

# Promoting economic development & capacity through procurement

Presentation to the 3<sup>rd</sup> Annual Tshwane International Trade and Infrastructure Investment Conference  
CSIR ICC  
24 May 2010

Dr. Miriam Altman  
Executive Director  
Centre for Poverty, Employment & Growth  
HSRC  
[maltman@hsrc.ac.za](mailto:maltman@hsrc.ac.za)

Social science that makes a difference



# Why procurement?

- The expansion of the base of small and medium size enterprise will be an important contributor to employment creation
- In an economy dominated by large corporates and government, small business entry is a challenge
- Leveraging private and public buying power (or procurement) to stimulate entry, competition and expansion of SMEs is critical strategy

# Value creation

- Currently, the main policy drive is towards black empowerment
- Economic representation is critical objective
- However, concern that this does not always lead to value creation and employment – which are critical to sustainable broad-based empowerment

# Tshwane Metro – HSRC Partnership

- The HSRC has established a programme of work focusing on identifying, testing and sharing procurement practices that are value-adding and employment promoting
- Tshwane Metro would like to see local economic development stimulated by private and public procurement
- The HSRC and Tshwane have come together in a long term partnership to benefit growth, job creation & competition in Tshwane Metro area

# Achieving potential

## Key Questions:

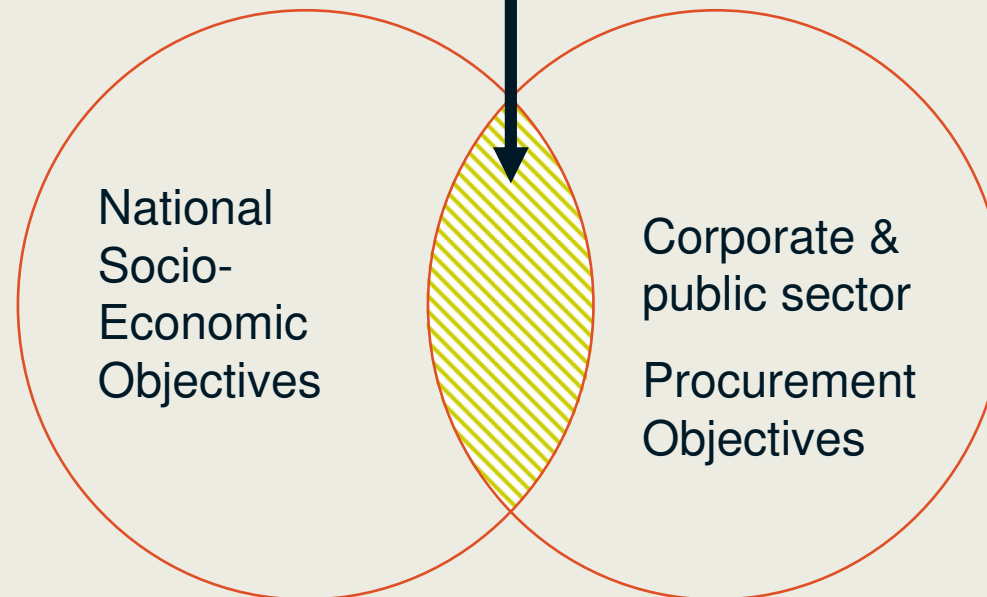
1. What is the size of the potential contribution that corporate procurement can make to national socio-economic objectives?
2. Is it anywhere near achieving its potential?
3. What needs to be done to realise its full potential?
4. To what extent is realising the potential a function of the regulatory and policy environment vs. knowledge, capacity and management approaches?

## Three key assumptions are:

1. There is still substantial unmet potential, and also substantial willingness to do so
2. Meeting potential will require attention to policy, but also management and organisational practices and capacities
3. As knowledge and capacity improve so too will policy and practice




















# Aligning interests

The contribution of corporate & public sector procurement to national socio-economic objectives



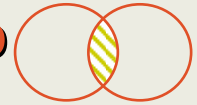
The focus is on developing and disseminating a knowledge base of procurement practices to grow this contribution

## National Socio-Economic Objectives and Primary Areas of Emphasis of Government Policies

Socio-Economic Challenge	Key Policy Objective	RDP	ASGISA	BBBEE Act, Codes and Charters	NIPF	CSDP
Unemployment and Poverty	Economic Growth					
	Job Creation					
	Industrial Development					
Unemployment, Poverty, and Racial and Gender Inequality	Skills Development					
Racial and Gender Inequality	BBBEE					

**Even though the policy environment changes, the core policy objectives remain.**

# Possible Contributions of Corporate Procurement to Socio-Economic Objectives



Socio-Economic Objectives	Corporate Procurement Objectives	<i>Only ways to meet BOTH corporate procurement and socio-economic objectives</i>
<ul style="list-style-type: none"> <li>• Economic Growth</li> <li>• Job Creation</li> <li>• Industrial Development</li> <li>• Skills Development</li> </ul>	<ul style="list-style-type: none"> <li>• Optimise Total Cost of Ownership</li> <li>• Quality</li> <li>• Security of Supply</li> <li>• Responsiveness</li> <li>• Reliability</li> <li>• Lower inventory and lead times</li> <li>• Innovation</li> <li>• Sustainability (increasing socio-economic stability)</li> </ul>	<ul style="list-style-type: none"> <li>• Replacing imports in upstream supply chain with competitive local suppliers</li> <li>• Increasing competitiveness of supplier base and supply chain leading to:                             <ul style="list-style-type: none"> <li>• growth of industry and hence suppliers</li> <li>• increased exports by suppliers</li> </ul> </li> <li>• Stimulating new enterprises downstream (creating forward linkages)</li> </ul>
<ul style="list-style-type: none"> <li>• BBBEE</li> </ul>	<ul style="list-style-type: none"> <li>• Sustainability</li> <li>• Improved brand with stakeholders</li> <li>• Access to public and private sector markets through BBBEE compliance</li> </ul>	<ul style="list-style-type: none"> <li>• Increase proportion of spend going to competitive BEE suppliers</li> </ul>

## NB:

- **The most that corporate procurement can do is to create conducive conditions for the growth of targeted suppliers. It is up to the suppliers to take advantages of these conditions**
- **Corporate procurement will always focus on its core objectives, thus it is unrealistic to expect corporate procurement to create more than the conducive conditions.**



# Categorisation of Corporate 'Socio-economic' Procurement Practices

Category	Description	Examples of Activities
Enterprise and Supplier Development	<ul style="list-style-type: none"> <li>Financial or non-financial support to potential or existing suppliers to assist them to establish, grow and/or become more competitive. <i>(For enterprise development, the emphasis is on BEE suppliers)</i></li> </ul>	<ul style="list-style-type: none"> <li>Finance in the form of equity or loans</li> <li>Training and Mentoring</li> <li>Technology transfer</li> <li>Management advice and services</li> </ul>
Preferential / Targeted Procurement	<ul style="list-style-type: none"> <li>Providing preference to certain categories of suppliers in the supplier selection process</li> </ul>	<ul style="list-style-type: none"> <li>Preferential Points System in Adjudication Process</li> <li>Set asides for certain categories of suppliers</li> <li>Mandatory or incentivised sub-contracting for certain categories of suppliers</li> <li>Contractual obligations to meet certain socio-economic targets</li> </ul>
Strategic Sourcing	<ul style="list-style-type: none"> <li>Selection and application of procurement strategies and tactics based on a thorough analysis of internal needs, supplier markets and demand markets</li> </ul>	<ul style="list-style-type: none"> <li>Total Cost of Ownership Analysis</li> <li>Industry Value Chain Analysis</li> <li>Internal spend analysis and long term planning                             <ul style="list-style-type: none"> <li>– Consideration of impact of procurement on supplier markets</li> <li>– Interrogation of business requirements (e.g. gold plating)</li> </ul> </li> <li>Collaborative value adding partnerships with suppliers</li> </ul>

**NB: All 3 of these practices can be used to achieve any or all of the socio-economic objectives**

## Sample of Corporate Preferential Procurement Practices\* Illustrating Diversity of Corporate Responses to Policy Objectives (1/2)

Programme	Brief Description	Main Socio-Economic Objective	Category of Procurement Practice
saibl Enterprise Linkages Initiative	<ul style="list-style-type: none"> <li>Assists corporations to jointly develop and share knowledge, experience and practices to promote supplier diversity through sustainable procurement, supplier development, access to a database of competitive black suppliers.</li> </ul>	<ul style="list-style-type: none"> <li>BBBEE</li> </ul>	<ul style="list-style-type: none"> <li>Enterprise and Supplier Development</li> <li>Preferential / Targeted Procurement</li> </ul>
Eskom - ASGISA	<ul style="list-style-type: none"> <li>Application of preferential procurement to achieve defined developmental outcomes through procurement</li> </ul>	<ul style="list-style-type: none"> <li>BBBEE</li> <li>Skills Development</li> <li>Job Creation <i>(through local content)</i></li> </ul>	<ul style="list-style-type: none"> <li>Preferential / Targeted Procurement</li> </ul>
Eskom - CSDP	<ul style="list-style-type: none"> <li>Contributes to improving the competitiveness, capability and capacity of Eskom's local supplier base</li> </ul>	<ul style="list-style-type: none"> <li>Industrial Development</li> <li>Economic Growth</li> </ul>	<ul style="list-style-type: none"> <li>Strategic Sourcing</li> </ul>
PPC Ntsika Pty Ltd	<ul style="list-style-type: none"> <li>A company established by PPC to assist enterprises and entrepreneurs to grow their businesses and achieve operational and financial independence.</li> </ul>	<ul style="list-style-type: none"> <li>BBBEE</li> </ul>	<ul style="list-style-type: none"> <li>Enterprise and Supplier Development</li> </ul>

## Sample of Corporate Preferential Procurement Practices (2/2)

Programme	Brief Description	Main Socio-Economic Objective	Category of Procurement Practice
Sasol – SIYAKHA	<ul style="list-style-type: none"> <li>Develops, funds and grows sustainable local medium sized BEE suppliers for Sasol, especially in commodities or services where the market would not produce such enterprises</li> </ul>	<ul style="list-style-type: none"> <li>•BBBEE</li> </ul>	<ul style="list-style-type: none"> <li>• Enterprise and Supplier Development</li> <li>• Preferential / Targeted Procurement</li> </ul>
Sasol ChemCity	<ul style="list-style-type: none"> <li>A wholly owned subsidiary of Sasol Chemical Industries, acts as a business incubator to facilitate the establishment of independent SMME's in the downstream chemical and related sectors</li> </ul>	<ul style="list-style-type: none"> <li>• Job Creation</li> <li>• BBBEE</li> </ul>	<ul style="list-style-type: none"> <li>• Enterprise and Supplier Development</li> </ul>
McCarthy Owner Driver	<ul style="list-style-type: none"> <li>Assisting formerly employed drivers to establish, run and grow new delivery enterprises using McCarthy as a launch customer</li> </ul>	<ul style="list-style-type: none"> <li>• BBBEE</li> </ul>	<ul style="list-style-type: none"> <li>• Enterprise and Supplier Development</li> <li>• Preferential / Targeted Procurement</li> </ul>
De-Beers Preferential Sourcing Programme	<ul style="list-style-type: none"> <li>Integration of preferential procurement practices in main stream procurement</li> </ul>	<ul style="list-style-type: none"> <li>• BBBEE</li> </ul>	<ul style="list-style-type: none"> <li>• Preferential / Targeted Procurement</li> <li>• Strategic Sourcing</li> </ul>

**Whilst enterprise development programmes tend to be well publicised, corporates also pursue preferential procurements as per the BBBEE scorecard. In fact, some corporates with enterprise development programmes score more highly on preferential procurement than on enterprise development.**

# The influence of legislation

1. There is predominant **focus on BBBEE** amongst private sector corporates:
  - Few corporates place an emphasis on local content and local supplier development
    - Could be failing to tap into the job creation potential of established local suppliers as well as possible commercial benefits of local supply
2. Eskom, which is state owned and hence more responsive to government's more general policy directives, is also seeking to achieve industrial development goals through procurement
3. Regulatory environment is **encouraging corporates to identify** products and services which were previously considered '**out of bounds**' for preferential procurement
  - '*Out of bound*' products and services were perceived to be too risky to switch suppliers, let alone BEE suppliers
  - Availability of '*low hanging fruits*' or '*quick wins*' to help corporates enhance their BBBEE recognition levels has diminished
  - Low hanging fruits were perceived to be of relatively low value and low risk and had an abundance of BEE suppliers due to low barriers to entry both in terms of capital and technical knowledge

# The influence of industry structure

The firm's **industry structure**, type of sourced products and services, and the governance structures within the industry have played a key role in influencing the strategies and tactics adopted by firms:

- McCarthy has a very limited addressable spend, whereas entities like Eskom, PPC, De Beers and Sasol with less restrictions have been able to develop strategies to pursue multiple opportunities
- Eskom has to impose local supplier development conditions in the contracts that it enters with its global first tier suppliers

## Industry governance in capital intensive sectors

- First tier supplier industries are global and concentrated (i.e., 3 to 5 global players per product category)
- Each global player controls access to their supply chains and to a limited extent access to the related after sales maintenance, repairs and overhaul (MRO) markets
  - This is done through the standards and accreditation processes they impose on suppliers
- Therefore any related supplier development has to be linked to these global first tier players

# Convergence between Preferential Procurement and Enterprise Development

1. Increased convergence between preferential procurement and enterprise development activities will become a necessity as corporates seek to improve their preferential procurement and enterprise development BBBEE scores
  - Firms already prefer to develop suppliers within their supplier chains ( e.g., Siyakha and PPC)
  - Will optimise commercial benefits for firms and increase employment creation
2. Greater emphasis should be placed on providing **sophisticated technical support** (i.e., assistance in industrial process, technology and product upgrading)
  - Enterprises supplying previously “*out of bound*” products and services will need more sophisticated support
  - Facilities or market entry paths to test and develop new products will be needed where products need to be prequalified and / or compete with established brands
3. Enterprise development programmes and preferential procurement programmes must be aligned without compromising the **commercial objectivity** required of procurement practitioners
  - Lessons from MNC which develop suppliers in their core supply chains
  - Presence of an integrated supplier management framework (e.g., DBCM partnership with saibl, relationship between PSM and Siyakha) is useful

# Integration of Socio-Economic Objectives into Core Procurement Policies and Practices

The maturity of the corporates' **strategic sourcing and supplier relationship management practices** is a key enabler of the successful pursuit of preferential procurement targets:

- Both Eskom and DBCM have embedded their preferential procurement activities within existing strategic sourcing methodologies
- Embedding allows procurement practitioners to:
  - Identify and define commodity sourcing strategies which allow for the participation of BBBEE or local suppliers
  - Objectively and holistically assess risk
  - Challenge prejudices and organisational cultural barriers to trying out new suppliers
  - Ensure that preferential procurement objectives are realised in a manner which is commercially sustainable
  - Provides access to opportunities in core supply chains, as opposed to focusing on peripheral areas of supply, such as catering

# Targeting Total Discretionary Procurement Spend

1. The **legislative environment needs to change** so that corporates are obligated / rewarded for using their total procurement expenditure (including the imported component) to achieve developmental outcomes
  - The BBEE codes excludes the imported components
  - CSDP and NIPP force SOE and their first tier suppliers to look at their total spend
2. Corporates will need to **engage with the foreign suppliers** to identify mechanisms to increase the participation of local enterprises in the supply chains
  - An understanding of how the supply chains of their foreign suppliers are structured and governed will be crucial
3. Corporates will need to **contribute to overcoming the market failures** to localisation e.g.,
  - Eskom experience of sharing information with suppliers, aggregating demand with other buyers, improved planning, procuring fleets of equipment, using TCO rather the purchase price to evaluate tenders, avoid gold plating



# Our initial recommendations

1. The Codes of Good Practice should be reviewed to:
  - Create stronger link between preferential procurement and enterprise development
  - Put in place stronger incentives for firms to engage in supplier development within their own core supply chains
  - Place a greater emphasis on utilising a corporate's total procurement spend, including its imports, for developmental purposes:
    - Recognise efforts to develop all local suppliers
    - Recognise efforts to replace currently imported inputs with locally sourced inputs
2. Corporate seeking to leverage their entire procurement spend, especially the import component, should collaborate with other buyers and devise strategies to overcome market failures to localisation
3. Need for forums that support knowledge sharing between procurement practitioners and senior managers
  - Many firms are still in a learning phase
  - Need for research and tertiary institutions to build a knowledge base

# Activities in Tshwane – HSRC partnership Phase 1

- Baseline assessments:
  - Institutional and policy review
  - Company case studies – private and SOEs
    - Sasol – SIYAKHA & Sasol ChemCity
    - De-Beers Preferential Sourcing Programme
    - McCarthy Owner Driver
    - Eskom – CSDP and Asgisa
  - Review of ‘best practices’ in municipal procurement nationally
  - Review of potential impact that Tshwane procurement practices could have on LED. Recommendations on how to move forward to achieve this potential.
    - Initial thoughts on waste collection, construction contracting, and operational expenditures (eg clothing, paper, cleaning, furniture etc)
- Knowledge network established

# Activities in Tshwane – HSRC partnership Phase 2

- Optimising Tshwane Metro procurement to impact on local economic development
  - Increase the participation of Tshwane based suppliers in the supply chain of Tshwane Metro
- Deepen Tshwane based suppliers access to large corporates operating within TMM boundaries
- Build knowledge network