

Covid-19 has hit SMEs in SA's food sector hard. What can be done to help them

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Covid-19 has prompted widespread discussion of the resilience of food systems and how efficiency and competitiveness have been previously understood.



Covid-19 has further emphasised the need for a more diverse food system, in which SMEs play a key role.

Recent decades have seen the growth of increasingly complex food value chains. These are underpinned by just-in-time delivery systems, a growing share of food products sold through supermarkets, and increasing concentration of ownership among powerful, large food manufacturers.

The pandemic has further emphasised the need for a more diverse and inclusive food system, in which small and medium-sized enterprises (SMEs) play a key role.

As part of a [larger project](#) investigating challenges faced by agro-processing SMEs, we conducted qualitative telephone interviews with 16 SME maize milling and dairy firms during lockdown to gauge the effects of the pandemic.

As essential businesses, food manufacturers continued to operate through lockdown, and it might be assumed Covid-19's

impacts on this industry were minimal. This was not the case. While aggregate production levels were maintained – super maize meal output in April was 25% higher than the same month last year – and consumer prices remained relatively stable, SMEs in these industries faced multiple disruptions throughout their supply chains.

There are still steps that can be taken to shield these enterprises from the worst effects of the pandemic. This should go beyond financial aid and improved access to credit to include, for example, supporting them in diversifying their routes to markets. Such support is critical because the exit of SMEs will exacerbate high levels of concentration and reduce diversity, with consequences for social inclusion and food system resilience. The implications for South Africa's food system would be far reaching.

Precarious

Many agro-processing SMEs were precarious before Covid-19 struck. Power in the South African food system lies with big businesses. In 2017, the 10 largest enterprises [accounted for 72% of revenue](#) in the manufacture of dairy products. In milling, the 10 largest accounted for 76%.

SMEs still play a critical role supplying localised and under-served markets, providing rural employment. They are also important for linkages with other small businesses. Typically they avoid doing business with the big supermarkets due to onerous conditions. Instead they target independent wholesalers and retailers, buyer groups and informal “spaza” shops. They also sell directly to local communities, school feeding schemes and catering.

Covid-19 has reduced SME access to these routes and therefore increased their vulnerability.



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What we found

During lockdown, supermarkets' sophisticated distribution systems enabled seamless operations. Panic-buying also diverted sales towards large retailers with higher stock levels. However, our qualitative research interviews found that the retailers relied on by most SMEs were less well-resourced, and faced a range of logistical and operational setbacks, with financial strains resulting in increased defaults on payments to suppliers.

The SMEs reliant on non-retail sales channels were the worst affected. The cessation of school feeding schemes and closure of hospitality and catering had devastating effects on suppliers. All dairy processing SMEs interviewed suffered major sales reductions, of between 20% and 66%. Some millers reported lower revenue, with some closing down entirely.

Switching to supplying mainstream supermarkets was not a feasible alternative. It would have pitted SMEs against large companies. They would also have had to meet higher standards for product quality, packaging, hygiene and traceability. SMEs would have had to accept the mainstream supermarkets' longer repayment periods, and often onerous rebate and returns policies. Government's emergency food parcel schemes meanwhile had been supplied by large firms, reflecting longer-standing challenges for SMEs with public procurement.

Perishability of raw materials and close links to farming were a further complicating feature. This was particularly common in the dairy sector in instances where SME processors were backwardly integrated into milk producers. Some started selling surplus raw milk to rivals or plan to retire herds because their normal routes to market were cut.

Milling SMEs faced severe difficulties sourcing raw material. They were also exposed to maize price volatility and the adverse rand-dollar exchange rate movement, given their lesser ability to hedge. Interviewees from both dairy and milling

companies also described severe difficulties securing machinery parts, repairs and maintenance services.

Compliance with hygiene regulations was a major cost for SMEs in ordinary circumstances. This dramatically escalated with the need to source personal protective equipment and sanitisers at elevated prices.



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The consequences

Most firms in our sample said they were forced to lay off workers, cut their pay or work reduced hours. Investments that had been planned to improve businesses were halted.

Sadly, government's business support measures provided insufficient remedy. The top-down approach to support provision, with a fragmented array of schemes, and complex application processes and qualifying criteria, proved confusing or too costly even to firms in need.

The [Unemployment Insurance Fund](#) provided a lifeline. Other measures, however, such as the [tax relief](#), [Department of Small Business Development funds](#) and commercial bank support through the [loan guarantee scheme](#), were less accessible.

Notably, firms in difficulty were typically reluctant to take on commercial debt. They argued that despite the loan guarantee scheme, interest rates are prohibitively high. One welcome development in relation to this was the announcement in June's [Supplementary Budget](#) of the relaxation of terms and conditions and extension of repayment holidays.

Even without a repeat lockdown, without greater support, many SMEs will fail or be severely weakened in this period of economic disruption. Adaptation is going to require significant and costly changes to business models.



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What could help?

We see three key actions that could help.

First, there should be commitments by the major retailers to offer SMEs preferential shelf space and to introduce local procurement policies at preferential terms.

Second, alternative routes to market need to be strengthened. This can involve improving infrastructure and implementing regulations that enable SMEs to operate in the peri and non-urban areas. Public procurement can also provide SMEs with consistent revenue streams but needs to be reconfigured to accommodate SMEs' needs. Delays by the state in paying SMEs and often complex and dysfunctional tendering processes remain a big problem.

The expansion of inclusive e-commerce platforms for retail and digital management of food logistics and sales can help SMEs access multiple new routes to market. But this requires state support to build firms' digital capabilities. It also requires policies and regulations to create a competitive digital space and curb the market power of dominant platforms.

Thirdly and finally, there should be improved short-term emergency support, with streamlined application processes and broadened access conditions. Commercial bank loans are inappropriate for SMEs in severe difficulties, and grant finance should be more easily available. Government should also provide assistance with personal protective equipment and sanitisers, in addition to training and advice on how to adapt to new requirements.

In the longer term, South Africa needs to consider how markets may undermine inclusive food systems through '[toxic competition](#)'. The country needs to rethink 'market shaping' policies and value chain governance to emphasise the critical role of the state and collective action.

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