The Impact of the Business Regulatory Environment on the Level of Entrepreneurship in South Africa: An Exploratory View

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Abstract-- This paper is a review of literature on the impact of the business regulatory environment on the level of entrepreneurial activity in South Africa. The existing literature focused mainly on other factors such as lack of finance, lack of education and business skills, crime, poor infrastructure and support system, among others and their influence on the level of entrepreneurship activity in South Africa. Despite the contention that the business regulatory environment is among the chief factors hindering the desired levels of entrepreneurship activity in South Africa, there is no/little empirical evidence to support this contention. This is not to imply that the regulatory environment is not important in as far as entrepreneurial activity is concerned but it is rather a call for researchers to gather empirical evidence on this purported important factor, particularly in the South African context.

Keywords--- Business Regulatory Environment, Entrepreneurship, South Africa

I. INTRODUCTION

With high levels of unemployment and poverty in South Africa, entrepreneurship has been recognised as the most effective way to address these problems [5], [6], [12]. Therefore, efforts to promote entrepreneurship in South Africa should be considered to be of critical importance. Among other factors, restrictive legislative and regulatory conditions are often viewed as critical constraints on the access of potential entrepreneurs into the business sector, and as obstacles to their growth [1]. There is therefore a need to critically examine the business regulatory environment in South Africa to assess its impact on the level of entrepreneurial activity. The Global Entrepreneurship Monitor (GEM) surveys from 2002 to 2011 reviewed that the level of entrepreneurship as measured by the Total Entrepreneurship Activities (TEA) rate in South Africa is very low compared to other developed and developing nations (12). In 2011, South Africa TEA rate of 9.1% was significantly low as compared to other BRICS countries, Brazil and China with 14.9% and 24% respectively.

With such a level of entrepreneurship, there is a need for a critical examination of the purported factors leading to such low levels. Simrie [12] revealed that 70.3% of experts interviewed cited government policies as a key constraint to entrepreneurial activity in South Africa.

Government policies form part of the business regulatory and policy environment. It is the task of policy makers, researchers and academics among others to identify gaps and to come up with recommendations to improve the business regulatory environment such that it promotes the much needed increase in the level of entrepreneurship in South Africa. Also given the enormous benefits of entrepreneurship in terms of reducing unemployment and alleviating poverty in South Africa, there is a dire need to create an entrepreneurship enabling environment.

Despite revelations by several studies [12], [6], [20] that the business regulatory environment is not supportive to entrepreneurship, there is little empirical evidence for South Africa to support this contention. Furthermore, none of these studies have attempted to identify and critically examine the specific factors within the business regulatory environment that hinder entrepreneurship in South Africa.

Several studies [5], [6], [12], [19] attempted to find solutions to other factors such as low levels of education, lack of access to finance, lack of or limited access to the necessary resources, poor infrastructure etc; and a little has been said about the business regulatory environment. It is paramount to note that even with availability of resources, skills and infrastructure, without addressing issues within the business regulatory environment, the much needed improvement in entrepreneurship may not be achieved.

The regulatory environment is a controlling element for business to legally and freely function [17]. Studies [8], [12] which mentioned the business regulatory environment as a constraining factor to entrepreneurship could not go much deeper into the roots of the problem. In this study the business regulatory environment will be thought of in terms of legislation, political and administrative factors that have an influence on businesses. Consequently, the role that business and corporate laws play in the formation, growth and transition of small-entrepreneurial ventures need to be investigated [17].

II. RESEARCH PROBLEM

Global Entrepreneurship Monitors (GEM) surveys from 2002-2011 revealed consistently low levels of entrepreneurship activities in South Africa [12]. The surveys also revealed that the level of entrepreneurship in South Africa is significantly low compared to the average of all the nations which participated in the GEM surveys in 2011. In a study, Rogerson [9] opines that in sub-Saharan African countries there is no overall scarcity of entrepreneurs, therefore there is
a need to create an entrepreneurship enabling environment in order to tap into enormous benefits brought in by new businesses in the form of job creation, poverty alleviation and economic growth. Several factors such as lack of financial support, education and training, government policies and programmes, economic climate, among others were cited as the reason for low entrepreneurial activities in South Africa [6], [12], [21]. Simrie et al. [12] further revealed that among the participating GEM 2011 countries, financial support and government policies are cited most frequently as factors constraining entrepreneurship. Economic Commission for Africa [2] also emphasizes the role of government in creating an enabling regulatory and policy environment for entrepreneurship. It [2] recommended that the regulatory and policy environment should be such that it creates a stable fiscal and monetary policy setting with sustainable interest rates, a system of financial markets that provides incentives to save, and mechanisms to channel savings into investments. Furthermore, policies that minimise the cost of business licensing and registration while at the same time safeguarding public interests and policies that facilitate business transactions such as infrastructure development, were recommended. In another study, Porteous [8] recommended assessing the impact of all new legislation to ensure that the costs and complexities of registration for new businesses are not increased by new legislation. Strengthening new business lobby groups and national audit of legislation affecting or constraining small businesses was also recommended [8]. An analysis of these recommendations point out that all other factors purported to be the reasons for low entrepreneurship activities in South Africa hinges on the business regulatory and policy environment. These need to be investigated in the South African context.

Simrie et al. [12] portrayed that the business regulatory environment is one of the major constraints to entrepreneurship in South Africa. It also plays a pivotal role in increasing the level of entrepreneurship. Among the BRICS countries (Brazil, Russia, India and South Africa) a 28% increase in Brazil’s entrepreneurship activities between 2006 and 2011 is attributed to its well-managed government policies to stimulate and support the development and growth of businesses, as well as numerous business policy reforms that have focused on making it easier to start businesses [12]. These show the importance of the business regulatory environment in increasing entrepreneurial activities of a nation.

The importance of the entrepreneurial environment as a stimulus to entrepreneurship should therefore not be underestimated. Furthermore, among the recommendations to improve entrepreneurship activities provided in the GEM 2011 South Africa’s report [12] was the need for an overhaul of the business regulatory environment. Therefore, this study recommends a critical examination of the business regulatory environment in South Africa so as to make it more favourable and more supportive to entrepreneurship.

III. RESEARCH QUESTIONS

Despite pointing out the business regulatory environment as one of the major constraining factor on entrepreneurship in South Africa, with exception of expert opinions, there is no sufficient empirical evidence to substantiate on that claim. Furthermore there is a failure to pinpoint the exact factors within the business regulatory environment affecting the level of entrepreneurship in South Africa. The fundamental questions therefore arise:

i. Are the claims that South Africa’s business regulatory environment does not promote entrepreneurship, valid?
ii. What factors within the business regulatory environment are constraining the levels of entrepreneurship in South Africa?
iii. What are the key features of the business regulatory environment in South Africa?
iv. What are the gaps in the business regulatory environment which need to be closed to improve the level of entrepreneurship in South Africa?
v. How best can South Africa fine tune its business regulatory environment to favour the much needed improvement in the level of entrepreneurship?

IV. AIM OF THE STUDY

The aim of this study is to stimulate and promote empirical debate on the business regulatory environment and its impact on entrepreneurship in South Africa. This is intended to ensure that improvements to the business regulatory environment promote entrepreneurship in South Africa.

A. The importance of entrepreneurship and challenges facing entrepreneurs

The importance of entrepreneurship and new businesses in particular is well-documented the world over as it makes significant contributions in addressing socio-economic problems such as unemployment, poverty, income inequalities, political stability and economic growth among others [1], [10], [16]. There is a general agreement in both developed and developing countries that the full potential of entrepreneurship is not being achieved in attempts to solve these problems [22]. In a study, Rogerson [10] proposed the need for specific policy interventions which are designed to enhance the successful survival and growth of small business more especially in light of the structural difficulties in the business environment. As a result, a lot of discussions and research [3], [5], [6], [12], [22] have been conducted on the factors impeding entrepreneurship in South Africa and other developing and developed countries. Several factors emerged as causes of low entrepreneurship and failure of new businesses, and these include lack of access to infrastructure, lack of access to finance, low managerial and business skills, crime, corruption and an unsupportive business regulatory environment [12] to mention just a few. In a study by Simrie et al [12] government policies was ranked high in terms of expert opinions on the factors impeding entrepreneurship in South Africa. For more than two decades these factors were investigated by researchers, academics, scholars, policy makers, to find solutions to improve the level of entrepreneurship in South Africa. However, despite all these attempts, South Africa’s level of entrepreneurship on average remain unsatisfactorily low [12], [19] and there is high failure
rate of new businesses [19]. Inspite of the low levels of entrepreneurship, South Africa was ranked number 28 on the list of top 30 economies consisting mainly of developed countries, on ease of doing business [13], which make paradoxical.

B. Impact of the business regulatory environment

There is a general agreement among several scholars that the business regulatory environment is among the chief factor impeding the growth and survival of SMEs is in South Africa [12], [19]. However, some studies portray a different picture. For example, in 2012 on a regional ranking, South Africa ranked 2nd after Mauritius and was ranked 36 on the all-rounder world ranking in terms of ease of doing business (regulatory restrictions). In terms of starting a business in particular, South Africa was ranked number 44 [14]. This is an indication that South Africa has a promising potential of becoming one of the leading economies in the world. This is also to challenge the authenticity of claims that South Africa’s business regulatory environment is among the most pressing obstacles to entrepreneurship. It is however important to note that to make the data comparable across economies, “Doing Business uses several assumptions about the business and the procedures. It assumes that all information is readily available to the entrepreneur and that there has been no prior contact with officials. It also assumes that all government and nongovernment entities involved in the process function without corruption. And it assumes that the business is a limited liability company, located in the largest business city and conducts general commercial or industrial activities” [14]. These assumptions may yield misleading results more particularly among small businesses which comprise the bulk of entrepreneurial activity in the South African context. Furthermore, World Bank and International Finance Corporation [14] pointed out that higher rankings do not necessarily imply better legislation and this discredit the reliability of such rankings. Moreover, the source of their data and information, that is experts’ opinions (14), may window-dress the information portraying a wrong impression on the matter at hand. Furthermore, it was revealed [14] that the surveys are restricted to limited liability companies and are not more concerned with the representative samples since it is not a statistical survey, thus the data is not generalizable to the whole of South Africa, more specially to the calibre and majority of entrepreneurship in the country. The most reliable sources of information are the entrepreneurs and potential entrepreneurs themselves. Therefore it remains necessary to investigate the loopholes in the business regulatory environment in order to make recommendations that aid in increasing the level of entrepreneurship in South Africa.

It is apparent that there are obstacles in the business regulatory environment that impede entrepreneurship in South Africa, however their extent and magnitude is yet to be investigated adequately. Venter, Urban and Rwigema [18] pointed out that arbitrary enforcement and erratic administration laws act as barriers to new venture creation and hence to entrepreneurship. It was further argued [18] that the more complex the procedure of registration or licensing a new business, the easier it is for governmental bureaucrats to abuse their power and impose their own discretion and complications for a new entrepreneurial venture. This is to argue that the problems in the business regulatory environment go beyond just mere laws and policies to further involve the associated criminal activities and corruption by political and other administrators. The influence of business regulatory environment can also go beyond the features of the regulation itself to include the procedural rules of the regulatory agency responsible for implementing the regulation.

Luthans, Stajkovic and Ibrayeva [7] further asserts that the political and administrative discretion not only invites corruption but also generates uncertainty, making it difficult for potential entrepreneurs to plan and also leaves individual and property rights less secure. Such activities increase the risk associated with pursuing entrepreneurial activities and the risk factor is among the many reasons why several potential entrepreneurs are hesitant to pursue their dreams. This is a major deterrent factor to entrepreneurship.

South Africa has embarked on more important regulatory reforms to make it easier for potential entrepreneurs to start businesses. For example, in 2011 South Africa removed the requirement that entrepreneurs have to obtain legal assistance or have their incorporation documents notarized in the amendments to the Companies Act of 2008 [14]. Some of the changes include; less administration or red tape when registering a business, reduced financial reporting requirements for small businesses, enhanced protection for minority shareholders, introduction of a business rescue scheme, and provisions have been made for the early turnaround of businesses in financial trouble. This will prevent companies going into major judicial management and also help to save jobs. These amendments also allow electronic submission of documents and publication, easing business start-up. Furthermore, in 2012 South Africa made starting a business easier by implementing its new company law, which eliminated the requirement to reserve a company name and simplified the incorporation documents [14]. It remains to be seen however as to whether these reforms are significant and sufficient enough to increase entrepreneurship in the country.

There is on-going concern that some regulations, rules, and government policies place a disproportionate burden on small businesses and entrepreneurs [17]. Further concerns are based on the argument that some of the regulatory reforms that are intended to support small businesses and entrepreneurship may not achieve the intended outcomes. Moreover, Dixon et al [17] further argued that the desire to support small businesses and entrepreneurship through regulatory reforms may come into conflict with the reason why the regulations were passed in the first place. For instance, most regulations were developed out of the concern about the effects of businesses on the society at large; this may be compromised out of the concern to increase entrepreneurship. This needs to be investigated in the case for South Africa.

Dixon et al. [17] further questions the effects of special regulatory treatment on small businesses and new entrepreneurs. Questions raised include:

- Why and under what circumstances does special regulatory treatment for small businesses occur?
• Why does it take the specific form it takes?
• What objectives are it designed to serve, and how effective is it in achieving these objectives?

These are also critical questions which need to be answered about South Africa’s business regulatory environment. Dixon et al. [17] further assert that there is little quantitative evidence to demonstrate the specific impacts of policies and regulations on entrepreneurs; nor has there been much evidence showing whether rules and exemptions designed to benefit small businesses and entrepreneurs actually have that effect. Despite lack of empirical evidence, challenges in the business regulatory environment continue to impede entrepreneurship in both developing and developed economies [2], [3], [5].

V. CONCLUSION

Despite the richness of literature concerning challenges facing new businesses in South Africa, there is a lack of depth in many studies, particularly on the factor, business regulatory environment. Thus there is a need for empirical investigations to determine the extent and depth of this factor in as far as its implications on entrepreneurial activity and success is concerned. Furthermore, regulatory reforms to strengthen the entrepreneur are necessary if the country is to achieve the much need increase in entrepreneurial activity levels and ultimately employment creation, poverty alleviation and sustainable economic growth.

Consequently this paper calls for the need to identify and critically examine the loopholes in South Africa’s business regulatory environment and come up with recommendations to improve it in order to create an entrepreneurial enabling environment in the country. This mean a critical examination of each piece of business legislation and policies in South Africa to establish their influence on entrepreneurship and finally with the aid of empirically investigations recommend changes to promote and support entrepreneurship in South Africa.

REFERENCES