

LEVERAGING SUSTAINABLE DEVELOPMENT



Psi

The Private Sector Initiative

TANZANIA

Cover photograph:

Anicet Buramu (left), purchasing officer for Shelys Pharmaceuticals, checks the quality of a label supplied by an SME. Shelys is part of the Sumaria Group, one of eight corporates participating in the Psi Tanzania.

‘This initiative is not charity; it’s hard-nosed business. As we all know, merely handing out money will not solve any problems. Charity does not foster entrepreneurship.’

The Hon Basil Mramba, minister of finance, at the launch of the Psi Tanzania, July 2002

The Hon Basil Mramba (right), Tanzania’s Minister of Finance, with Samuel Mupanemunda, former CEO of BP Tanzania, at the launch of the Psi Tanzania ... the government’s support is crucial to the programme’s success.



A year after its introduction in early 2002, the Private Sector Initiative and Business Linkages Programme (Psi) Tanzania is deeply entrenched in that country. Key role players in the Tanzanian economy regard it as a developmental model with enormous potential. Thus the Hon Basil Mramba, Tanzania’s Minister of Finance, has stated: ‘This could be a model not only for Tanzania but also for other countries throughout the developing world.’

But what is the Psi, and what is it trying to achieve? This publication will explain the philosophy behind this model, its general objectives, and how these fit with both government policy and development realities in Tanzania. It will also explain how the Psi works, and why it is so useful to have an outside agent – the Small Business Project (SBP) in this case – managing the process.

The challenge

Poverty is often a self-perpetuating trap; poor countries embarking on market-driven economic development rapidly run into constraints posed by their very underdevelopment. Tanzania is no exception. Since economic liberalisation began in 1985, and especially after the election of President Benjamin William Mkapa in 1995, the country has been relatively successful in attracting direct foreign investment, particularly in large projects. Of course, this is exactly how successful development starts. But what comes next? This sort of development tends to create a structural situation where the economy consists of a small number of large, mostly multinational, corporations at one end of the spectrum and many small, often informal, enterprises at the other, with few links between the two sectors.

According to development theory, such a situation is characterised by a ‘missing middle’. In other words, formal small and medium enterprises (SMEs) are under-represented in the national economy. As a result, linkages between big investors and the domestic economy are weak, and the developmental impact of large-scale investment – wealth accumulation, employment, and increased capacities – inherently limited. The challenge is to turn the kick-start provided by large-scale investments into sustainable national development. But this will only happen if the gap between small local enterprises and corporations is filled by thriving SMEs. It is precisely this area that the Psi Tanzania has targeted.

The Psi model

The Psi is a model pioneered by the Small Business Project (SBP), a specialist support and research unit engaged in small business development based in Johannesburg, South Africa. It provides large companies with a vehicle for collaborating with each other as well as with donor agencies and government in order to promote a more joined-up economy, and thus contribute to filling the ‘missing middle’. The participating corporations make up a core knowledge-based network, sharing information, insights and methods, especially in supplier development and outsourcing, but also in relation to wider local enterprise development.

One of the virtues of this model is its flexibility. Variations between countries are important, and the concerns that drove the original South African Psi, as well as its methods and types of benchmarks, are not always appropriate to Tanzania. For example, in Tanzania import substitution – sourcing goods domestically – is far more significant as a factor in national development and as a benchmark than in South Africa. It is also important for the legitimacy of the programme that it dovetails with the development policies of a particular government.



But why do Tanzanian corporations need a Psi? Why can they not simply get on with supplier development and outsourcing themselves? In fact, all the corporations participating in Psi Tanzania were active in these areas prior to this programme. But the Psi has added something to the process. This is partly a result of SBP's facilitative role, and partly of the momentum generated by the Psi process itself.

SBP provides a single point of co-ordination that frees up busy corporate chief executives, managers, and buyers, and so prevents the Psi from becoming a time-consuming burden. A process co-ordinated from outside any one corporate makes it easier to align the agendas of chief executives, managers, and buyers. And a single point of co-ordination makes the dissemination of cross-learning more effective.

SBP brings to the process its extensive experience in the fields of business linkages and small business policy – especially in respect of creating an enabling environment for small business development. Even with the best will in the world, it can be difficult for corporations to properly understand the concerns and priorities of SMEs. Regulatory compliance issues, for instance, are often only a minor irritant to big companies, given their extensive resources in the form of in-house lawyers and accountants – but can be crippling for an owner-managed SME. Small-scale entrepreneurs, for their part, are often even further from understanding how big business operates, and how to interact with it.

Finally, SBP brings to the process a number of tools developed during the implementation of the Psi in South Africa, and now specially tailored to conditions in Tanzania. These include an SME accreditation system, a reporting format for corporate spend – which is being used as a diagnostic tool – and a database format for SME suppliers.

It's not just philanthropy

Many people believe the Psi is a charitable initiative. This is not the case. Although perceptions of precisely where the Psi fits in vary between companies, the model is easily able to accommodate different emphases. So for some corporations the Psi is an integral part of corporate social responsibility (CSR), while for others it is a part of their core business. But no Psi participant considers the programme to be a matter of charitable donations.

What renders the distinction between CSR and core business unimportant in this context is the Psi's overarching objective. The programme is, above all, intended to develop local markets. One of the primary constraints on emerging indigenous SMEs is the underdevelopment of the domestic market, and thus low demand for the goods or services they sell. A proven strategy is for the corporations to effectively act as the market during the crucial early stages of development, thereby leveraging sustainable small business development.

The Psi working group, facilitated by the SBP – the engine room of the process, where operational officers of participating corporates exchange information on supplier development.

'Our foreign direct investment might be significant, but it makes little difference to the life of the ordinary person in the street. That is where we have to prove our credentials.'

Roy Meade, senior vice-president and general manager, Kahama Mining Corporation

CORPORATE PARTICIPANTS IN THE Psi TANZANIA

BP Tanzania
Kahama Mining Corporation
Kilombero Sugar Company
National Microfinance Bank
Sumaria Group
Tanga Cement Company
Tanzania Breweries
Tanzania Cigarette Company

BP Tanzania's tank farm in Dar es Salaam, right, and spaza shops in the same city, facing page, symbolise the extremes of Tanzania's economy ... the Psi Tanzania is aimed at helping to fill in the 'missing middle'.



Much of the Psi's work thus far has focused on budgetary decision-making and supply chain development. In 2002 the eight Psi corporations spent about US\$21 million – about 35 per cent of their aggregate US\$60 million local purchasing budgets – with Tanzanian SMEs. But this figure represents only 12,7% of their total purchasing budgets. The Psi's objective is to increase both local and SME spend and, over time, ratchet up the quality and complexity of these purchases. The Psi hopes to create a 'snowball effect': as SMEs develop, through their linkages with corporations, they too will contribute to developing local markets. Eventually, the SMEs that supply corporations will buy from other local SMEs, resulting in second-tier linkages. The more indigenous SMEs thrive, the more competitive and efficient local markets will be, to the benefit of all consumers in Tanzania.

Of course, the Psi will not solve all the problems of Tanzania's developing markets. But because corporations face the pressures of global competition, they are in many ways the most technologically and organisationally advanced entities in developing countries. The Psi is a way of leveraging sustainable development through nothing more than doing day-to-day business in a slightly different way. This type of initiative is probably the most effective way for corporations to bring their capacities to bear on developmental issues.

The SBP's role

- To facilitate the involvement of Tanzanian corporations in the Psi
- to provide the tools for participating corporations to accredit SMEs
- to create a database of local small and medium suppliers
- to help identify outsourcing and supplier development opportunities within each participating corporate's value chain
- to help identify synergies among corporations' local supplier development programmes
- to provide templates for corporate spend maps, monitoring and evaluation systems

The Psi and Tanzania

The SBP was initially approached by BP Tanzania and invited to explore the possibility of a Psi in that country. It was clear from the outset that success would hinge on the continuing commitment of corporate participants, the backing of the government of Tanzania, and the efficacy of the SBP itself as facilitator.

Corporate commitment is essential because supplier development often comes with a potentially heavy cost in kind. At the very least, corporate buyers have to spend time with local suppliers as both sides work to understand cost and quality issues. But buyers are not likely to do this voluntarily unless supported by their chief executives. It is in the nature of buying departments that when one supplier cannot meet cost or quality standards they will simply look elsewhere, offshore if necessary. The Psi asks buyers to do something with a risk profile different to the job for which they are trained. There may well be failures or at least unforeseen difficulties as they come to terms with a different mode of operating; under these circumstances, buyers need to know that they have the support and understanding of the chief executive.

The Tanzanian corporations all stated a more than adequate commitment at the outset. But words are cheap. What has been more impressive is the chief executives of all

the participating corporations – Sam Mupanemunda of BP, Roy Meade of Kahama Mining, David Haworth of Kilo- mbero Sugar, James Nehmer of the National Microfinance Bank, Jayesh Shah of Sumaria Group, Leon Hooper of Tanga Cement, Natwar Gotecha of Tanzania Cigarette Company, and Justice O’Donovan of Tan- zania Breweries – have been actively involved in driving linkages under the programme.

The second precondition for success was the support of the government of Tan- zania. The government has committed itself

to a process of continuing consultations with the private sector, and has embarked on a series of Investor Round Table (IRT) meetings, which started in 2002. Significantly, the government has included the Psi in a matrix of actions aimed at addressing key issues raised in IRT meetings. In recasting the enabling environment for business, especially for SMEs, in Tanzania, the practical insights produced by the Psi are invaluable. Given the nature of their business, small-scale entrepreneurs usually do not have much time at their disposal for policy advocacy. When corporations understand the conditions under which their indigenous SME suppliers operate, and are committed to the development of the latter, their role in communicating the concerns of this sector to government is crucial. Policy advocacy is not the immediate objective of the Psi, but, because the participating corporations are involved in a policy dialogue with the government of Tanzania, it is crucial to informing the process.

The government’s central policy platform, introduced as a component of the World Bank’s Highly Indebted Poor Country (HIPC) debt relief programme, is a Poverty Reduc- tion Strategy Paper (PRSP). The PRSP emphasises the need for private sector-led and mar- ket-driven growth, and the development of SMEs. In return, it is only reasonable that the government requires the private sector to actually be seen to be leading. This is one of the ways in which the Psi is playing a major role.

Gathering momentum

The Psi consists of three components:

- a Steering Group, made up of the chief executives of the participating corporations, whose function is oversight, general direction, and overall vision;
- a Working Group, the engine room of the process, where corporate operational people (mostly, although not exclusively, buyers) exchange information on value chain and supplier development; and
- the SBP, which acts as a facilitator and technical support agency, monitors and evaluates the process, and helps to capture and share good practice.

One of the most important tools the SBP brings to the table is a format for evaluating and accrediting SMEs. This does not replace the corporations’ own supplier accredita- tion systems, some of which have been painstakingly devel- oped over many years. Instead, the SBP format is designed to supplement such systems and is based on years of prac- tical experience in South Africa, coupled with the Psi com- panies’ experience in Tanzania.

The SBP’s mandate is to set up the Psi and then spend two years working its way out of the job, handing over cer- tain functions to Tanzanian business development suppliers, with mentoring and development programmes if neces- sary. Such an exit strategy is crucial – the Psi is intended to



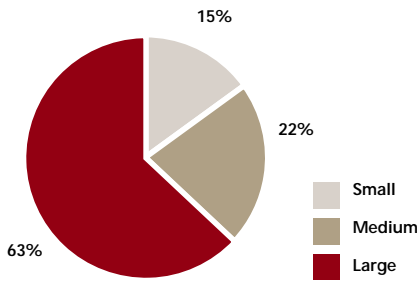
‘The vision ... is the creation of a vibrant and dynamic SME sector that ensures effective utilisation of available resources to attain (an) accelerated and sustainable growth rate.’

*Ministry of Industries and Trade,
Government of Tanzania*

Gerald Luganga (right), procurement manager of BP Tanzania, with an SME contractor at a new BP service station ... thriving SMEs are needed to turn foreign investment into sustainable national development.



**SPENDING PATTERNS
OF PARTICIPATING CORPORATIONS,
2002**



'We spend hours, even weeks, with new suppliers. If they can't match the price of a supplier from abroad, we look at their production process and work with them to find ways of bringing their prices down.'

Gerrie Fischer, technical director, Tanzania Breweries

be the exact opposite of the sort of long-running donor programmes that only serve to increase dependency.

By early 2003 the Psi had achieved several important objectives. First, a dipstick survey of SMEs and Business Development Services (BDS) was commissioned from a local research agency. It revealed a great deal about the generic obstacles faced by SMEs in Tanzania, and provided participating corporations with essential information in the course of their search to increase their spend on local suppliers. Of course, these corporations were far from ignorant of these factors even before the survey, but general problems with the BDS market were revealed for the first time. This is significant, as a well-developed BDS environment reduces the pressure on corporations in developing their supply chains. Corporations have less to worry about when SMEs use specialist service providers to help them address deficiencies. The Psi is currently developing a strategy that will play a part in dealing with this problem.

Second, the participating corporations have all produced 'spend maps' which has allowed their aggregate SME spend to be calculated (see accompanying graph). This provides a baseline against which their future local SME spend will be assessed. Analysis currently under way is also expected to reveal new areas of synergy between the corporations, as well as hitherto untapped opportunities within each of their value chains. Thirdly, the SBP has compiled and is maintaining a central database of Tanzanian suppliers, available to all participating corporations, which helps them to enhance the local supply content of their value chains, and set enhanced targets for local spend. The database will eventually be handed over to a local host.

Dealing with cost and quality issues

Supplier development and outsourcing is not easy, even when a supportive network such as the Psi is in place.

Corporations operate in terms of globally benchmarked quality, delivery, cost, environmental, and safety standards. Suppliers in developing countries with a 'missing middle' are often unaware of these benchmarks and, even if they are, often don't understand how to meet them. Interactions between corporations and indigenous SME suppliers are as much about mutual education as anything else. And the Psi enables lessons learned by one corporate to be shared with others.

Given the tension between the twin imperatives of maintaining cost efficiency and raising local SME spend, buyers may be tempted to pay a premium for local goods and services. But special deals are contrary to the Psi philosophy. In any case, most of the participating corporations are local subsidiaries of international firms. Even if they were prepared to pay a premium for locally supplied products, they would have to work vigorously to justify this within the group; they would invariably have to guarantee to reduce the price of locally sourced supplies down to at least parity with imported products within a very short time – usually less than one year.

Most participating corporations deal with cost and quality issues by means of a contribution in kind. One of the most important aspects of this is trust. Tanzania Breweries, for example,

insists on open book accounting by its suppliers. This means that the corporate knows exactly what its suppliers' profit margins are. In return, those SMEs benefit from very strong – although not unconditional – support from the corporate. These elements of support play a key role in getting SMEs to spend the time, money, and effort to get their operations up to a standard acceptable to the corporations.



Gerrie Fischer (right), executive director: technical of Tanzania Breweries, with Muthu Karambaya, MD of Carnaud Metal Box, one of numerous SME suppliers benefiting from the programme.

Future challenges

The Psi generally

- To provide an example of international best practice in SME/local supplier development
- To fully establish an autonomous and self-sustaining SME/local supplier development programme.

The corporates

- To continue developing local SME suppliers
- To maintain the continuing commitment of purchasing and technical staff
- To really 'earn their operating licences', in the eyes of the government and citizens of Tanzania, through this and other programmes.

The SMEs

- To make use of the window of opportunity on offer by linking with corporates, upgrading operations, and delivering quality goods and services.

The government

- To utilise the lessons and insights of the Psi in developing an enabling environment for private sector-led SME development.

The SBP

- To continue collecting, processing, and disseminating learning, and to refine its basic model in the light of the Tanzanian experience.
- To implement the refined model in other developing countries.
- To systematically disengage from Tanzania, leaving a sustainable programme in place, maintained by local BDS and corporate buy-in on sound commercial grounds.



Sophisticated machinery at Simba Plastics, an expanding subsidiary of the Sumaria Group, and also a beneficiary of the programme.



A production line at Shelys Pharmaceuticals ... in Tanzania, import substitution is crucial to national development.

'Our philosophy is to "buy Tanzania, build Tanzania". Where possible, Tanzanian products are given preference. And we will be looking to increase our local purchase as a percentage of our total purchase.'

Natwar Gotecha, former CEO, Tanzania Cigarette Company

ACHIEVEMENTS DURING THE FIRST YEAR

- Analytical approach: The SBP has developed tools used by the participating corporations to organise their spend into 'spend maps', and categorise their SME spend. This enables a pragmatic approach to corporate SME objectives and SME target-setting.
- Systems adopted: Systems within corporations have been adjusted to enable the tracking of local SME spend.
- Key performance indicators (KPIs): Local purchasing or 'buy Tanzanian' has been defined as a key performance indicator for both the participating corporations' chief buyers and their technical directors.
- SME database as a tool: A total of 506 Tanzanian SMEs are currently active on database, enabling corporations to cross-reference suppliers with each other. This mechanism expands the potential marketplace for existing SMEs.
- Annual reports: Due to Psi value-add, some corporations intend building the Psi into their annual reports in order to demonstrate its efficacy as a core development programme.

Supplier development: a Tanzanian success story

Tanzania Printers is one of the early successes associated with the Psi. Until recently, the company was a fairly undeveloped local printing operation. Today, following a major expansion programme sparked off by the Psi, it is a supplier to Tanzania Breweries, Kahama Mining Corporation, BP Tanzania, and the Sumaria Group. Encouraged by the enthusiasm of its MD, Aliraza Khimji, Tanzania Breweries decided to involve this printer in its supplier partnership programme (SPP). The key criteria associated with its SPP, that must all be satisfied, are:

Open book accounting + quality + cost + supply = approved supplier

Following a high level of commitment and hard work on both sides, Tanzania Printers invested about US\$2,5 million in new technology, in the knowledge that if its products met price and quality standards it would almost certainly secure future orders. Today, it provides a broad range of sophisticated printing services from a modern plant.

The printer has now entered the next stage of technical capacity-building and development: it has employed a South African printing lab technician – sourced by Tanzania Breweries – for six months to help it reach the required quality in printing labels for beverage bottles, and particularly in metallic printing. Among other things, this will require the establishment of an in-house laboratory.

Illustrating the win-win nature of such supplier development strate-

gies within the Psi, the idea is that Tanzania Printers will print all Tanzania Breweries' labels, thus obviating the need to import them from South Africa. The participating corporations have not given the printer any guarantees, but their commitment to local spend is so strong that an adequate product will certainly secure future business.

Tanzania Printers is an example of high-impact SME development. Experience in eastern Europe has shown that once a supplier has been approved by a recognised corporate SPP, other multinationals accept this as their 'supplier audit', and also start placing orders.



A new press at Tanzania Printers ... the Psi Tanzania has sparked off a major expansion programme.



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