SUSTAINABLE FINANCE AND SMALL, MEDIUM AND MICRO ENTREPRISES IN SOUTH AFRICA

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ABSTRACT

Sustainable finance is of importance to the achievement of the sustainable development goals (SDGs). However, sustainable finance has tended to focus on large firms. Small, medium and micro enterprises (SMMEs) have generally been left behind despite their importance to the achievement of the SDGs. The paper seeks to explore the role of private and public institutions in providing sustainable finance to SMMEs in South Africa. In addition, the paper suggests policy recommendations that can help to improve the use of sustainable finance by SMMEs. The study adopted the desk research methodology that involved the synthesis of extant local and international secondary data sources on sustainable finance and SMMEs. The findings indicated that sustainable finance is an emerging trend in small business finance. Recommendations to improve the use of sustainable finance by SMMEs are suggested.

Keywords: Sustainable Finance, Sustainable Development. Sustainable Development Goals, SMMEs, South Africa.

INTRODUCTION

Schoenmaker (2017) points out that there are many aspects to sustainable development. These include environment challenges such as the depletion of natural resources and climate change. Economic and social challenges include development that does not pay adequate attention to poverty, income inequality and the provision of basic needs to all people. According to the World Economic forum (2021), Global Risks Report, there will be an increase in environmental challenges, economic fragility and societal fragmentation. This will be demonstrated through rising unemployment, youth disillusionment and widening digital divides. Poverty and income inequality will increase and the gaps between the poor and the wealthy will widen further. In order to manage these highlighted challenges, the 2030 Agenda for Sustainable Development was adopted by all the United Nations member states in 2015. The agenda provides a plan for peace and prosperity now and in the future for people and planet. Twenty Seven Sustainable development goals (SDGs) that will help to end poverty, improve health and education, tackle climate change and spur economic growth were developed (United Nations, 2015).

Small, medium and micro enterprises (SMMEs) have a major role to play in sustainable development. SMMEs create sustainable employment which helps to reduce poverty and income inequality and spur economic growth (United Nations, 2020). As indicated by Nursini (2020), SMMEs activities also contribute towards economic growth and development. SMMEs account for the majority of private sector businesses in developing and developed countries (World Bank, 2020). Formal SMMEs contribute about 45% of total employment and 33% of gross domestic product in developing countries. These figures are significantly higher if informal SMMEs are added (World Bank, 2020). According to the National Development Plan of South Africa, SMMEs are expected to generate 90% of the eleven million new jobs and contribute 60-80% of the increase of the gross domestic product by 2030 (National Planning Commission, 2012). SMMEs are of significance in achieving the SDGs especially SDG 1 (end poverty), SDG 2 (zero hunger), SDG 3 (good health and well-

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being), SDG 5 (gender equality), SDG 8 (promote inclusive and sustainable economic growth, employment and decent work), and SDG 9 (improve sustainable industrialization and fostering innovation) (Tonis, 2015; World Bank, 2019; Organisation for Economic Co-operation and Development (OECD), 2019). In addition, SMMEs on the aggregate have a significantly high environmental footprint but also have the potential to substantially innovate ecologically and make significant contribution to clean technology and environmental improvements (OECD, 2018).

Sustainable finance defined as the process of taking into consideration environmental, social and governance (ESG) issues in making lending decisions by the financial sector is one of the key tools to deliver the SDGs (Schoenmaker, 2017; European Commission, 2021). Fullwiler (2015) argues that while traditional finance is driven by a narrow set of goals namely financial risk and financial return, investments in projects and companies produce much broader set of outcomes. Sustainable finance provides the opportunity to develop a more general finance theory that has a multi-dimensional focus. Sustainable finance has led to the important role of non-financial factors–environmental, social and governance (ESG) in financing decisions (Ziolo et al., 2019; Ziolo et al., 2020). Many financial institutions have incorporated sustainable finance in their investment decisions and implemented ESG principles in lending. However, SMMEs have not received adequate attention (United Nations Environment Inquiry, 2017; Durst & Gerstlberger, 2020). The financing of SMMEs and sustainable finance have operated largely in parallel and this represents a missed opportunity. Sustainable finance can help conventional SMMEs to improve their sustainability performance. In addition, sustainable finance can help to develop SMMEs that are green innovators (United Nations Environment Programme, 2017). Therefore, financial institutions and policy makers need to give attention to the sustainable financial needs of SMMEs.

The aim of this study is to explore how the sustainable financing of SMMEs can help to achieve the SGDs in the South African context. The paper aims to answer the following questions: What is the role of private and public institutions in providing sustainable finance to SMMEs? and (2) what are the policy recommendations that can help to improve the use of sustainable finance by SMMEs? Sinkovics et al. (2020) as well as Onwunta & Railoun (2021) remark that since the introduction of SDGs by the United Nations in 2015, research has largely focused on how government agencies and large organisations can work towards attaining these goals. Limited research has focused on SMMEs despite the fact that they contribute the majority of firms in both developing and developed countries.

LITERATURE REVIEW

Definition of SMMEs in South Africa

SMMEs can be defined as

"A separate and distinct business entity, together with its branches or subsidiaries, if any, including cooperative enterprises, managed by one owner or more predominantly carried on in any sector or subsector of the economy mentioned in column 1 of the Schedule and classified as a micro, a small or a medium enterprise by satisfying the criteria mentioned in columns 3 and 4 of the Schedule" (Government Gazette, 2019, p1).

Table 1
QUANTITATIVE DEFINITION OF AN SME IN SOUTH AFRICA

Company category	Employees	nual turnover(SA Rand)	Gross assets, excluding fixedassets
Medium-sized	51 to 250	Less than 4m to 50m depending on Industry	Less than 2m to 18m depending onIndustry
Small	11 to 50	Less than 2m to	Less than 2m to

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		depending onIndustry	5 m dependingon industry
Micro	1 to 10	Less than 150 000	Less than 100 000

Source: Adapted from Government Gazette (2019)

Sustainable Development Goals (SDG)

The Bruntland Commission in a report titled "*Our Common Future*" linked the issues of economic development to environmental stability. The Bruntland Commission report defines sustainable development as

> *"Development that meets the needs of the present without compromising the ability of future generations to meet their own needs" (United Nations General Assembly, 1987, p. 43).*

The sustainable development goals (SDGs) are a group of seventeen interlinked goals that are designed to ensure a better and more sustainable future for all (United Nations General Assembly, 2015). The 17 SDGs are: (1) No Poverty, (2) Zero Hunger, (3) Good Health and Well-being, (4) Quality Education, (5) Gender Equality, (6) Clean Water and Sanitation, (7) Affordable and Clean Energy, (8) Decent Work and Economic Growth, (9) Industry, Innovation and Infrastructure, (10) Reducing Inequality, (11) Sustainable Cities and Communities, (12) Responsible Consumption and Production, (13) Climate Action, (14) Life Below Water, (15) Life On Land, (16) Peace, Justice, and Strong Institutions, (17) Partnerships for the Goals. Schoenmaker (2019) classify the goals into the levels of the economy, the society and the environment. Economic goals include goals 8, 9. 10 and 12. Societal goals include goals 1, 2, 3, 4, 5, 7, 11, 16. Environmental goals include goals 6, 13, 14, and 15. The National Development Plan of South Africa (NDP): Vision 2030 has a 74% convergence with the SDGs. The plan gives priority to the elimination of poverty and reduction of income inequality, creation of jobs and growing an inclusive and sustainable economy by 2030 (Sustainable Development Goal in South Africa, 2019).

Sustainable Finance

Definition of Sustainable Finance

Ziolo et al. (2020) point out that financing is necessary to achieve the SDGs. Conventional finance that focuses primarily on profit and not the three-dimensional perspective of sustainable development is unsuitable and inadequate for the financing of SDGs. Sustainable finance incorporates non-financial (Environmental, Social and Governance) factors into the risk analysis of financial institutions and is the new the paradigm in finance (Zorlu, 2018; OECD, 2018). The Swiss Sustainable Finance (2021) defines sustainable finance as "*any form of financial service integrating environmental, social and governance (ESG) criteria into the business or investment decisions for the lasting benefit of both clients and society at large*" Migliorelli (2021, p) defines sustainable finance as "*finance to support sectors or activities that contribute to the achievement of, or to the improvement in, at least one of the relevant sustainability dimensions*". The European Commission (2021) defines sustainable finance as "*the process of taking environmental, social and governance (ESG) considerations into account when making investment decisions in the financial sector, leading to more long-term investments in sustainable economic activities and projects*". The National Treasury (2020, p16) proposes the following definition of sustainable finance for South African policy making: "*Sustainable finance encompasses financial models, services, products, markets and ethical practices to deliver resilience and*

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long-term value in each of the economic, environmental and social aspects and thereby contributing to the delivery of the sustainable development goals and climate resilience".

Sustainable finance takes into consideration environmental social and governance factors. Environmental considerations include climate change mitigation, pollution prevention, the circular economy, and the preservation of biodiversity, Social considerations relate to the issues of inclusiveness, inequality, labour relations, human rights issues and investment in human capital and communities. Governance considerations include employees' relations, executive remuneration and management structures (European Commission, 2021) Sustainable finance is important to ensure economic growth that reduces pressure on the environment while taking into consideration social and governance issues. Sustainable finance can make a significant contribution to the creation of low carbon, climate resilient economy and finance long-term growth in a sustainable manner. In addition, investments are reoriented towards more sustainable businesses and technologies and the achievement of SDGs (European Commission, 2021; National Treasury, 2021).

Private and Public Institutions that can Provide Sustainable Finance for SMMEs

Tang (2021) points out that there are many private and public institutions that can provide sustainable finance to firms. These include (1) corporations through CSR activities and investment in renewable energy (2) commercial banks (3) international finance institutions (4) international organisations such as the United Nations and OECD (5) climate funds (6) National governments (7) institutional investors and (8) Stock exchanges that specialise in green and sustainable investments. The sources of sustainable finance for SMMEs can be divided into debt and equity. Sustainable loans: The major banks in South Africa have products and services dedicated to sustainable or green finance. This is in line with international trend in the banking industry. Some international banks also have green hire purchase and leasing products and sustainable trade finance that can be used to finance goods to meet agreed sustainability standards and to support SMMEs that meet ESG metrics. Green, social or climate bonds are fixed-income debt instruments that can be issued by corporates, banks and government to finance projects with positive social and environmental impacts (National Treasury, 2020). Donation-based crowdfunding focuses on investors that are motivated by social reward and is closely related to sustainability. In addition, crowdfunding investors are becoming increasing motivated by factors, such as philanthropy (Martínez-Climent et al., 2019). Sustainable venture capital firms and angel investors are a major part of sustainable finance and invest = in projects with far-reaching social and environmental impact (Bocken, 2015; Antarciuc et al., 2018; Truong & Nagy, 2020). Government agencies that provide financial support for SMMEs such as the Small Enterprise Finance Agency (SEFA) can establish funds with the goal of financing sustainable-oriented SMMEs.

RESEARCH METHODOLOGY

The study adopted the desk research methodology that involves the use of already existing data. The desk research was carried out between January and May 2021 and involved the synthesis of extant local and international secondary data sources on sustainable finance. The review of the literature included government papers such as the draft national policy in South Africa by the National Treasury, papers on sustainable finance by international organisations such as the European Commission. In addition, the websites of the big banks in South Africa and international banks were examined for sustainable finance products and lending requirements. The keywords were sustainable finance, responsible finance, green finance, impact finance, SMMEs, commercial banks on the Google search engine. The search

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resulted in 86 journal articles, government reports and reports of international agencies on sustainable finance. The author conducted an initial screening by checking the abstracts and executive summaries to identify the materials that are relevant in achieving the aim of the study. First, reports and websites of government agencies in South Africa and international organisations such as the European Commission were checked to develop a good understanding of sustainable finance and policies aimed at promoting sustainable finance. Second, the websites of the big banks in South Africa and internationally were checked to examine their sustainable development products and services. Third, the websites of local and international universities were checked to discover if there are departments and centres that focus on sustainable finance. Fourth, journal articles on sustainable finance were downloaded. Thereafter, a qualitative content analysis of the selected articles, papers and reports was done with the goals of summarising existing research and identifying conceptual patterns.

FINDINGS

The findings indicate that there is a universal realisation of the importance of sustainable development and that sustainable finance is important to achieving the SDGs. Sustainable finance is a new finance paradigm, and there is a growing recognition that ESG issues have to be taken into consideration in financing decisions. International institutions such as the European Commission and the G20 have developed action plans that aim to increase the flow of capital towards sustainable investment. South Africa's sustainable finance initiative has the goal of incorporating perspectives from all parts of the financial sector including banking, pension funds, insurance and the capital markets. In addition, many local and international commercial banks have sustainable/green finance products and services. The use of sustainable finance by SMMEs is limited. However, policies that specifically relate sustainable finance to SMMEs have started to gain international recognition. For instance, the report commissioned by Italy's Ministry of the Environment titled "*Mobilizing sustainable finance for small and medium sized enterprises reviewing experience and identifying options in the G 7*" aims to explore the emerging links between financing for SMMEs and sustainable development. Empirical research on sustainable finance is growing, however research focusing on SMMEs and sustainable finance is limited both internationally and in South Africa. To promote research on sustainable finance, some international universities have created centres for sustainable finance.

RECOMMENDATIONS TO IMPROVE THE USE OF SUSTAINABLEFINANCE BY SMMEs

Government: South Africa has a draft policy on the financing of sustainable economy. The draft policy includes sections on the definition of sustainable finance, banking, retirement funds, private equity, capital markets and insurance. A section should be created with a focus on Sustainable finance and SMMEs because of their potential contribution to sustainable development. There is the need for government to create awareness about sustainable development and sustainable finance for SMMEs in South Africa. Government agencies that support small businesses such as the Small Enterprise Development Agency (SEDA) and the Small Enterprise Finance Agency (SEFA) should include sustainable business, ESG and sustainable finance in their promotion, development and support initiatives and financing model for SMMEs. There is also the need for adequate capacity building in government agencies in the area of ESG and sustainable finance. Government can also promote the movement of SMMEs into sustainable businesses through economic incentives and tax rebate.

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Commercial banks: Large commercial banks in South Africa generally have sustainable/green products and services. There is the need to create awareness about the availability of these products and services to SMMEs. ESG issues should be included in the lending requirements for SMMEs. Banks need to work with SMMEs on their journey towards sustainable business through awareness and the provision of funds specifically targeting sustainability-oriented small businesses.

Equity providers: Venture capitalists and angel investors that finance early stage and growth SMMEs should focus on impact investing especially firms that have incorporated ESG in their operations

SMMEs: SMMEs need to introduce sustainability and ESG issues into their operation and reporting and move from the shareholder perspective to an approach that balances the interests of all their stakeholders. SMME owners to be proactive and attend training and seminar on sustainable development, ESG and sustainable finance.

Universities: In line with the emerging research interest in the areas of sustainable development and sustainable finance, South African universities should have research centers or departments that focus on sustainable development and sustainable finance. Sustainable development, sustainable business and sustainable finance should be introduced in the curricula of South African universities. Community engagement programmes by universities and students should include the training of SMMEs in the areas of sustainable business and sustainable finance. Research on sustainable finance and SMMEs should be expanded**.**

CONCLUSION

Sustainable finance is of importance to the achievement of the sustainable development goals (SDGs). However, sustainable finance has tended to focus on large firms. However, the use of sustainable finance by SMMEs is limited. The study explored the role of private and public institutions in providing sustainable finance for SMMEs. The findings show that Sustainable finance is a new finance paradigm and there is a growing recognition that ESG issues have to be taken into consideration in financing decisions. Recommendations to improve the use of sustainable finance by SMMEs are suggested. The study has some limitations. The study does not claim to be an exhaustive review of all relevant literature on sustainable finance given the growing research on the subject. In addition, the review focused on publicly available journal articles and government papers in English because of cost constraints and language barrier. Further studies should focus on empirical research that involves primary data collection and analysis on sustainable finance and SMMEs especially in developing countries.

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