 2030, 90% of which will come from small and growing enterprises[163]	NDP does not explicitly mention how the informal sector will be supported, how entry barriers will be addressed for the informal sector
National Informal Business Upliftment Strategy (NIBUS)	Uplift informal businesses within the informal economy and support local chambers, local business associations, municipalities, and Local Economic Development offices to access upliftment programmes[164] Shared Economic Infrastructure Facility (SEIF) collaborates with local authorities to provide co-working space for small enterprises and the Informal and Micro Enterprise Development Programme (IMEDP) works to improve the working conditions of individual enterprises[165]	First nationally coordinated informal sector policy Policy targets both entrepreneurs and the working conditions of informal workers through its two-pronged approach (SEIF and IMEDP) NIBUS bridges the gap left open by the exclusion of informal SMMEs in strategic frameworks such as the National Development Plan[166] NIBUS has been criticised, however, for its anti-migrant undertones in its pursuit to strengthen *South African* informal sector businesses**Error! Bookmark not defined.**

[163] Skinner, C. 2019, Informal-sector policy and legislation in South Africa: Repression, omission and ambiguity.

[164] Institute for Economic Justice 2018, Jobs Summit Policy Brief 1 of Stream 3: Informal Economy/Sector

[165] Department of Small Business Development 2019, Speech by Minister of Small Business Development on the occasion of stakeholder engagement in Dundee. Available online: http://www.dsbd.gov.za/speech/speech-minister-small-business-development-occasion-stakeholder-engagement-dundee. Accessed: 23 January 2023

[166] Charman, A. 2017, Micro-enterprise predicament in township economic development: Evidence from Ivory Park and Tembisa.

Name of policy/regulation	Objective and relevance to the informal sector	Impact on the informal sector and or formalisation
Provincial Policy Examples**Error! Bookmark not defined.**: KwaZulu-Natal Informal Economy Policy Township development strategies in Limpopo Western Cape Informal Sector Framework Gauteng Informal Business Development Strategy eThekwini Municipality Policy for Informal Economy Support	Facilitate the transition from informal to formal economy Promotion of enterprise development Promotion of social protection rights for all persons within the sector Regulation of the informal sector through a balanced approach between incentives, enforcement, and compliance Financial and non-financial support to informal businesses The eThekwini Municipality Policy for Informal Economy Support sought to introduce 'a new category of economically trained sector specialists' to better understand the informal economy	All policies seek to support access to enterprise-related infrastructure, promote township economies, and review regulations and bylaws to eradicate the exclusion of informal workers and entrepreneurs Unfortunately, the policies in KwaZulu-Natal, Limpopo, Western Cape and Gauteng had an anti-migrant sentiment, with the worst case being Limpopo, where an overtly xenophobic approach was used against informal businesses owned by migrants Implementation of policy pillars in practice is non-existent or slow
ILO Recommendation 204: Transition from the Informal to the Formal Economy **Error! Bookmark not defined.**	Providing rights, protections and incentives for informal workers Recognising public spaces as workplaces (allowing for unregulated access by informal workers) Promoting social protection for informal workers, including gender protection Including organisations of informal workers in all negotiations that affect them Preserving the livelihoods of informal workers during the transition to formalisation	A specific gender-focused angle is useful for women as a vulnerable group in the informal sector Recognises that the transition to formality requires an approach that does not eliminate informal workers' income, leaving them destitute Challenges with implementation include inadequate financial resources for the R204 Expanded Task team to engage Lack of resources to allow for informal worker organisations to meet Insufficient engagement with the Department of Cooperative Governance and Traditional Affairs and its constituent municipalities to ensure implementation at a local level
National Small Enterprise Act (via the draft National Small Enterprise Amendment Bill)[167]	Allows for the establishment of the National Business Council and provides guidelines for organs of state to promote small businesses	Mainly administrative and empowers the functions of the Minister of Small Business Development Not necessarily centred specifically on the informal sector

[167] South African Government website, National Small Business Act 102 of 1996. Available online: https://www.gov.za/documents/national-small-business-act Accessed: 23 January 2023

Name of policy	Objective and relevance to the informal sector
National Informal Business Upliftment Strategy (NIBUS)	The NIBUS prioritises five economic sectors[168] for strategic interventions – services, retail, manufacturing, agriculture, construction and maintenance. The NIBUS also aims to assist the informal sector through: - A Shared Economic Infrastructure Facility, which will cover the funding of a common infrastructure[169] that is maintained and shared by informal businesses, SMMEs and cooperatives. - Informal Business Upliftment Facility, which will be targeted at informal businesses and prioritising women, youth and people with disabilities owning businesses, focussing on the provision of machinery and equipment. - An Informal Traders Upliftment Project aiming at developing the capacity of informal traders to increase their competitiveness.
National Integrated Small Enterprise Development (NISED) Masterplan[170]	NISED is essentially DSBD's strategy for SMMEs focusing on the following objectives: - An integrated approach across all spheres of government and other key stakeholders in advancing small enterprises - formal, informal, and cooperative - to achieve higher growth and labour absorption. The co-ordination of the different levels of the public sector is explicitly mentioned in this regard. - Advancing inclusivity with tailored support and services (both financial and non-financial) and incentives. There is a specific focus on vulnerable groups – youth, women, people with disabilities and previously disadvantaged groups both in the formal and informal economy. - An acknowledgement that SMMEs are not homogenous, and that the lifecycle of the enterprise and the intent of the business owner will largely determine how such enterprises are positioned in the economy. Understanding the needs of these different types of enterprises, including the needs of informal enterprises, is necessary to make it easier for small enterprises to thrive and for informal enterprises to be included in the mainstream economy. - Advancing a simplified regulatory regime to ease the migration of enterprises towards greater formality. Early-stage enterprises and informal enterprises must be assisted and incentivised to graduate into more formal arrangements. The document acknowledges that previous drives to formalise informal businesses have had little effect over the years. This assistance should include enhancing income protection of informal workers and enterprise owners, providing greater access to skills development and assisting in the access to technology and infrastructure. - Recognition that the national support agencies providing both financial and non-financial support should be re-organised to provide better service and coordination of public and non-public support to small enterprises.
SMMEs and Cooperatives Funding Policy	This policy is aimed at the SMME sector, but specific references are made to access to finance for informal enterprises: - Establish guidelines to recognise informal SMMEs without the need for full formalisation. - Establish the means to uniquely identify SMMEs on a voluntary basis, extending this to enable access for all support but not using this to immediately position the SMMEs for full taxation.

	- Include identifiable SMMEs in the alternative data system for credit assessment, specifically by including digital payment data from such enterprises. - Including SMMEs operated by identifiable foreign nationals. - Explicitly positioning Sefa as a development financial institution for the SMME sector, enabling a range of FSPs to better service the sector, including informal enterprises. Consideration should be given to incorporating the CBDA in this effort to improve the capacity of cooperative financial institutions to service their enterprise members. - Working with the National Treasury and regulators to enable a sufficiently diverse range of FSPs to serve all SMMEs.
National Treasury's Financial Inclusion Policy	*An Inclusive Financial Sector for All*[171] represents a broad-based approach to extend financial services beneficially and sustainably to all South Africans. Although informal enterprises are not mentioned explicitly, several policy interventions are put forward that will be of direct benefit to informal enterprises. This includes: - Improve access to credit by building credit infrastructure for small businesses: This refers to strengthening the credit information system by including payment data, improving the capacity of the credit guarantee system to be available to all FSPs, working with involved parties to establish a movable collateral registry, and improving business knowledge and financial literacy in conjunction with other organisations, including Seda. - Suitable insurance for SMMEs: This intervention requires research to understand the risk-management needs of SMMEs and then develop minimum product standards to meet these needs. Exploring the feasibility of index insurance for agriculture is also included. - Strengthening financial cooperatives and the developmental microfinance sector. This intervention has two focus areas – strengthening cooperative financial institutions and banks and introducing a tiered (or risk-appropriate) licensing for deposit taking with the aim to broaden the diversification of providers in the banking system. - The National Treasury has a direct interest in and provides support for financial literacy policies and programmes. This is a key pillar for them to move informal enterprises to formality through financial literacy.

[168] Department of Economic Development Gauteng Province 2016
[169] The Shared Economic Infrastructure Facility is a 50/50 cost-sharing facility with a maximum funding of up to R15 million.
[170] Department of Small Business Development 2022
[171] National Treasury 2020

Annexure B: Wording of Section 42 of the Immigration Act of 2002

The following extract is obtained from Section 42 of the Immigration Act of 2002[172].

42. Aiding and abetting illegal foreigners

(I) Subject to this Act and save for necessary humanitarian assistance, no person shall aid, abet, assist, enable or in any manner help -

(a) an illegal foreigner; or

(b) foreigner in respect of any matter, conduct or transaction which violates such foreigner's status. When applicable, including but not limited to-

(i) providing instruction or training to him or her. or allowing him or her to receive instruction or training;

(ii) issuing to him or her a licence or other authorisation to conduct any business or to carry on any profession or occupation;

(iii) (iii) entering into an agreement with him or her for the conduct of any business or the carrying on of any profession or occupation

(iv) conducting any business or carrying on any profession or occupation in cooperation with him or her;

(v) assisting, enabling or in any manner helping him or her to conduct any business or carry on any profession or occupation;

(vi) obtaining a licence or other authority for him or her or on his or her behalf to conduct any business or to carry on any profession or occupation;

(vii) doing anything for him or her or on his or her behalf in connection with his or her business or profession or occupation

(viii) harbouring him or her, which includes providing accommodation: or

(ix) letting or selling or in any manner making available any immovable property in the Republic to him or her.

(2) In any criminal proceedings arising out of this section, it is no defence to aver that the status of the foreigner concerned, or whether he or she was an illegal foreigner, was unknown to the accused if it is proved that the accused ought reasonably to have known the status of the foreigner, or whether he or she was an illegal foreigner.

[172] Government Gazette 2002, https://www.gov.za/sites/default/files/gcis_document/201409/a13-020.pdf

Annexure C: Summary of key programmes supporting the SMME sector

The following table summarises selected key projects implemented to support SMMEs in South Africa[173, 174, 175].

Organisation	Support/programme offered	Support/programme objective	Requirements/eligibility criteria
Department of Small Business Development (with Nedbank)	Township and Rural Entrepreneurship Programme (TREP)	1. Encourage small enterprises' participation in rebuilding and restructuring the economy in townships and rural areas 2. Improve the quality and competitiveness of small enterprises for both domestic supply and the export market 3. Encourage small enterprises to seize opportunities in various sectors availed by the Covid-19 pandemic through the value chains and beyond.	1. Registration for small business funding via online form on the national SMME website (RSA identity document and valid municipal trading permit required) 2. Use of a mobile phone to apply for a grant.
Department of Small Business Development through Seda's network	The Informal Micro Enterprises Development Programme (IMEDP)	1. Empower and develop informal traders to become skilled and adequately equipped to manage their businesses 2. Provide equipment and machinery that enterprises in the sector need 3. Provide a 100% grant to informal and micro-enterprises ranging from R500 to R40,000 to assist them in improving their competitiveness and sustainability.	1. Minimum of three months trading 2. Applicants must be South African, black-owned and an informal micro-enterprise (RSA identity document is required) 3. Applicants must provide proof of banking and proof that they use a stokvel, i.e. a savings or investment society 4. Applicants must have completed mandatory business development training at one of Seda's 53 branches.

[173] http://www.dsbd.gov.za/programmes

[174] Shttp://www.Seda.org.za/Programmes/Pages/Home.aspx

[175] https://www.Sefa.org.za/products/direct-leaning-programmes

Department of Small Business Development	SMME-focused Localisation Programme	1. Reconfigure supply chains to co-create market opportunities for SMMEs 2. Develop a manufacturing sector for an improved industrial base (productive economy) through a focused import replacement programme as well as build an industrial base for both domestic and external markets 3. This programme is enabled through the Small Enterprise Manufacturing Support Programme (SEMSP), which offers up to R15 million in loans and blended financing to SMMEs.	1. Complete the simplified online application form 2. Company statutory documents 3. FICA documents 4. Certified ID copies of directors/members 5. Six (6) months' bank statements 6. Latest Annual Financial Statements or Management Accounts (not older than three months) 7. Business profile 8. Project execution plan 9. Twelve (12) months cash flow projections 10. A copy of the lease agreement or proof of ownership 11. Relevant industry certification, facility statements of other funders and quotations for applied funding.
Department of Small Business Development	Enterprise and Supplier Development Partnership Programme	Partner with major corporates and state-owned companies to unlock supplier opportunities for black-owned and women-owned SMMEs, including those based in townships and rural areas	Each corporation's ESD or supplier development programme has a unique set of requirements; however, the common requirements include the following: 1. Registered enterprises 2. Qualifying B-BBEE rating 3. A well-defined business plan 4. Proven financial history

			5. Overall positive performance
Department of Small Business Development	Incubation and Digital Hubs Roll-Out	1. Establish 250 incubation and digital hubs by 2024 in collaboration with universities and TVET colleges across the country 2. Establish 27 new incubators, specifically in rural areas and townships.	Eligible enterprises will be assessed according to the following criteria: 1. Defined identity, vision and strategy of the business 2. Business model 3. Implemented business model (products or services sold in a specific market). Seda branches provide the necessary assistance with regard to the requirements listed above.
Department of Small Business Development (with NYDA and Seda)	Young Entrepreneurs Support	Support young entrepreneurs through financial support and the provision of business development skills	The requirements vary depending on the specific component of the programme being applied for. The following are general requirements: 1. Aspirant youth entrepreneurs, youth-owned and managed enterprises (unemployed youth, graduates and youth in rural areas) Requirements for the Youth Entrepreneurship Collateral Fund: 1. Registered start-up

			enterprises (SMMEs and cooperatives) owned by young people.
Department of Small Business Development	Co-operatives Development Support Programme (CDSP)	1. Support cooperative enterprises financially and non-financially in partnership with other key strategic stakeholders 2. Offer blended financing in partnership with Sefa. The grant funding portion is capped at 70% while the loan portion is capped at 30% of the total approved funding – the total funding is limited to R2,500,000 3. Support the acquisition of machinery, equipment, infrastructure, commercial vehicles and business development support.	Primary cooperatives: 1. Must be registered in South Africa in terms of the Co-operatives Act, Act no 14 of 2005 2. Must be a primary cooperative with a majority black membership 3. Must have business activities in any economic sector 4. Must adhere to cooperative principles, be biased towards women, youth and people with disabilities 5. Must provide proof of training or experience in areas of cooperative governance. Cluster cooperatives: 1. Must be a registered secondary cooperative in South Africa registered in terms of the Co-operatives Act 14 of 2005 (as amended)
Department of Small Business Development	Shared Economic Infrastructure Facility (SEIF)	Fund industrial hubs, SMME container clusters, informal trader markets, etc.	Eligible applicants must either be: 1. A municipality of the Republic of South Africa 2. A municipal entity as defined in Section 1 of the Local

			Government Municipal Systems Act, 2000 3. A provincial government entity 4. Private sector (a registered legal entity in South Africa in terms of the Companies Act, 1973 (as amended) or the Companies Act, 2008 (as amended); or the Co-operatives Act, 2005 (as amended).
Department of Small Business Development	Khula Enterprise Finance	1. De-risk bank finance for SMMEs by offering mentorship to entrepreneurs to help them manage their business successfully 2. Provide mentorship programmes that include skills transfer, assistance with business plan development, and pre- and post-loan services.	1. Applicants must be South African citizens and the owner of the enterprise 2. The enterprise must be located within South Africa's borders and economically viable with a profit motive 3. Applicants must have sufficient business skills and experience 4. A minimum of 10% personal contribution is required, either in cash or assets 5. Businesses must be registered and have a sound business plan.

Department of Small Business Development	Support for new economy start-ups	1. Create an enabling ecosystem for high-tech start-ups and increasingly link incubation to this key growth area 2. Increase the accessibility of the DSBD, Seda and Sefa services in townships and rural areas 3. Raise awareness of the TREP and ensure that local economic development offices adequately support SMMEs in registering or applying for products and services offered by the DSBD.	All SMMEs, both registered and unregistered.
Small Enterprise Development Agency (Seda)	Seda Technology Programme (STP)	1. Increase accessibility to, and utility of technologies and management support for SMMEs through structured platforms such as technology business centres 2. Facilitate the acquisition and transfer of technology to SMMEs, particularly those operating in the second economy 3. Promote the use of quality and standards by SMMEs 4. Improve SMMEs' performance and productivity 5. Improve SMMEs' competitiveness 6. Promote entrepreneurial activity and the success of identified target groups, particularly women and youth 7. Reduce the failure rate of SMMEs.	The focus of the fund is on the manufacturing sector. 1. Applicants must demonstrate their ability to increase turnover and create jobs, as well as show existing products with proven market demand, established pricing, and how channels to market are accessed. 2. Approved applicants are required to commit to a three-year contract of continuous performance monitoring and reporting to deliver impact and return on the fund's investment through job creation and turnover 4. Preference will be given to women-owned businesses and operational manufacturing enterprises with high job creation

			potential in underserved areas.
Small Enterprise Development Agency (Seda)	The Quality and Standards Programme	1. As part of the STP, this programme aims to ensure that small businesses have access to quality control and assessment processes and provides training and access to accreditation and certifications 2. The aim is to promote the importance of quality and standards as key drivers of South Africa's competitiveness to enhance the quality and standard of products and services produced by South African small businesses through management systems implementation.	As above
Small Enterprise Development Agency (Seda)	Seda Incubation Programme	Strengthen technology commercialisation and harness the entrepreneurship of the technology community in South Africa	Anyone with a viable business idea or any registered SMME who is struggling to grow may apply to participate in this programme.

Small Enterprise Finance Agency (Sefa)	Business Viability Programme	1. Promote SMME competitiveness, sustainability, viability and growth; promote job creation, reduce job losses and business closure, and provide sufficient financial and non-financial support to enable SMMEs to operate efficiently. 2. The programme covers the acquisition of new equipment, machinery, vehicles and other related business assets for business-related purposes only, in addition to working capital and non-financial support such as business development services.	The programme is open to all eligible enterprises that meet the qualifying criteria. The following enterprises will be prioritised: 1. SMMEs that are already funded by the Small Business Development portfolio through grants and various other interventions, Sefa-funded SMMEs, and Seda-supported entities 2. SMMEs that applied for the SMME Debt Relief Facility but were not approved due to budget constraints 3. Preference will be given to SMMEs owned by youth, women and people with disabilities, including SMMEs operating in townships and rural areas.
Small Enterprise Finance Agency (Sefa)	Small Business Innovation Fund (SBIF)	Steered towards supporting start-up enterprises through a combination of a grant and a loan	1. Applicants must be South African citizens with a fixed physical address 2. Applicants must have a registered business with a business plan and a valid tax clearance certificate 3. The ability to repay the loan is a requirement.

Annexure D: Summary of Recommendations

Recommendation	Description	Suggested responsible parties	Time horizon	Applicable segments
Pillar one: Policy Approach				
Priority 1: Issue a stand-alone policy statement from the Office of the Presidency that articulates a policy approach that prioritises informal businesses.	• This policy statement should guide and align the actions of all government entities and all other actors in the informal ecosystem towards supporting the informal sector. • Emphasis should be made on the fact that this policy requires effort from various government departments. • The policy should position informal enterprise owners as valid and valued corporate citizens; it should acknowledge the diverse nature of the sector and commit to supporting the sector appropriately to achieve greater economic significance while ensuring sustainability and beneficial outcomes for all actors, including workers, owners and the supporting ecosystem.	NT, DSBD, DTIC, Presidency	Short-term	1 – 4
Priority 2: Determine a segmented approach for the informal sector to allow for the extension of market support services and initiatives.	• The segmented approach should be based on attributes such as business maturity, the size of the business, the characteristics of the business owners, entrepreneurial skills and attitude, the reasons behind the establishment of the business and the desire to grow or develop the business. • The proposed segments of informal enterprises could comprise of: a) A **basic segment** consisting of businesses with turnover below R100,000. These are primarily single-owner-operated enterprises where there is little evidence of a desire to extend the business to the extent where further employment would become likely. The intent of such enterprises is primarily to support the household with a market focus rooted in the community in which they operate. b) An **emerging segment** with a business turnover of R100,000 to R300,000, where further support could boost the potential of the business. Employment has either taken place or is likely to take place, and the enterprise may have an interest beyond just the community in which it operates, either through directly serving further afield or by arrangements with other enterprises. c) An **established informal business segment**, with business turnover >R300,000 and where the viability of the business has been proven and the enterprise is already, or largely, operating in a similar fashion to enterprises that have formalised. This segment may include potential high-growth start-ups. c) An **agricultural segment,** with operating realities and aspects of required support that is different from the segments above. • The segmented approach will allow for the extension of market support, such as access to financial services, support services and access markets and market initiatives.	DSBD, DTIC, CIPC and NT	Medium-term	1 – 4

Pillar two: Identification, registration, and onboarding				
<u>Priority 3</u>: Implement a pre-registration identification system for all informal enterprises on a voluntary basis and delinked from tax and labour law requirements.	• This system should not imply registration at SARS or at the Department of Labour and Employment and should identify enterprises much the same way that individual IDs are used. • The identification system should be kept as simple as possible, with the owner/manager of the enterprise serving as a proxy for the informal enterprise. It should capture the following details: business name, ID of owner(s), segment category (according to the approach in priority 2 above), business sector, contact details, address, and number of employees.	DSBD, DTIC, CIPC and NT	Short-term	2 – 4
<u>Priority 4:</u> Reshape the SMME registration and licensing process to be more integrated and streamlined.	• Introduce a fully integrated business registration system with: a) A one-stop process, completely digital and assisted if required. b) Links to all appropriate authorities, including local authorities. All required business registration should, therefore, happen as part of the process, with local support staff involved where required for support and/or verification purposes. c) A link to and registration with SARS. d) Link and registration to the Department of Employment and Labour e) Link to any specific (sectoral) business support services and information on any specific compliance issues applicable to the sector(s) in which the enterprise operates. f) Availability of data in the registration database should be immediate and directly available to qualifying entities via a standardised interface. This will enable FSPs to immediately establish a business relationship with registering entities. g) Reduce the cost of this registration to zero or near zero, as the advantage of having a fully registered business far outweighs any registration revenue.	DSBD, DTIC, CIPC SARS, FIC and NT	Medium-term	2 – 3
<u>Priority 5:</u> Update registration, licensing, finance and other laws and regulations to support informal businesses	• Review regulations to accommodate the new legal statuses of identified businesses. • Consideration should be given to the implications of other laws that might be impacted by the business identity system (e.g. Immigration Law)	DSBD, DTIC, CIPC and NT	Medium-term	1 – 4

Pillar three: Access to finance				
Priority 6: Broaden accessibility of financial services to the informal sector, particularly through CFIs, MFIs, agency networks and fintechs	• The National Treasury's strategy to diversify the financial services sector should be harnessed for the informal sector. The following avenues of implementation should be considered: a) Champion products to propel the MFI and cooperatives sector, including development finance facilities, agri- and business insurance, payments, and deposit protection; this should include these institutions being integrated into the national payment system b) Promote the adoption of cooperative models by the informal sector to enable such enterprises to move to economies of scale c) Promote the adoption and use of digital technology and credit information systems in the cooperative sector d) Explore options to encourage the emergence of more deposit-taking MFIs, in consultation with the Prudential Authority housed within the South African Reserve Bank e) Identify and address the market and legal/regulatory barriers to the greater use of spaza shops and other widespread networks as retail agents and agent aggregator models f) Explore how the role of fintech companies in the informal sector can be enhanced, including through regulatory support (national payment network reform), incentives and enablers, and partnerships and linkages g) Fast-track legislative reforms in the NPS Act and the CoFI Bill, including enhanced supervision of fintechs and non-banks role in retail payment and credit reporting systems, with interim measures to buttress supervision and monitoring of fintechs.	DSBD, NT, SARB, FSCA, NCR, FIC	Long-term	1 – 2 (coops, MFIs) and 2 – 4 (agents, fintech)
Priority 7: Redesign public credit support programmes in line with international best practices	a) Review and redesign public credit support programmes, phasing out direct lending and strengthening outreach towards smaller businesses and the informal sector b) Review the size, parameters and intermediaries in the existing partial credit guarantee schemes to increase outreach and additionality in the informal sector, considering additional channels and more flexible lending criteria.	DSBD, DTIC, NT	Medium-term	2 – 4
Priority 8: Improve the availability of credit information relevant to informal SMMEs	a) Legal reform to underpin the use of movable assets as collateral b) Establish a modern, centralised and computerised movable assets registry c) Expand the range and depth of data available from credit bureaus to include more SMME-related data, including alternative data such as payment data.	DSBD, NCR, NT, SARB, FSCA	Medium-term	2 – 4
Priority 9: Promote use of digital payments by informal SMMEs	a) Legal reform (the National Payment System Act) to enhance the role of non-bank payment service providers b) Review regulations and practices to promote interoperability of retail payments instruments c) Community-based interventions to pilot community digitisation.	DSBD, Seda, Sefa, CBDA, digital service providers, innovative technology companies	Medium-term	2 – 4
Pillar four: Business Support				
Priority 10: Develop new programmes and extend existing SMME support to the informal sector	a) Development of programmes targeting basic/survivalist SMMEs in the informal sector b) Extending existing market access support to larger informal enterprises as well as: - Inclusion of informal businesses in supply-chain development initiatives led by both the public and the private sector - Inclusion of informal businesses in government procurement targets and programmes - Extension of formal support to informal enterprises and workers involved in those enterprises, e.g. emergency support. At the enterprise level, this should include emergency support measures	DSBD, Seda, Sefa, CBDA, Development Bank of Southern Africa, FSCA	Long-term	1 – 2 (new programmes) and 3 – 4 (existing programmes)

	such as those implemented to deal with the Covid-19 lockdown - Acceleration of informal enterprise access to incubator projects that include programmes that upskill entrepreneurs in their area of focus - Support to encourage clustering of SMMEs for economies of scale.			
Priority 11: Promote financial, digital and business skills among informal enterprise owners.	• The national coordination platform proposed for the informal sector should be used to coordinate and align existing efforts to improve business skills currently being conducted by the FSCA, CBDA, Seda and Sefa. • Efforts should be closely linked with the National Financial Inclusion Strategy and National Financial Education Strategy processes, both currently in development by the National Treasury • Innovative technological companies should be encouraged to support the improvement of the digital capacity of SMMEs.	DSBD, Seda, Sefa, CBDA, FSCA	Short-term	1 – 4
Pillar five: Enabling taxation framework				
Priority 12: Develop a tiered taxation system to cater for the informal sector	• Overhaul the approach to tax collection with consideration of the following: a) An exemption of tax collection for the basic segment of informal businesses as outlined in pillar two above b) Implement a simple all-inclusive tax on all emerging enterprises with a business ID. This should be not much more than a token contribution to the state's revenue. A fixed amount is proposed, with allocation to municipal fees, income tax, VAT and the UIF done on an ex-post basis c) Introduce a higher rate for the established informal business segment, on the same basis, except that VAT and UIF contributions could be based on real turnover and actual employees. A single payment should still be used to limit compliance costs for such enterprises. This will enable enterprises in the segment to 'ease into' full compliance d) Rationalise and simplify the graduated entry into the tax system once full registration takes place e) Improve education on tax literacy to sensitise enterprise owners to the various elements of tax and what implications these have for their businesses.	DSBD, National Treasury, SARS	Long-term	1 – 4
Priority 13: Establish a formal coordination mechanism to catalyse informal sector support	• Establish formal coordination mechanisms to strengthen and align informal sector support that: a) Sets the national agenda as regards the informal sector b) Is cross-cutting across government ministries, agencies and levels c) Considers the overall objectives of the reforms and vulnerable segments, and responds to the country's context.	DSBD, Presidency	Short-term	1 – 4

Annexure E: Legislation impacted by recommendations

Legislation	Description	Relevance to recommendations
Companies Act, 2008	The overarching Act from which the CIPC's primary institutional mandate is derived.	**Priority 3 and Priority 4:** Recognition of informal businesses through issuance of business identifiers and reshaping the registration process for enterprises.
Financial Sector Regulations Act, 2017	The objective of the Act is to split the regulating authorities of the financial services sector into two centres: a) Prudential Authority (PA) which supervises the safety and soundness of financial institutions b) Financial Sector Conduct Authority (FSCA), which supervises the way financial institutions conduct business and treat their customers.	**Priority 6**: Broaden accessibility of financial services to the informal sector. The merging of CBDA, Seda and Sefa and the implications of this on informal enterprises is especially relevant under this legislation.
Business Act No.71, 1991 (including the Act as amended in 1993)	The Act governs the licensing of enterprises in South Africa. The amendment to the Act in 1993 governs the issuing of municipal licenses and permits to businesses.	**Priority 4:** Reshaping the licensing process for enterprises to allow for a new legal status that will be granted to businesses identified through the unique business identifier.
Protection of Personal Information Act, 2020	The Act is a privacy law that safeguards the integrity and sensitivity of private information.	**Priority 3 and Priority 8:** Implementing a pre-registration identification system for all informal enterprises and credit information will need to adhere to the POPI Act. The usage of this data by DSBD, financial institutions and other entities will have to adhere to the Act.
Immigration Act, 2002	This overarching Act provides for the regulation of admission of persons to, their residence in, and their departure to RSA; and for matters connected therewith.	**Priority 10:** The extension of formal support to the informal sector will have implications for migrant-owned informal enterprises. Depending on DSBD's approach, this reform could impact immigration laws.
Tax Income Act, 1962 & Tax Administration Act, 2011	These acts provide for the effective and efficient collection of tax.	**Priority 3 and Priority 12:** Implementing a pre-registration identification system and tiered tax will require tax laws to explicitly exempt some informal enterprises and recognise onboarded SMMEs using the unique business identifier that is recommended.
National Credit Act	This is the overarching Act that regulates the credit industry and also ensures compliance by credit providers.	**Priority 7 and Priority 8:** Redesigning public credit support programs in line with international best practices and reforms to credit information will impact the National Credit Act.
Labour Relations Act, 1995	This Act seeks to advance economic development, social justice, labour peace and democratisation of the workplace.	**Priority 5:** Update registration, licensing, finance and other laws and regulations appropriately to support informal businesses.
Basic Conditions of Employment	This Act seeks to give effect to fair labour practices.	**Priority 5:** Update registration, licensing, finance and other laws and regulations appropriately to support informal businesses.
Security by Means of Movable Property Act 57 of 1993	The Act underpins movable collateral interventions.	**Priority 8:** Reforms to credit information will impact the secured transactions law and related frameworks.
National Payment System Act and its regulations	Promote inclusive digitisation	**Priority 9:** Enhance the use and interoperability of retail payments instruments **Priority 6:** Broaden accessibility of financial services to the informal sector – enhancing the role of non-bank players.

Annexure F: Maximum Prescribed Interest Rates in South Africa

Credit type	Maximum Prescribed Interest Rates	Current Repo Rate (RR) is 8.25%	Previous Repo Rate was 7,75%
1. Mortgage agreements	[RR+12%] per year	20,25%	19,75%
2. Credit facilities	[RR+14%] per year	22,25%	21,75%
3. Unsecured credit transactions	[RR+21%] per year	29,25%	28,75%
4. Developmental credit agreements	[RR+27%] per year	35,25%	34,75%
- Small business			
- Low-income housing			
5. Short-term transactions	5% per month on first loan. 3% per month on subsequent loans	5% per month and 3%	5% per month and 3%
6. Other credit arrangements	[RR+17%] per year	5,25%	24,75%
7. Incidental credit agreements	2% per month	2% per month	2% per month

Annexure G: Policy Impact Matrix

Pillar	Priority	Anticipated impact on informal SMME segments			
		Basic (<R100k turnover)	**Emerging (R100 – 300k)**	**Business (> R300k)**	**Agriculture**
I. Policy and governance	1. Policy direction	Acceptance as a viable job creation mechanism to be supported holistically, e.g. capacity, finance, compliance	Acceptance as a viable job creation mechanism to be supported holistically, e.g. capacity, finance, compliance	Acceptance as a viable job creation mechanism to be supported holistically, e.g. capacity, finance, compliance	Acceptance as a viable job creation mechanism to be supported holistically, e.g. capacity, finance, compliance
	2. Segmented approach	Better alignment between SMMEs and products, services and initiatives	Better alignment between SMMEs and products, services and initiatives	Better alignment between SMMEs and products, services and initiatives	Better alignment between SMMEs and products, services and initiatives
II. Identification, registration and onboarding	3. Pre-registration	Access to a unique identity usable across providers and platforms	Access to a unique identity usable across providers and platforms; Increased access to various formal services, e.g. finance, business development services, coaching, etc.	Access to a unique identity usable across providers and platforms; Increased access to various formal services e.g. finance, markets, business development support; First step towards formalisation	Access to a unique identity usable across providers and platforms; Increased access to various formal services, e.g. finance, business development services, coaching, etc.
	4. Registration and licensing			Registration and licensing process integrated and streamlined for those that wish to register/formalise; immediate verifiability by FSPs for services	
	5. Update laws and regulations	Formal recognition for those who pre-register; eased	Formal recognition; eased compliance and access to services; use of unique business	Formal recognition; eased compliance and access to services; use of unique business	Formal recognition; eased compliance and access to services;

		compliance and access to services	identifiers across platforms and services	identifiers across platforms and services	use of unique business identifiers across platforms and services
III. Access to finance	6. Financial access points footprint	Wider access to alternative providers (MFIs), lighter KYC	Wider access to alternative providers (MFIs, CFIs, agency networks, fintechs), lighter KYC	Wider access to alternative providers (MFIs, CFIs, agency networks, fintechs), lighter KYC	Wider access to alternative providers (MFIs, CFIs), lighter KYC
	7. Credit information	-	Use of movable assets as collateral; credit history on credit bureau based on alternative data	Use of movable assets as collateral; credit history on credit bureau based on alternative data	Use of movable assets as collateral and credit history on credit bureau based on alternative data for larger agri-SMMEs
	8. Public credit support	Increased access through MFIs who access public finance	Increased access through MFIs and CFIs who access public finance	Increased access through MFIs and CFIs who access public finance; increased access to portfolio guaranteed products; access to public finance through fintech companies.	Increased access through MFIs and CFIs who access public finance; increased access to portfolio guaranteed products; access to public finance through fintech companies.
	9. Digital financial services		Access to digital platforms (from fintechs, mobile money and others) to serve customers	Access to digital platforms (from fintechs, mobile money and others) to serve customers	Access to digital platforms (from fintechs, mobile money and others) to serve customers, especially for larger agri-SMMEs
IV. Business support	10. Extend coverage of existing/create new programmes	New support programmes developed for smaller (survivalist) informal SMMEs (Segment 1 and 2)	New support programmes for smaller emerging SMMEs; for larger SMMEs, wider access to existing programmes, government procurement, and incubator initiatives	Wider access to existing support programmes; access to government procurement programmes, social protection programmes, and incubator initiatives	Wider access to new and existing support programmes; access to government procurement targets and programmes

	11. Financial, digital and business skills	Wider access to skills development programmes	Wider access to skills development programmes	Wider access to skills development programmes	Wider access to skills development programmes
V. Tax	12. Tiered taxation system	Increased knowledge of tax laws and implications for their businesses; exemption from tax most in the basic segment	Increased knowledge of tax laws and implications for their businesses; Exemption from tax for most in emerging segments and simplified tax registration and payment for others	Increased knowledge of tax laws and implications for their businesses; Simplified tax registration and payment	Increased knowledge of tax laws and implications for their businesses; Exemption from tax for some and simplified tax registration and payment for others

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