



*competition*commission  
south africa

# **OIPMI PROVISIONAL REPORT**

## **CHAPTER 8**

### **GENERAL FUNDING**

# Table of Contents

|                                             |    |
|---------------------------------------------|----|
| 1. Introduction.....                        | 1  |
| 2. Venture Capital Industry.....            | 1  |
| 3. VC Funding and Focus.....                | 4  |
| 4. Incubators and Accelerators.....         | 7  |
| 5. VC Investment into HDP owned firms ..... | 9  |
| 6. Public Sector Funding .....              | 13 |
| 7. Appendix .....                           | 16 |

## List of Tables

|                                                                         |    |
|-------------------------------------------------------------------------|----|
| Table 1: Total investment in relevant sectors by investment stage ..... | 5  |
| Table 2: Percentage of black owned companies funded in 2020 .....       | 11 |
| Table 3: Percentage of female owned companies funded in 2020.....       | 12 |

## List of Figures

|                                                 |   |
|-------------------------------------------------|---|
| Figure 1: Contribution by stage of deal .....   | 6 |
| Figure 2: Source of funds for VC managers ..... | 6 |

## List of Graphs

|                                                                               |   |
|-------------------------------------------------------------------------------|---|
| Graph 1 Total investment in relevant Sectors split by stage of business ..... | 7 |
|-------------------------------------------------------------------------------|---|

## 1. Introduction

1. One of the four broad focus areas and public interest concerns outlined in the Inquiry's Term of Reference<sup>1</sup> are market features that *"may negatively impact on the participation of Small to Medium sized enterprises ("SME" s) and Historically Disadvantaged Persons ("HDPs")* in the online economy. Section 43C(2) of the Act<sup>2</sup> mandates that the Inquiry, in making its decision have regard to market features, that may impact or adversely affect the participation of SMEs and HDP owned firms in the online economy.<sup>3</sup> The preceding platform category chapters provide an assessment and findings in respect of specific features of those platform markets that may hinder SME and HDP participation at either the platform level or at the business user level.
2. However, in respect of the platform level, it was apparent that there was a cross-cutting issue of access to Venture Capital ("VC") funding for startups, both to establish themselves and then fund growth.<sup>4</sup> Furthermore, it soon became apparent that the funding challenge was peculiarly acute for HDP entrepreneurs seeking to enter the platform markets. For this reason, the Inquiry solicited submissions from the VC industry and government departments around the levels and approach to funding of tech startups in South Africa more generally, and specifically in relation to intermediation platforms. This chapter reports on the provisional findings of the inquiry in relation to funding.

## 2. Venture Capital Industry

3. Tech startups typically fall within the realm of VC funding rather than typical bank funding for businesses. This is because they are higher risk as they involve innovation that requires specialist skills to assess. As one VC fund stated, the VC landscape pursues *"...financing that investors provide to businesses, in the start-up and early growth phases [of a business] ...this funding deals predominantly with start-ups or small businesses who have no access to capital markets..."*.<sup>5</sup>

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<sup>1</sup> OIPMI Terms of Reference, 9 April 2021

<sup>2</sup> Competition Act 89 of 1998

<sup>3</sup> OIPMI, Statement of Issues, 19 May 2021

<sup>4</sup> Stakeholders have also raised the issue of developing tech skills and the role of tech education to enhance start-up entry, especially HDP entrepreneurs. However, this is a very broad economic environment issue and well beyond the scope of the Inquiry.

<sup>5</sup> Naspers Foundry, WS1, page 2

4. Venture Capital funding can be an essential source of financing and mentorship for start-ups and small businesses that have the potential to generate high rates of growth and returns, with support and backing. The online economy can be a catapult for rapid growth for start-ups and small businesses as seen in other jurisdictions. VC funds fulfil a unique function in the investment marketplace because they are actively involved in growing companies, alongside the founders. VC investors help the business become successful by providing a combination of capital and strategic know-how. The fund managers themselves work closely with the company they have invested in to support it. It is important to understand the VC landscape and how it can be a tool to affected transformation and change in online markets.
5. There are multiple stages of VC investments, each with their own objectives:
  - 5.1. Pre-Seed funding The first phase is called *pre-seed funding*: this stage of funding typically refers to the period when the company's founders are first starting their operations. The most common "pre-seed" funders in this category; are the founders themselves, or close friends, and family, essentially, called "angel investors".<sup>6</sup> Depending on the nature of the company and the initial costs involved with developing the business idea, this stage of funding can happen quickly, or it may take some time. It is also likely that investors at this stage are not making an investment in exchange for equity in the company, and so this stage, according to investors, is the riskiest of all the stages.
  - 5.2. Seed Funding The next stage of funding represents the first official money that a business venture or a company raises. With seed funding, a company has assistance from its investors in determining what its final products will be and who its target market is. Seed funding is also used to build a team that would steer the mandate of the investors and the company itself.<sup>7</sup>
  - 5.3. Series A Funding Series A funding occurs once the company is 'post-revenue', i.e. has developed a track record (i.e., an established user base, consistent revenue figures, or some other key performance indicator). The purpose of Series A funding in order to further optimise the company's user base and product offering, as well as to explore opportunities to scale the company's products across different markets. In this stage of funding, it is important for investors of the company to have a plan for developing a business model that will generate long-term profits. Seed start-ups often have good ideas that generate substantial amounts of enthusiastic users, but the

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<sup>6</sup> SAVCA, OS1, page 6

<sup>7</sup> Naspers Foundry, WS1, page 3

founders at this stage normally do not know how to monetise this user base. So, the investors can be a support for the Seed start-up to develop a business model that will monetise its user base for long-term profits.<sup>8</sup>

5.4. Series B Funding Series B stage funding involves investors moving a company past the developmental stages, to expanding its market reach. According to investors, at this stage, a company that's already moved past the first 3 stages of funding already has developed a substantial user base and therefore has already proven it can scale. Series B phase funding is used by investors to essentially scale.<sup>9</sup>

5.5. Series C Funding At this stage, investors will optimise a company that can meet its user base demands and they will help the company develop new products and expand into new markets, or even acquire other companies. In the Series C phase, investors inject capital into the business to receive more than double the returns and is focused strictly on scaling quickly.

6. The stages of VC funding set out above illustrate the ongoing process of support that is required for growth of a startup into a sizeable company and effective competitor. The first two phases of funding (seed funding) are important as it provides the initial start-up capital for a startup to enter the market and generate revenue. Once the start-up or small business overcomes the seed phase, investors can work alongside the business from the beginning to assist it achieve its desired growth. VC fund managers actively support the company in its growth, in addition to the initial capital investment.<sup>10</sup> The VC brings experience in scaling, accessing markets and connections for the small business, which it would otherwise not be able to without the kind of VC support.<sup>11</sup> Some startups do not go through multiple rounds of funding if their business does not meet the criteria for further rounds of funding, and funding ultimately is determined by the investors' appetite to take risk.<sup>12</sup>
7. A VC fund will raise funding from institutional and private funders, and will be given a mandate by the firms. The broad mandate around the VC firm's investment strategy is to invest in high-growth companies that can scale quickly.<sup>13</sup> However, the mandates may also extend to the types of businesses and the level of risk that the funders are willing to take. Early-stage businesses are inherently seen as risky and for this reason the SA

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<sup>8</sup> Naspers Foundry, WS1, page 3

<sup>9</sup> Naspers Foundry, WS1, page 3

<sup>10</sup> SAVCA OS1, Transcript page 7 Presentation, slide 6 ("OS1")

<sup>11</sup> SAVCA, OS1, page 9. Information submitted from the South African Venture Capital Association ("SAVCA"), illustrates this significant gap. SAVCA is the VCPE industry association and public policy advocate in Southern Africa. It has about 180 members, including more than 130 VCPE fund managers and 50 advisory firms that support the industry.

<sup>12</sup> SAVCA, OS1, Transcript page 10

<sup>13</sup> Naspers Foundry, WS1, page 4, para 4.7.3

market tends to focus on the “post-revenue” stage i.e., Series A to Series C funding and not necessarily early-stage start-ups.<sup>14</sup> As such there is a gap in the domestic VC industry relative to more mature VC markets.

8. Information received from the SA Venture Capital Association (SAVCA)<sup>15</sup> indicates that most early-stage funding comes from angel investors, “...by number of deals, some of the investors that these investments and the kinds of [funders] that invest in early stage would be angel investors...so those individuals that invest in their own capacity...”<sup>16</sup> Angel investors (also known as a private investor, seed investor or angel funders) are high-net-worth individuals who provide financial backing for small start-ups or entrepreneurs, typically in exchange for ownership equity in the company. Often, angel investors are found among an entrepreneur's family, friends, and networks. Angel investors account for 21.1% of the overall investment deals made in 2020.<sup>17</sup> With Approximately 30.3 million people of the South Africa population living below the national upper poverty line, it is not difficult to realise how inequality affects access to the online economy.<sup>18</sup>

### 3. VC Funding and Focus

9. SAVCA submits that the VC industry is still relatively nascent, with just under R7bn in funds under management in 2020, compared to R205 billion in Private Equity management.<sup>19</sup> There is a lack of local institutional capital investment in South Africa, which limits the number of investments that can be concluded by a single fund manager and ultimately the total quantum of capital investments available for entrepreneurs. Furthermore, South African investment managers tend to be risk averse<sup>20</sup> and often apply private equity metrics to fund businesses at early-stage.<sup>21</sup> This means that early-stage businesses are assessed by their performance indicators instead of their potential for growth and innovation. This means that the true VC funding available is likely to be smaller than that measured.

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<sup>14</sup> Naspers Foundry, WS1, page 9

<sup>15</sup> SAVCA, W1, page 6

<sup>16</sup> SAVCA, OS1, page 6, presentation slide 3.

<sup>17</sup> SAVCA, OS1, presentation slide 4

<sup>18</sup> P. Ricci Available at: [https://databank.worldbank.org/data/download/poverty/33EF03BB-9722-4AE2-ABC7-AA2972D68AFE/Global\\_POVEQ\\_ZAF.pdf](https://databank.worldbank.org/data/download/poverty/33EF03BB-9722-4AE2-ABC7-AA2972D68AFE/Global_POVEQ_ZAF.pdf) (accesses 19 June 2022)

<sup>19</sup> SAVCA, WS1, page 1

<sup>20</sup> SAVCA, OS1, transcript page 23

<sup>21</sup> SAVCA, OS1, page 51

10. Indeed, in SAVCA's own statistics it classifies startup funding as including seed funding as well as Series A and B, and we understand that the majority of funding classified as startup is in fact Series A and B. SAVCA then classifies later stage funding as series B and C funding, with growth funding then outside of the typical VC funding categories.
11. From 2018- 2022, SAVCA reported that online intermediation investment opportunities have been focused on E-Commerce, Fintech, retailing distribution and software. Table 1 below shows the growth of investment opportunities in online markets since 2018 as well as the split across different funding stages. The total value growing by c.R250m in 2 years. Growth phase funding remains the highest investment with c.R180m in 2020, but start-up funding (seed, series A and B) is also growing rapidly at c.R165m in 2020.<sup>22</sup>

**Table 1: Total investment in relevant sectors by investment stage**

| <b>Total for all 4 sectors</b> | <b>2018</b>        | <b>2019</b>        | <b>2020</b>        |
|--------------------------------|--------------------|--------------------|--------------------|
|                                | <b>rand</b>        | <b>rand</b>        | <b>rand</b>        |
| <i>Start-up</i>                | 52 331 587         | 142 270 066        | 164 211 332        |
| <i>Later stage</i>             | 2 047 650          | 20 139 210         | 12 949 431         |
| <i>Growth</i>                  | 55 946 243         | 92 870 955         | 181 421 460        |
| <b>Total Value</b>             | <b>110 325 480</b> | <b>255 280 231</b> | <b>358 582 223</b> |

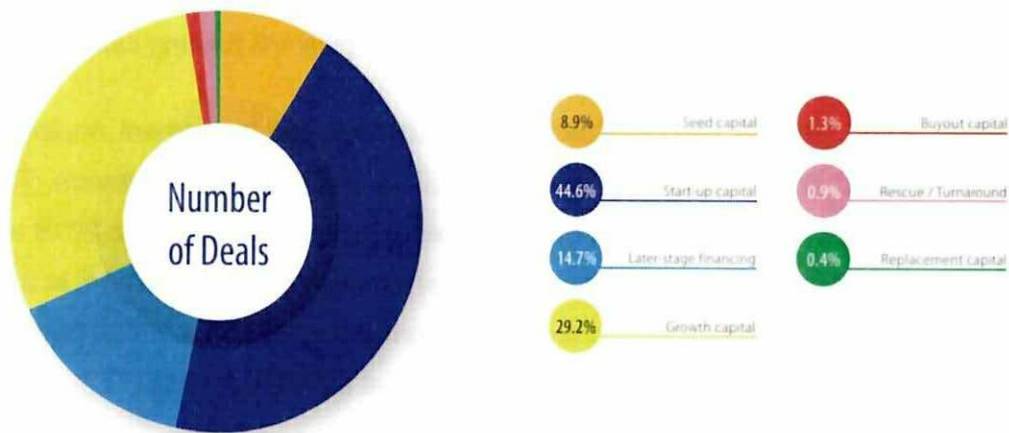
SAVCA - 2020 Annual Survey Report

12. Figure 1 provides a review of contribution by stage of deals where all deals are still invested. This separates out the seed from the other startup stages of funding and shows how significant the gap between seed phase capital investment and the next phase of growth fund managers are willing to inject in capital.

<sup>22</sup> SAVCA, WS1, page 3

**Figure 1: Contribution by stage of deal**

Contribution by stage of the deal; by number of deals, all deals still invested



13. Figures 2 below provides information on the source of funding for VC firms with Angel investors making up 21.1% of funders, but the bulk coming from independent funds. There is also a fair amount of corporate and government funding, albeit that this may be linked to the SA SME Fund discussed below.

**Figure 2: Source of funds for VC managers**

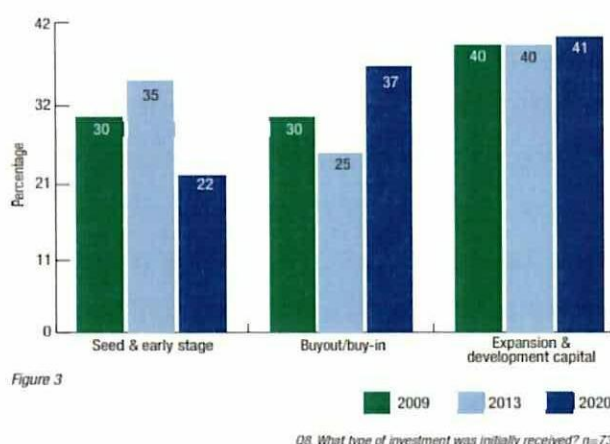
Contribution by fund manager type; by number of deals, all deals still invested



Source: SAVCA Public Hearing Presentation -dated 3 November 2021

14. Looking over a longer period, SAVCA reported that majority of investments made since 2009 have been focused on expansion and development with 41% of funding<sup>23</sup>, while there have been fewer investments made for startup.<sup>24</sup> In addition, more funding has gone into buy-in and buy-out, with less now being attributable to startup funding. This is illustrated in Graph 1 below:

**Graph 1 Total investment in relevant Sectors split by stage of business**



Source: SAVCA Annual Survey, *The Impact of Venture Capital and Private Equity in South Africa 2020*, Published February 2020

## 4. Incubators and Accelerators

15. Whilst seed funding is limited, some local and foreign VC funders or tech companies do provide assistance in the form of incubators and accelerators, even if it is not financial. An incubator or accelerator is “an organization designed to accelerate the growth and success of entrepreneurial companies through an array of business support resources and services that could include physical space, capital, coaching, common services, and networking connections...”<sup>25</sup>
16. Incubators can assist pre-seed phase businesses to develop their ideas in a manner that can see the idea develop and create some interest from VC industry funders. VC funders

<sup>23</sup> SAVCA Annual Survey, *The Impact of Venture Capital and Private Equity in South Africa 2020*, Published February 2020, page 10 (“SAVCA, Annual Survey”)

<sup>24</sup> SAVCA Annual Survey, *The Impact of Venture Capital and Private Equity in South Africa 2020*, Published February 2020, page 10 (“SAVCA, Annual Survey”)

<sup>25</sup> Business incubation programs are often sponsored by private companies or municipal entities and public institutions. Their goal is to help create and grow young businesses by providing them with necessary support and financial and technical services. <https://www.entrepreneur.com/encyclopedia/business-incubator> accessed 19 June 2022

also deliberately use programs like these to assist in the selection process of new ideas that may create future investment opportunities and to aid determining a business model able to scale and grow which is what VC investment looks for. As SAVCA indicated in the public hearing, *“Working with experts in an incubator or accelerator, a pre-seed business has a chance to realise its ideas by fully fleshing out the business, i.e., its a) suitability, b) fundability or c) both...”*<sup>26</sup> Most incubators in South Africa are linked to universities<sup>27</sup> and many are mandated to measure the quantity of entrepreneurs that participate in the programs more than the quality of the start-ups.<sup>28</sup>

17. These programmes can be an essential feature in curbing the high-risk perception by the VC industry in South Africa. Incubators can act as a source of streamlining the entrepreneurs that already have some element of traction or user base at early-stages to help them develop a value proposition that can the mitigate the start-ups’ risk.<sup>29</sup> During the Inquiry’s public hearings, held in November 2021, SAVCA submitted that there is still much more that needs to be done by the VC industry and not enough “mentorship capital”<sup>30</sup> is available for start-ups. Some of the incubators that were available a few years ago, are not available today. However, there are still a few incubators that still exist in South Africa.

17.1. One project is Grindstone, who have partnered with the SA SME Fund, Knife Capital and Google for Start-ups have produced several start-ups like OneCart, PayFast and Locum.base, SME Snapshot and many others.<sup>31</sup>

17.2. Google for Start-ups Accelerator Africa: Google offers a three-month accelerator program to technology start-ups across Africa. The accelerator provides mentorship, technical project support and workshops focused on product design, customer acquisition and leadership development. Through the Google for Start-ups Black Founders Fund Africa, Google supports early-stage Black-founded start-ups and start-ups that are benefitting the Black community on the continent through non-dilutive funding.<sup>32</sup>

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<sup>26</sup> SAVCA, OS1, Submission by Mr Keith van Zyl, dated 3 November 2021, page 21

<sup>27</sup> SAVCA, OS1, page 25

<sup>28</sup> SAVCA, OS1, page 26

<sup>29</sup> SAVCA, OS1, page 24

<sup>30</sup> SAVCA, OS1, page 20

<sup>31</sup> SAVCA, OS1, Page 24, [Grindstone Accelerator \(Thinkroom.Co.Za\)](https://www.thinkroom.co.za/grindstone-accelerator) Accessed 6 April 2022.

<sup>32</sup> Google, oral submission by Google LLC, Charles Murito, dated 3 November 2021, page 17 *“For small businesses, Google provides free guidance on setting up a Google business profile, we [Google] also have a start-up accelerator program which is a three-month program for tech start-ups across the continent. This scheme provides mentorship, technical project support and workshops focused on a number of issues including product design, customer acquisition as well as leadership development.”*

18. Given the lack of pre-seed and seed funding, the VC firms submit that there is a need for the development of innovation hubs, micro-financing, upskilling young people and the provision of adequate funding for SMEs that aim to develop online platforms.<sup>33</sup> A number of tech companies have tech education initiatives which may assist the ecosystem of developing tech entrepreneurs but are not specifically targeted at supporting specific startup businesses.<sup>34 35</sup>

## **5. VC Investment into HDP owned firms**

19. The Inquiry heard evidence from HDP entrepreneurs and the venture capitalists, including SAVCA, about the challenges for HDP start-ups. We split this between pre-seed / seed where the VC industry does not typically get too involved, and post-revenue funding where it does.

### Pre-seed and seed funding

20. Entrepreneurs at the pre-seed and seed funding stages rely on angel investors in their immediate circle of family and friends or putting up assets as collateral for debt funding given that there is no revenue source yet. The Inquiry found that a lack of wealth and asset accumulation by HDPs due to exclusion from the economy under apartheid has created a substantial barrier to accessing pre-seed and even seed funding from a family or associate 'angel investor', unlike their white counterparts. Almost without fail, the HDP entrepreneurs that came before the Inquiry had difficulties in raising sufficient funds to move their ideas forward. Whilst many HDP start-ups reached out to government funding sources, these are not focused on start-up VC funding and lack the skills to assess a tech business plan, resulting in a mixture of non-responses or applicants being informed that the agency does not fund online ventures.

21. One more successful HDP entrepreneur did point to the benefit from being included in incubators and later accelerators, as well as the exposure through these to some foreign

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<sup>33</sup> Naspers Foundry, OS1, page 8

<sup>34</sup> Naspers Submission by Webber Wentzel, Comments to SOI, page 14 - Naspers Labs is a youth development programme aimed at increasing economic participation of Historically disadvantaged communities. The programme addresses the skills gap and training needs of young people, enabling them to become productive contributors in an increasingly digitally driven economy. Although this programme is provided by the largest investment contributor South Africa, its target is mainly upskilling the young in vocational and technical skills more than funding up and coming seed businesses.

<sup>35</sup> Google play, oral submission by Google LLC, Charles Murito, dated 3 November 2021, page 17 Google stated that it has also tailored support to "historically marginalised groups", by providing grants of R7.5 million to the YES Foundation which has enabled 165 young black South Africans to take part in a yearlong placement program.

venture capital funds.<sup>36</sup> It seems that the foreign funds are more willing to take on risk and get involved at the seed stage. When the Inquiry asked SAVCA about this, they indicated that the foreign funds are more proper VC funding given the maturity of their funding markets, and that foreign funds are also looking for ideas that they can scale across other emerging markets. It also seems the SA SME Fund discussed in the next section has moved into some pre-revenue or seed funding.

22. The significant gap in investments for start-ups (pre-seed or seed phase businesses) essentially means there is a significant capital and funding barrier for access to online markets in terms of the Venture Capital industry, a critical component in accessing markets and competing within those markets for SMEs and HDP owned firms.<sup>37</sup>
23. The Inquiry finds that the industry perception that pre-seed phase businesses are inherently high risk heightens the barriers to entry for HDPs, as most, if not all HDP entrepreneurs are then forced to bootstrap for longer periods of time and have a higher risk of failing due to lack of funding and the inequality gap.<sup>38</sup> Many ideas may simply never get off the ground. This constitutes an enormous waste of talent and potential growth for the economy.

#### Post-revenue funding

24. The barriers faced at the pre-seed and seed stage mean that fewer HDP entrepreneurs are likely to get through to the post-revenue stages. However, for those that do and at the stage where the VC industry gets involved, HDP start-ups continue to face far greater barriers to funding support than white entrepreneurs.
25. The VC industry concedes that it lacks transformation itself, even if this is something it is actively seeking to address. It also accepts that in general the industry perceives the risks in township economies to be higher than they actually are. The result is that the industry does not actively seek out HDP opportunities unless there is a mandate to do so from funders. The primary VC fund with an HDP mandate for 75% of funding, of which 50% is to black Africans, is the SA SME Fund, a joint initiative by government and CEOs of large corporations. The fund has had support from a number of reputable companies and

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<sup>36</sup> [REDACTED]

<sup>37</sup> SAVCA, WS1, page 1.

<sup>38</sup> SAVCA, OS1, date 3 November 2021, page 23

Venture Capital firms and has raised around R1.2 billion in investable capital.<sup>39</sup> However, this is not exclusively focused on tech markets, but rather any business that can scale and create jobs, and covers both VC and private equity growth funds. Beyond this, the industry indicates that mandates are scarce. The Inquiry also identified that even the largest VC funder in SA, Naspers with a R1.4bn fund, has no mandate to support HDPs and could cite only a single small investment in an HDP entrepreneur. This set of circumstances clearly places HDP entrepreneurs in a significantly disadvantaged position relative to their privileged white peers.

26. The industry body SAVCA was able to provide the Inquiry with some information on the B-BEE status of the invested companies for the VC industry (for those SAVCA members that reported on rating). Whilst this does not provide specific information on the HDP status of the entrepreneur, one may infer that the HDP businesses are more likely to be level 1 or at worst level 2 given that there may be a small team and many points are allocated to ownership and management. In 2020 only 6% had a level 1 B-BBEE status and a further 14% had a level 2 B-BBEE status.<sup>40</sup> The vast majority were level 3 and 4 B-BBEE status as illustrated in the table 2 below. It is also the case that much of the HDP investment that is occurring is the result of the SA SME Fund's specific mandate, and the picture outside of that mandate is likely to be a lot worse.

**Table 2: Percentage of black owned companies funded in 2020**

| B-BBEE Level | Percentage (%) |
|--------------|----------------|
| 1            | 6.1            |
| 2            | 14.3           |
| 3            | 77.3           |
| 4            | 2.0            |

SAVCA submission dated 17 January 2022

27. Naspers raised the fact that following rounds of funding there will be a natural dilution of the ownership of the start-up which will reduce the HDP ownership structure, but it seems this does not negate the fact that initially few HDP entrepreneurs funded. [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED].<sup>41</sup> [REDACTED]

<sup>39</sup> SA SME Fund

<sup>40</sup> SAVCA, WS1, page 2

<sup>41</sup> See <https://www.naspers.com/news/naspers-foundry-invests-r30-million-in-sweepssouth/>

28. Some of the SAVCA members have also reported on female ownership as this is another dimension to diversity in entrepreneurs that the Inquiry is interested to understand given the fact that women are likely to be excluded from the tech industry more broadly. The response was that 32.7% of investment was in start-ups with no female equity, and in total two-thirds of start-ups had less than 50% female equity. These figures are illustrated in the table below:

**Table 3: Percentage of female owned companies funded in 2020**

| Female Equity | Percentage (%) |
|---------------|----------------|
| Zero or None  | 32.7           |
| Less than 25% | 17.3           |
| 25 to 50%     | 15.4           |
| 50 to 100%    | 28.8           |
| Don't know    | 5.8            |

SAVCA response to RFI - submission dated 17 January 2022

29. The above figures illustrate the gap for HDP owned firms, especially female equity companies. If 32.7% of SAVCA members reported that they have not invested any funds into black female companies in 2020, this is an indication of a lack of transformation in the industry. Part of the transformation must come from improved mandates<sup>43</sup> that are targeted at growing and developing SME and HDP owned firms.

30. A further systemic barrier faced by many HDP entrepreneurs is getting large business user support to contract with their start-up platforms. Business user support is essential to move a start-up into the post-revenue phase where VC funding comes into play, and to get that post-revenue growth to move into later series of funding. The high levels of concentration and lack of transformation of most industries served by intermediation platforms, characterized by networks of white privilege, makes penetrating the boardrooms in search of contracts a severe challenge for HDP entrepreneurs. The Inquiry was confronted with many stories from HDP platform start-ups of not even getting through the door of key

<sup>42</sup>The largest capital investors in South Africa, [REDACTED]

Naspers Foundry, WS3, Annexure A

<sup>43</sup> An investment mandate is a set of rules laying out how a pool of assets should be invested. Mandates may include guidelines on priorities, goals, benchmarks, risk, and types of funds to be either chosen or avoided. Some may require job creation; others may require investing in green the economy. SAVCA, OS1, Page 5

business users or being rebuffed if they did. In stark contrast, the public hearings were characterized by submissions from successful platforms led by a procession of white males. Their stories sometimes involved similar modest starts too but received a boost from a network that provided initial angel funding, and then networks which enabled contracts with large businesses that provided a huge boost to the growth prospects that attracted larger amounts of further funding.

31. The Inquiry's provisional finding is that HDP entrepreneurs face systemic and material funding barriers even if they reach the post-revenue stage. This is directly a result of their historical disadvantages but also the lack of transformation of the VC industry. This means that conscious efforts need to be made to overcome these barriers much like the SA SME Fund has sought to do. However, the Inquiry finds that this intervention cannot be the only one and the industry and funders need to more consciously invest in HDP entrepreneurs.

## **6. Public Sector Funding**

32. In 2019 President Cyril Ramaphosa tasked the South Africa's 4<sup>th</sup> Industrial Revolution ("4IR") Presidential Commission ("the 4<sup>th</sup> IR Commission") to create creates space for stimulating dialogue, understanding and action to shape a coherent 4IR plan for South Africa. The department of communications and digital technologies introduced the report in 2020, the 4<sup>th</sup>IR Commission was tasked, amongst others, to provide an enabling environment for South African companies that are attempting to innovate technology in the digital sector. The report recommends that support for SMEs is required to enable them to compete in the global competitive environment. In this regard, the report notes that enabling ease of global competitiveness is essential for expansion.
33. In its efforts to uphold these recommendations, the SME Fund was established, a joint initiative by government and corporations, mandated to assist 75% SME and HDP owned firms. The fund holds just under R1.4 billion of capital.<sup>44</sup>
34. There are support programmes under existing South African government structures such as the Department of Trade and Industry and Competition (DTIC") which aim to boost innovation, its Support programme for Industrial Innovation ("SPII")<sup>45</sup> programme provides

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<sup>44</sup> SA SME Fund integrated Report 2021, page 11. Accessed 11 July 2022 [The-SA-SME-Fund-Integrated-Report-and-Notice-of-AGM\\_compressed.pdf \(sasmefund.co.za\)](https://sasmefund.co.za/The-SA-SME-Fund-Integrated-Report-and-Notice-of-AGM_compressed.pdf)

<sup>45</sup> However, the SPII program needs to be further targeted at online innovation. Unfortunately, the DTIC needs also to target funding for existing SME or HDP owned firms that have existing online businesses with online platforms or online sales channels, rather than through university programmes.

grant fund to help entrepreneurs commercialise innovative projects and The Technology and Human Resources Programme (“Thrip”) also grants entrepreneurs, that work with universities or colleges carry out research in order to commercialise innovative solutions.<sup>46</sup> DTIC has introduced policy interventions that aim at deconcentrating markets where HDPs are unable to participate, this policy framework is still at introductory phase.<sup>47</sup>

35. Other government structures such as the Industrial Development Corporation (“IDC”) provides finance for industrial development projects. In 2014, the IDC launched the *Start-up Nations South Africa Initiative* to unleash high-impact entrepreneurship and innovation. However, the programme are not directly targeted at entrepreneurs in the digital space, *“The IDC does not provide direct funding support for businesses that are dedicated on-line companies...”*<sup>48</sup> The Inquiry also notes that its funding criteria is as vigorous as private sector funding the criteria for funding is that *“the business [needs to be able] to service all its debt and ensure future sustainability, especially in terms of profitability, job creation and retention, as well as future growth prospects...”*<sup>49</sup>
36. IDC submitted to the Inquiry that, while funding for online platform development is not within IDC’s mandate, the IDC manages DTIC’s *Khoebo Innovation Promotion Programme* (“KIPP”) which provides funding for locally developed innovations which could include apps and platforms. Over the last five years, ending in 2020, IDC has approved R71.4 billion in funding to support black industrialists, black owned, women empowered and youth entrepreneurs. Over 75% of the funding supported business expansion and start-ups, but not targeted at online markets.
37. In its submission to the Inquiry, the IDC notes that more still needs to be done in the online economy for SME and HDP owned firms, there still exist prevalent challenges, such as -  
1) Access to capital: Equity contribution to the business can be prohibitive; 2) Access to markets: Lack of long-standing relationships and networks for HDPs; 3) Access to opportunities: Limited opportunities due to limited experience and networks that can be leveraged; 4) Access to information: Limited information on available capital, opportunities, and markets for potential black industrialists; 5) Capacity, skills and business mentorship: High rate of failure for new businesses can often be due to lack of management experience, skills and access to business mentors; and Continued monopolistic structures;

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<sup>46</sup> Naspers Foundry, WS1, page 13, Annexure A

<sup>47</sup> DTIC, OS1, page 2

<sup>48</sup> Industrial Development Corporation by Tshepo Legodi, dated 17 September 2021, page 1 (IDC, WS1)

<sup>49</sup> IDC, WS1, 17 September 2021, page 2

- 6) The monopolistic nature of certain industry structures continues to exclude black entrepreneurs.<sup>50</sup>
38. The Department of Small Business Development (“DSBD”) is currently leading the development of the digital strategy for the small business development (“SBD”) portfolio which includes the DSBD, Small Enterprise Development Agency (“SEDA”) and Small Enterprise Finance Agency (“SEFA”).<sup>51</sup> The aim of the project is to enhance the small enterprise eco-system and to create universal access through quality infrastructure, devices, services, and content. However, the Inquiry notes that these plans are at early stages, and the DSBD has submitted that it still needs to Develop an implementation plan for the digital strategy, incorporating deliverables and responsibilities of each institution within the short, medium, and long-term periods.<sup>52</sup>
39. During the public Hearings in November 2021, the Inquiry was able to hear from HDP owned business users and SMEs who have sought funding from government departments and access to funding opportunities that are specific to online initiatives but have struggled. The Inquiry’s provisional finding is that systemic and online focused support is required in government. Although there exist various programmes targeted at SME and HDP owned firms, many of the programmes have stringent standards as highlighted in the IDC submission, many are at early planning or non-implementation stage, and some do not target online focused businesses. Government still needs to target support for the digital start-ups aside from funding committed to the SA SME Fund, which itself has a broader mandate.
40. Government funding is necessary if the systemic barriers faced by HDP entrepreneurs in the digital economy is to be overcome, and that the inequity in participation that persists in the traditional economy is not made even worse in the shift to the digital economy. However, given the specialised nature of VC funding, it is not apparent to the Inquiry that government has the skills to undertake the actual task of evaluation of funding pitches and oversight and mentoring required by digital start-ups. This may be the reason for the structure of the SA SME Fund, but it is also likely to apply to initiatives going forward.

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<sup>50</sup> IDC, WS1, 17 September 2021, page 3

<sup>51</sup> Another government programme introduced by The Gauteng Provincial Government was launched in 2001, an Innovation Hub aimed at fostering socio-economic development and competitiveness in the region. The Innovation Hub is behind a range of projects such as mLab, eKasi Labs and the Climate Innovation Centre South Africa. However, the Inquiry did not receive submissions from the Provincial Department.

<sup>52</sup> Department of Small Business Development, by Mojalefa Mohoto, dated 17 August 2021, page 1 (DSBD, WS1)

## 7. Appendix

| Submission made by                        | Stakeholder type                     | Submission full name                                           | Date      | Submission made by                             | Report shorthand reference |
|-------------------------------------------|--------------------------------------|----------------------------------------------------------------|-----------|------------------------------------------------|----------------------------|
| Naspers Foundry                           | Investment subsidiary of Naspers Ltd | Response to 1st RFI                                            | 10-Sep-21 | Daryl Dingley                                  | Naspers Foundry, WS1       |
| Naspers Foundry                           | Investment subsidiary of Naspers Ltd | Response to 2nd RFI                                            | 24-Jan-22 | Daryl Dingley                                  | Naspers Foundry, WS2       |
| Naspers Foundry                           | Investment subsidiary of Naspers Ltd | Response to 3rd RFI                                            | 9-Feb-22  | Daryl Dingley                                  | Naspers Foundry, WS3       |
| Naspers Foundry                           | Investment subsidiary of Naspers Ltd | Comment on Inquiry Statement of Issues                         | 30-Jun-21 | Daryl Dingley                                  | Naspers Foundry, WS4       |
| Naspers Foundry                           | Investment subsidiary of Naspers Ltd | Public Hearing Session with Naspers SA Ltd and Naspers Foundry | 3-Nov-21  | Phuthi Mahanyele-Dabengwa                      | Naspers Foundry, OS1       |
| South African Venture Capital Association | Association                          | Response to 1 <sup>st</sup> RFI                                | 23-Sep-21 | Shelley Lotz                                   | SAVCA, WS1                 |
| South African Venture Capital Association | Association                          | Response to 2 <sup>nd</sup> RFI                                | 17-Jan-22 | Shelley Lotz                                   | SAVCA, WS2                 |
| South African Venture Capital Association | Association                          | Public Hearing Session with SAVCA                              | 3-Nov-21  | Shelley Lotz, Keith van Zyl and Tanya van Lill | SAVCA, OS1                 |
|                                           |                                      |                                                                |           |                                                |                            |
| Department of Small Business Development  | Government Department                | Response to 1 <sup>st</sup> RFI                                | 17-Aug-21 | Mojalefa Mohoto                                | DSBD, WS1                  |
| Industrial Development Corporation        | Government Department                | Response to 1 <sup>st</sup> RFI                                | 17-Sep-21 | Tshepo Legodi                                  | IDC, WS1                   |

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|--------------------------------------------------|-----------------------|----------------------------------|-------------|--------------------------------------|-----------|
| Department of Trade and Industry and Competition | Government Department | Public Hearing Session with DTIC | 29-Nov-21   | Brian Zondo                          | DTIC, OS1 |
| Black Business Council                           | Council of Businesses | Response to 1 <sup>st</sup> RFI  | 26-Oct-21   | Kganki Matabane                      | -         |
| ICASA                                            | Government Department | Response to 1 <sup>st</sup> RFI  | 2-Sep-21    | Willington Ngwepe                    | -         |
| SA Tourism Agency                                | Government Department | Meeting with SA Tourism Agency   | 14-Oct-2021 | Tony Nkadameng and Morongwa Moraladi | -         |
| Ascension Capital Partners                       | Venture Capital       | Response to 1 <sup>st</sup> RFI  | 29-Sep-21   | Naairah Motala                       | -         |
| Tshikulu Venture Capital                         | Venture Capital       | Response to 1 <sup>st</sup> RFI  | 30-Aug-21   | Adam Boros                           | -         |