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Is risk management a determinant of financing sustainable empowerment deals of commercial and industrial properties?

Kubheka, Nomathemba

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IS RISK MANAGEMENT A DETERMINANT OF FINANCING SUSTAINABLE EMPOWERMENT DEALS OF COMMERCIAL AND INDUSTRIAL PROPERTIES?

Nomathemba Kubheka

A research report submitted to the Faculty of Engineering and the Built Environment, University of the Witwatersrand, in partial fulfilment of the requirements for the Masters in Building

Johannesburg 2013

Declaration

I declare that this research report is my own, unaided work. It is being submitted for the degree of Master of Science (Building) Property Development & Management in the University of the Witwatersrand, Johannesburg. It has not been submitted before for any degree or examination in any other University.

……..

Nomathemba Kubheka

January 2013

Dedication

This is dedicated to my family, immediate and extended, who offered me unconditional love and support throughout the course of this work. Special gratitude goes to my mother Ntombizethu who has passed on. Thank You Mom for holding a torch for my life!

Acknowledgements

I would like to thank the staff of the University of the Witwatersrand's School of Construction Economics and Management for the guidance they gave me during this journey. A special gratitude goes to Dr. Harry Quainoo for his assistance.

Above all I would like to thank God for His Love and the special gifts that He has given me.

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ABSTRACT

The introduction of Black Economic Empowerment (BEE) was one of imperative economic tools that the South African government established to achieve its transformational objectives of growing the economy, decreasing inequalities, and creating more job and business opportunities for the majority of the population. Although this legislation is not yet fully implemented, more and more companies and individuals are buying into its concepts to address the past inequalities within the economic market. Risk management is at the core of the BEE transactions; while this is the case, the understanding of the profile of the ideal investor by the financiers would enable them to ensure sustainability of the property transactions they finance. The primary focus of all investments is rendering of a return in the future by forfeiting scarce resources, normally capital. Industrial and commercial properties deals are expected to generate rental income so as to realise a capital gain of profit in the long term. Risk management entails the identification, measurement and evaluation of risk associated with the process of decision making. The sustainability of the abovementioned deals ensures that the alluring factor of risk management is indispensable as most activities in the property investments contain risk.

The main purpose and objectives of this research were to investigate the general understanding of the BEE partnerships in the commercial and industrial property sector, pre-cautionary measures (risk management) to take note of in such partnerships (investigated as success and failures of the deals), and the financing and the sustainability of such BEE deals. Given a certain risk profile, property investment looks lucrative, but the risk of failure and factors that guarantee the expected positive outcomes by the investors are of paramount importance.

The research methodology included a combination of secondary and primary data collection and analysis. The latter included different rounds of questionnaires and interviews and the analysis of data through the use of the Delphi method. A sample of 20 representatives from the insurance industries, banks, trading houses, property valuation market as well as the property investment companies took part in this research study.

The findings indicated that there is a general understanding of what BEE is and companies are utilising the legislation. The main success factors raised was that previously disadvantaged participants need not only be part of the deal or contribute financially, but should be operationally involved in the daily running of the business. This in a way minimises the risk of the failure of the deal. Some of the success factors included knowledge, skills and experience of the project team, the application of the codes of good practice, and delivering on the goals set. The most common cause of failure is when deals are concluded for the wrong reasons; i.e. partnering for the purpose of meeting the required BEE scorecard or fronting. Lack of planning and implementation the risk management techniques is another cause of failure.

Therefore, risk management techniques are critical to the success of the empowerment property deals and they should be encouraged as a persuasive tool that will ensure that the BEE deals are sustainable.

CHAPTER 1: INTRODUCTION

The South African economy has been going through a major transformation for more than a decade now. This has seen a number of Charters being launched with the ultimate goal of bringing economic growth. The introduction of Property Charter and Financial Services Charters has been followed by many deals. There has however ,been much speculation about the benefit that these deals bring to the empowerment partners involved in them as well as the envisaged risk associated with financing such deals.

The nature of Commercial and industrial property investment is long term with uncertainties associated with its returns. These normally comprise factories and warehouses, cold storage and distribution warehouses, and mixed commercial buildings with shops, offices and warehousing. Also included are buildings zoned for “business” with shops and offices, pure office blocks and shopping centres.

In a property financing context, commercial properties also include some residential projects, such as sectional – title housing, cluster houses and blocks of flats. Conglomerate projects such as mini-factories and office parks are also included, as are specialist buildings such as clinics, hospitals, garages, hotels, resorts and restaurants. Uncertainties may vary in either direction of a most probable estimate the decision makers or the financiers are pleased when the estimate performs as expected, but it is the downside risk that really concerns them the most.

Since the South African democratic elections in 1994, the government tried through a number of policies and laws to address all the issues of inequalities among different racial groupings. Wealth redistribution among different population segmentations was one of the key areas. Although there has been progress to date, there are still traces of social, racial and gender inequalities, as well as severe poverty among other groupings. According to Booysen (2005), if not addressed, the inequality issues among racial groups will continue to be detrimental to South Africa’s long-term growth and will hinder the intentions of transformational process. A study conducted by Hofmeyr in 2004 found that white people still hold 93 per cent of top positions, a 2 per cent reduction from the 95 per cent in 2002 (Booysen, 2005).

BACKGROUND TO STUDY

South African Black Economic Empowerment (BEE) legislation was launched to redress the inequalities of apartheid by giving previously disadvantaged groups economic opportunities previously not available to them. The legislation includes measures such as ownership, preferential procurement, employment equity, skills development, and management, and socioeconomic development (Empowerment business page, 2006).

BEE as defined in the Broad-Based Black Economic Empowerment legislation means the economic empowerment of all black people, including women, workers, youth, people with disabilities and people living in rural areas, through diverse but integrated socio–economic strategies (Empowerment business page, 2006).

The Broad Based Black Economic Empowerment (BBBEE) Strategy was initiated and introduced to assist in the transformation process and the South African Broad-based Black Economic Empowerment Act 53 in 2003 was also promulgated to support this. The main aim of the strategy was to outline the roles of all stakeholders in the BBBEE, promote transformation charters in various sectors, and ensure that Government utilises its leverage in implementing BBEEE. The Act serves to be enabling rather than prescriptive, with the establishment of the BEE Advisory Council, the release of Codes of Good Practice, and the gazetting of some of the transformation charters. Black Empowerment is considered by the Corporate South Africa to be both economically and socially necessary (Sethi cited in Gunter, 2005).

The Codes of Good Practice are binding on the private sector as it interacts with the public sector in day-to-day business interactions. The Codes aim to provide guidelines for all businesses that currently do not have an industry charter. Simple logic would accept that the black people's portion in South Africa, representing almost 75 per cent of the total population, should account for 75 per cent of the country's wealth and disposable income; however, this 75 per cent has not yet been achieved.

The Government established a commission (the Black Economic Empowerment Commission) in 1997 to investigate growing concerns about the pace and results of existing BEE initiatives. The BEE Commission (BEECOM) adopted a definition of BEE as an integrated and coherent socio-economic process that is located within the context of South Africa's national transformation programme - namely the RDP (Redistribution and Development Programme)

aimed at redressing the imbalances of the past. This redress was to happen through transferring management and control of South Africa's financial and economic resources to the majority of its citizens, ensuring that there is a broader and meaningful participation in the economy by black people in order to achieve sustainable development and prosperity in the future (Banda, Herzenberg and Paramoer cited in Gunter , 2005).

The BEECOM report showed that for BEE to be successful it is imperative that the implementation be a state-driven programme. The main shortcoming of the BEECOM preliminary report was that it returned the responsibility for a successful BEE strategy and implementation to the Government without making any proposals. Furthermore, the BEECOM should create a co-ordinated, simplified and streamlined set of guidelines and regulations to provide targets and demarcate roles and obligations of the private sector, and the public sector and civil society over a period of ten years (Banda, Herzenberg and Paramoer, 2003).

The Codes of Good Practise were not only introduced to guide business with the implementation of BEE, but also to address the some of the immense challenges identified. These challenges included issues such as undereducated black populace (Sasol Limited, 1993:31), scarcity of black capital resources (Levin, 1994:3; Nyati, 1993:85), a lack of adequate managerial, technical and administrative skills among some managers (Riley, 1993:62) and, finally, the fact that major corporations in South Africa were controlled by whites, who generally had been perceived to be unwilling to relinquish power voluntarily (Mbatha, 1993:57).

The transformation of the South African property industry is also not immune to these inequality issues, where the sector itself is equally influenced by the advancement of the previously disadvantaged groups into the mainstream economy. This advancement requires established companies to enter into joint ventures with black companies or empower their black work force into becoming shareholders in the companies. Risk management becomes critical in the formation of these new relationships. The most important risk is that the black empowered partner should have financial risk in this joint venture. Many black partners are not eligible to have access to financial capital in order to invest in the joint venture, despite the fact that there are instruments available for addressing this problem.
In any trading environment there are risks which have to be assessed and managed. These uncertainties are associated with the changes in the value of the properties which entail price, market, credit, property rights or obligations. There are various risk management strategies which depend on functions, market liquidity and unchanging definitions of underlying

commodities. The unanticipated risks will always emerge and therefore preventive or curing measures of such risk become more than necessary.

However, one question that is then raised is that is the property market open to the transformational agenda intended by the BEE strategy and its codes of good practice or not? The literature indicates that there are emerging black property enterprises; i.e. Mvelaphanda and Phatsima. Funding is still perceived as a challenge. According to an article written in the Financial Mail in July 2005 (Property July 22) “In the context of the new South Africa, one would think the "new emperors" would be black individuals benefiting from the country's black economic empowerment (BEE) dispensation. As it happens, none of the new emperors come from the previously disadvantaged communities”. The article further indicates that “Madison, a property asset manager which has built a portfolio of more than R16bn over the past few years; Zen prop, with about R4, 5bn; Atterbury, with about R5bn; the Ellerine brothers; and City Properties are all owned and managed by white individuals. So are several other, smaller portfolios” (Radebe, 2005).

The institutional investors, because they buy and sell larger volumes of stock are better positioned to accelerate the involvement of BEE investors in their property transactions since they are the main drivers of prices.

1.1 Problem statement

During the financing process of the BEE deals of commercial and industrial properties do the financiers consider the lack of expertise or skills of the future empowerment partners as one of the risk factors to be considered in line with the requirements of the BBBEE Codes OF Good Practice and Empowerment Charters e.g. Property Charter.

1.2 Scope of the research

1.2.1 Main purpose

The main purpose of this study is to provide a detailed analysis and measurements of the business operation and subsequent credit risk associated with financing BEE deals for the commercial and industrial property sector in South Africa, prior and post the application of the BBBEE code of good practice. Secondly, the study also intends to establish whether the deals are sustainable and whether they will add long –term benefit to the intended empowerment shareholders in the long run, and will ultimately assist transformation. It is important that such deal be structured such that the empowerment partner also adds value in the process while minimising credit risk

1.2.2 Key Objectives

The main objectives covered in this research were:

- To investigate the general understanding of BEE partnerships and how to structure them such that the business risk is minimised;
- To investigate the measures used to manage risk while promoting the sustainability of such partnerships within the property sector;
- To outline the precautions that needs to be taken by the financiers in making decisions of financing such deals (investigated in a form of success and failures of the deals).

Research design

A comprehensive literature review was done to gather more information on the problem areas identified as well as on related matter. This was covered in chapters 2. This mainly comprise of secondary data, Secondary data provides references on issues and steer the research in the right direction. On the sector such as a topic such as Commercial and industrial property, which does not change rapidly, secondary data is valuable for much longer periods than for instance in the electronic industries where changes happen almost on a daily basis. Furthermore, as a general rule, real estate practices follow a similar pattern. This was supplemented by observations and experiences of the researcher.

Primary data was collected firstly, to test the conclusions and recommendations flowing from the literature review process, and secondly, to obtain additional recommendations from respondents,

Methods dealing with the risks and decision-making models were established using the basic theory of Risk Management, applying the process of Risk Management, combining with the real estate practice, using both qualitative and quantitative methods.

In summary, the methodology for this study includes (1) a comprehensive literature review to identify an initial list of unique or critical risks and mitigating measures for the risks associated with financing BEE commercial and industrial property deals ; (2) purposive sampling used in selecting and interviewing representatives - property financiers, investors, developers, managers, landlords and tenants. A total of sample of 20 representatives from insurance industries, banks, trading houses, the property valuation market as well as the property investment companies took part in this research. These representatives were also either involved with the transactions that require stringent and/or pertinent risk management measures required for the different deals; (3) a combination of secondary and primary data collection and analysis. The primary data method, in the form of interviews and discussions with experts, covered different rounds of questioning and interviews and the analysis of gathered data. The main method was done through the use of the Delphi technique.

1.3 Structure of the report

Chapter Two of this research report starts by presenting the literature gathered and reviewed through the secondary research methodology. It highlights the issues gathered from different authors, public documents, as well as the media reports on the issues under investigation.

Chapter Three outlines the research methodology used in collecting the research data and analysing it. It covers the secondary and primary data used, questionnaires developed and used for the discussions and interviews conducted, the sample selection process and the data analysis methods.

Chapter Four presents detailed key findings for all the key themes investigated. These themes ranged from the perceptions of all the stakeholders or the company representatives as per the sampling method, the expectations around partnerships, key success and failure of BEE partners, and the risks and sustainability issues to take note of when entering the BEE deals.

Lastly, Chapter Five outlines the key summary of this research finding, the conclusions drawn from both the literature and the findings of the primary research, and the recommendations for either further research or to be considered for the implementation of BEE and its good code of practice.

The appendices include questionnaires requesting participants to participate.

CHAPTER 2: REVIEW OF RELEVANT LITERATURE

One of the major challenges faced by the South Africa business community is in implementing BEE legislation and ensuring its sustainability within the different economic sectors. There are proposed measures that need to be applied in implementing BEE within the property sector. However, to date there have been challenges around the implementation and sustainability of BEE and risks associated with the overall implementation processes (Sethi, cited in Gunter, 2005).

Therefore, the main focus of this chapter is to review the literature on the background around the BEE legislation and its charters, the Code of Good Practices, the risk and challenges associated with its implementation. It further looks at the cause of successes or failures of BEE and the perceptions around it. The report is also intended to find the correlation between the risk management as a determinant of financing sustainable empowerment deals of commercial and industrial properties and performance monitoring mechanism of the BEE partners in order to develop a comparative analysis prior and post implementation of the Code of Good Practices. The analysis of the abovementioned issues serves as a guide for the detailed literature review as presented in this chapter.

2.1 Black Economic Empowerment (BEE) and Broad Based Black Economic Empowerment (BBBEE)

2.1.1 Black Economic Empowerment (BEE)

South Africa is not realising its productivity potential because of the imbalances that exist (South Africa Broad Based Black Economic Empowerment Act 2003)The underperformance of South Africa's economy and the potential threat of instability have spurred the country's administration to enact a BEE policy that aims to redress the situation.

BEE is an integrated and coherent socio-economic process located within the context of South Africa's national transformation programme, namely the RDP (Redistribution and Development Programme). It is aimed at redressing the imbalances of the past by transferring the management and control of South Africa's financial and economic resources to the majority of its citizens. It thereby ensures that there is a broader and more meaningful participation in the economy by black people, which achieves the aim of sustainable development and prosperity in the future (Banda, Herzenberg and Paramoer, 2003).

In its Strategy for Broad Based Black Economic Empowerment the South African government goes on to assert that BEE should result in one or more of the following outcomes:

- A substantial change in the racial composition of ownership, management and the control of existing and new enterprises;
- Listed companies to take proactive steps to achieve black participation in their shareholding;
- An increasing portion of the ownership ,management and control of economic activities vesting amongst communities ,workers , and collective enterprises;
- Skills transfer to management and staff; and
- The development of rural communities and the empowerment of local communities by enabling access to economic activities, land, infrastructure, ownership and skills.

The outcomes reflected above should be seen as an endeavour by the government to quantify and become specific about the issues that are being targeted. The intent is to move away from generalisations that more often create confusion, with the result that ultimately nothing happens. These outcomes would form a platform for benchmarking and measurement, making it easier to evaluate and track progress in terms of the achievements made.

In February 2007 the gazetting of the Conduct of Good Practice took place, which ensured that companies would have implemented BEE ownership and management control. Companies would also have adopted employment equity, skills development, preferential procurement, enterprise development and socio-economic development policies. At the present moment there are public and private companies that are complying with the BEE requirements. Most state-owned and public companies are compelled to have BEE policies in place (Esser and Dekker, 2006).

Figure 2.1 shows the supply chain process for companies complying with BEE requirements.

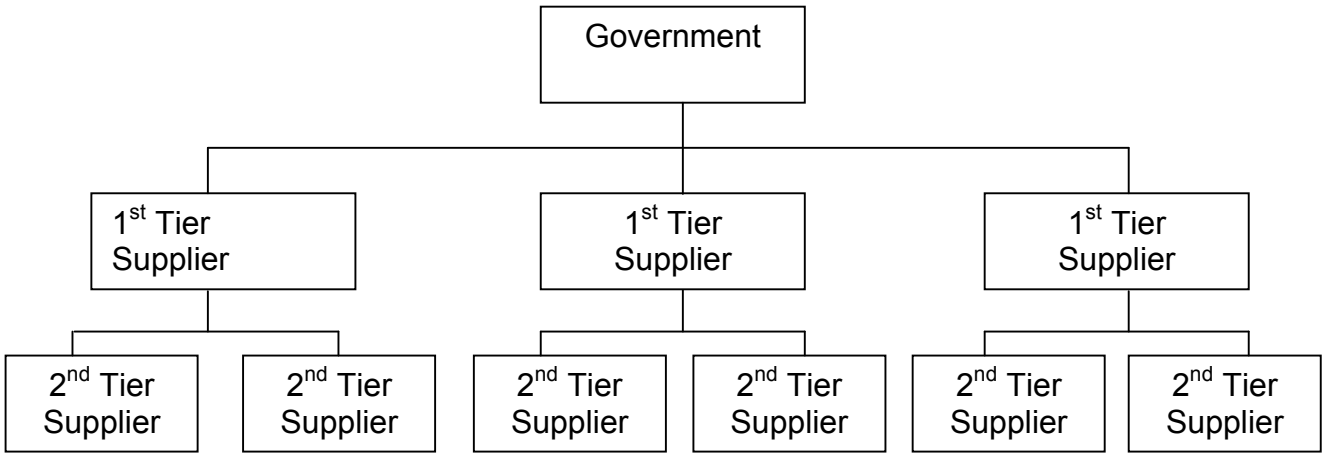


Figure 2.1: Supply chain of companies complying with BEE requirements Source: FNB (2005)

As Figure 2.1 demonstrates, the principle behind the model is that Government deals only with suppliers who meet its BEE requirements. In order to remain fully compliant, these companies will in turn have to deal with suppliers that comply. This trickle-down effect will ensure that transformation actually takes place and that the benefits of BEE are received by all companies in the supply chain that are making the effort to transform.

Nowadays, the concept of BEE is used and the concept has been described as an investment that is a matter of survival for South Africa and the economy (Balshaw & Goldberg, 2005: 16). Kench (2000) states that BEE can sound simple but in reality it is far from that and unfortunately not all Black Economic joint ventures are successful.

Dexter (1999) writes that BEE is considered as a process that reduces the relative power of the privileged over the economy and transfers it to the poor, the disadvantaged, and the underprivileged.

Black Economic Empowerment is also a process of assisting and educating previously disadvantaged individuals to enable them to contribute to the economy. BEE policy is not so much a policy of redistributing wealth, but a process of redistributing economic opportunities within the market structure (Edwin Ritchken 2004: 6).

In the redistribution of economic opportunities within the market structure, basic principles of the market have to be adhered to and risk management becomes the determining mechanism of this process.

Management of risk means that sustainable transfer of wealth should depend on the fit of the empowered company to access and deliver on the opportunities that will result in growth and the value of business in order to exceed the cost of capital.

The process includes issues such as strategy, cost and opportunity which could be summed up as the management of risk based on the market driven outcomes. The main goal is to have an empowered partner who will add value to the company. It is for this reason that businesses entering into empowerment partnership have to identify partners that are able to add significant value so as to enable the business value to grow at a rate that exceeds the empowering partners' cost of capital. Such process will result in the growth in shareholders' value and sustainable empowered shareholding. Therefore, the partnership will have qualities that would effectively and efficiently manage the risk associated with unsustainable ownership deals.

Sanlam CEO, Mr. Johan van Zyl, stated that “The aim of empowerment is to correct some of the distortions of the past and therefore stretches over all spheres from buying and investment to personnel and social investment. All these elements are important for the successful implementation of empowerment” (Finance Week 20 October 2004:15). Such factors show that buying or preferential procurement is an important part of empowerment.

BEE has been criticised for giving preference to black empowered companies associated with individuals who appear to have the appropriate political connections instead of individuals who had the necessary experience and capacity to add value in the direct operations of the target company (Business Map, 1999:14).

Serious concerns have been raised about the benefits of BEE not trickling down to ordinary people. The ruling party, the ANC, has given this flaw special attention. The ANC further questions the current state of BEE: The fundamental question is whether BEE aims to ensure that blacks are fairly represented among the top owners and managers of companies or whether BEE aims to improve the position of all black people, especially women, through the measures that ensure a more equitable distribution of incomes and assets overall.
Orford and Wood (2003) wrote the following, which reiterates one of the problems that, according to the researcher, black economic empowerment faces. “The programme has three significant challenges; firstly raising the opportunity based participation of blacks in owner-operated new businesses, secondly increasing the survival rate of black-owned start-ups and lastly expanding the growth potential of black-owned new businesses”. The lack of focus from the BEE companies to invest in enterprises where they can add value poses a problem, especially while a number of opportunities are presented to them (Legae Securities, 1999). It is therefore impossible for the new investment to survive and grow without hands-on participation of the new investors.

The preferential procurement category on the BEE Scorecard ensures that previously disadvantaged South Africans have the opportunity to now tender and obtain contracts. Black owned companies are increasingly expanding with their growth and have a higher survival rate between 2002 and 2007. This does not make the problem of ‘fronting’ to go away as there has never been any means to monitor the activities of the complying company post the award of the contracts

The literature indicates that empowerment means to give increased power and authority and corresponding responsibilities and competencies to employees (Klagge, 1998:550). Koolen (2004) writes: “Most interesting, in the time it takes to go from concept to transaction, there is

a convenient switch from Black Economic Empowerment to Business Economic Empowerment. There is no clear evidence that identifies changes in relative performance by newly empowered companies compared to non-empowered companies".

Koolen (2004) also states that there is immense pressure on South Africa to reflect the majority of its population and that in turn creates a skewed market at times, because the skills and experience of the broader population are not generally the same as those of the narrow segment. The reality is that most of the large, established BEE companies only acquire stakes or shares in the existing mainstream enterprises. In most cases, the net impact of such interventions on jobs and investments in skills and training has been marginal.

According to Ritchken (2003), the Government is using its position to regulate certain sectors of the economy and its position as a customer in other sectors to redistribute opportunities towards those companies which provide both commercial and empowerment value in the delivery of their product or service. However Ritchken (2003), he states further that many empowerment deals have not resulted in a redistribution of wealth towards an empowerment group, but in a redistribution of shareholding, that benefits the financiers. The ability to add value in the business by the empowered individual thus contributing to the economy is critical in ensuring that the business becomes sustainable. Mere inclusion of PDIs for compliance purposes poses a huge risk for all stakeholders as well as financiers.

2.1.1.1 Reason for BEE

The perception of BEE is driven by the effectiveness of the operational influence of BEE partners. Professional influence leads to potential business expansion and, therefore, the determinant of success of BEE transaction.
Dlamini states (2001: 36) that one of the critical success factors in BEE transactions is having a rationale for introducing a BEE partner. Therefore, according to some studies conducted on BEE policies, the following were identified as company objectives for BEE (Thakurdin, 2002; Nompozolo, 1998):

- To provide opportunities for black business to implement their own Economic Empowerment Programmes;
- To create an understanding and awareness and support for black economic objectives amongst the joint venture's stakeholders;
- To create employment opportunities for disadvantaged communities;
- To involve black people in the mainstream economy;

- To redress the economic imbalances that are a result of the past political dispensation;
- To uplift black people economically in the sense of improving their living standards;
- To obtain access to and control of resources;
- To acquire skill (technical, professional, and managerial) leadership and positions of authority;
- To obtain new capabilities by making it easy for black persons and companies to do business with the company, ensuring that an increasing proportion of contracts are awarded to black owned businesses;
- To define a position;
- To gain access to new markets;
- To reduce risk, and
- To benefit from sharing resources.

Traditionally, potential BEE partners often do not have the same attributes as their empowered partners, due often to the lack of experience in the particular sector of the target company and, therefore, they have to add value in other ways. This lack of similar attributes could have a significant impact on success bred by mutual professional respect and on the basis of theory because the BEE partner is here viewed as an investor only.

Nompozolo (1998) researched the factors that contribute to the full success of BEE and identified those which promote the increase in BEE deals:

1. Globalisation;
2. Changing technologies;
3. Growing competitiveness; and
4. Emergence of new markets.

There is no doubt that through globalization South Africa has been exposed to numerous business opportunies. However, the globalization has played a major role in marginalising those potential BEE players who lack assets, skills and access to markets.

Ritchken (2004: 8) states that empowerment sensitive stakeholders are trying to facilitate a process of BEE through redistributing market opportunities. Whilst there is no way of predicting the success or failure of any particular empowerment deal or of the process as a whole, the way the market will respond to this redistribution will depend significantly on the criteria used to allocate the opportunity. The challenge to empowerment- sensitive

stakeholders is to construct a series of implementable criteria that will nurture a social transformation of business that is in line with building a globally competitive economy.

Dyer (2004:9) maintains that BEE is a vehicle for entrepreneurship. He states that BEE and entrepreneurship are regarded as critical drivers of economic growth and political stability in South Africa. Both are rich in theory and concept but encounter difficulties in execution.

The only way of achieving this economic growth and political stability is through financing or rather supporting the deals whereby the players demonstrate capability to be hands-on owners and fully involved in the day–to-day running of the business. This in a way minimises the risk of financing the new venture with minimal chances of being sustainable.

BEE transactions create different relationship dynamics among the partners as the motives for partnership are usually dependant on industry charter guidelines and /or political necessity. In essence, BEE transactions have the potential to enhance the company's competitive advantage, especially if the lack of a BEE partner in an organisation could result in loss of contracts or trading licences.

The main reasons for entering into BEE transactions are therefore, mainly a genuine desire to ensure the transformation of the economy; the desire to attract or protect lucrative government contracts; and the requirement of the legislation. These reasons in essence leave the possibility that the actual reasons for transacting could impact the business success as the BEE transaction would be a transaction whereby the Empowered Company / partner entered into, for the sake of complying with the regulations and the desire to prevent the loss of the market share.

The other reasons for entering into a BEE transaction include the following traditional business combinations i.e., expanding the supplier base, increased competitiveness, lower prices, and the attainment of a positive public image, reducing the risk of punitive government legislation and reinforcing the company's commitment to social development. However there is no single business combination could attest to satisfying all the motives noted in the literature.

For this research, the term BEE was used as the process of integrating historically disadvantaged people in the mainstream economy of sustainability of both democratic system and market economy.

2.1.1.2 BEE - enforcing legislation

New Acts or charters have not dealt with issues such as the concept of 'Fair market value" and exit mechanisms fully. It is therefore doubtful whether a vendor, in fact, obtains the fair market value since the market perceives the sale as a forced transfer of assets into the hands of relatively inexperienced players in the industry (DuMoulin, 2004).

In the first wave of empowerment in the mid 1990s, BEE deals meant, giving empowerment partners special-class shares that held no voting rights and that held diluted value. Currently, the requirements of the BEE Act and industry charters require full economic ownership and voting rights to be transferred to empowerment players. The transfer of full ownership and control in a way requires a lot of capital, which most BEE players are battling to come up with.

The literature highlights the importance and the prominence of funding structures in BEE deals. Special finance structures for BEE transactions have the potential to affect the business relationship between the partners and, ultimately, impact the success of transaction.

2.1.1.3 Current Perceptions of BEE

In 1993, Innes wrote that, "Often organisations have put blacks into token positions, using them simply as window-dressing to meet their legal requirements rather than empowering them within the organisation". Furthermore, Innes writes (1993) that affirmative action policies involve a two-stage strategy. The first stage uses legal quotas to force organisations to employ and promote blacks, and then, after blacks have gained a foothold in the organisation, they can work at empowering themselves.

Sethi (1989) states that corporate leaders are making an effort to promote black executives and technical personnel, including bursaries and scholarships to encourage more blacks to pursue their education. A study curried by the National Department of Education showed that between 1997 and 2007 the number of black students in tertiary education has doubled. In 2004 more than 50 per cent of tertiary qualifications went to black students (Right BEE mix, 25 May 2005: 6).

Kirwan (1995) states that there are four key ingredients for an empowerment program to succeed; top management must agree to support the program, that the program inauguration warrants fanfare, rewards must be offered for ideas generated and accepted, and, finally, that

training is essential for team leaders, programme coordinators and evaluation committee members.

According to Alberts, Coetzee, Coleman, Eloff, Marsden and Payne (1994:1), in order for real restructuring of ownership to be achieved, the commitment of three key role players are required, namely the Government, labour and business. Furthermore, the authors propose two particular options, or models, that have, the specific objectives of broadening equity ownership by black South Africans - the Community Growth Fund Model (CFG) and the Employee Share Option Schemes (ESOPS). The CGF model is a unit trust that was launched by the trade unions in June 1992 and it directs members' retirement fund savings into "socially responsible" companies. The funds of seven trade unions are currently invested through the CGF.

In a study conducted by Van Gass in 2005 it is evident that there is a shift in attitude occurring in business. In 2000, 57per cent of whites and 70per cent of blacks agreed, "blacks are as competent as whites". By 2004, these figures had increased to 73per cent of whites and 85per cent of blacks in agreement (Booysen, 2005). From this study, it is clear that there has been an increase in understanding and respect for all cultures in the workplace. According to the South African Communist Party (SACP), the failure to link Black Economic Empowerment Charters and the Growth and Development Strategy will result in charters operating parallel to, and even in contradiction with, any growth and development strategy (Banda, Herzenberg and Paramoer, 2003).

The Congress of South African Trade Unions (COSATU) has expressed concerns that while black economic empowerment is broadly defined, proposed measures often tend to focus on increasing black ownership amongst a few wealthy individuals, rather than on a broad empowerment process (Banda, Herzenberg and Paramoer, 2003). In a recent report, the International Monetary Fund (IMF) expressed some concern about South Africa's BEE policy, saying that there were insufficient safeguards against empowerment that would benefit small elite of black entrepreneurs rather than the greater society.

2.1.1.4 The Public Sector

Government institutions (i.e. National Department of Public Works, Transnet, Intersite and South African Post Office) can play a major role in presenting economic opportunities to the PDIs. Most emerging BEE groups focus on the massive portfolios of these institutions for

opportunities. This is because private companies are not sufficiently diligent to BEE due to the lack of skills among individuals from the previously disadvantaged communities. Also most importantly there is a concern regarding the difficulty in sourcing funding for BEE. Since most banks' funding systems subjects BEE players to rigorous vetting, these players usually do not make it through the bank system because of their financial records. The National Department of Public Works, through its incubator programme, is trying to assist the BEE groups, especially those without good financial records, to participate in this sector. In the incubator, business skills as well as property-related skills are encouraged.

2.1.2 Broad Based Black Economic Empowerment (BBBEE)

The Broad Based Black Economic Empowerment (BBBEE) Act No 53 of 2003 came into effect on 21 April 2004. The Code defines "black people" as "Africans, Coloureds and Indians but limits the term to South African citizens".

The three core components of BBBEE scorecard contained in the Codes are:

I. Direct empowerment (encompassing ownership and management indicators);
II. Human resource development (encompassing employment equity and skills development indicators); and
III. Indirect empowerment (encompassing preferential procurement, enterprise development and residual elements indicators).

BBBEE economic empowerment is described as the broadening of the beneficiary base to include all black investors, management, employees, and supplies and communities.

It is important to note that white women and disabled white women are not included in the definition of historically disadvantaged South Africans, according to the BBBEE Act (Singh, Jekwa, Ryan & Southey, and 2005: 20).

The BBBEE status matrix is given in Table 2.1

Table 2.1: BBBEE status Matrix

BBBEE Status	Qualification	Weighting
1	≥ 100 points on the Generic Scorecard	135per cent
2	≥ 85 but <100 points in the Generic Scorecard	125per cent
3	≥ 75 but <85 on the Generic Scorecard	110per cent
4	≥65 but <75 on the Generic Scorecard	100per cent
5	≥ 55 but <65 on the Generic Scorecard	80per cent
6	≥ 45 but <55 on the Generic Scorecard	60per cent
7	≥ 40 but <45 on the Generic Scorecard	50per cent
8	≥ 30 but <40 on the Generic Scorecard	10per cent
9	<30 on the Generic Scorecard	0per cent
Where any enterprise is in excess of 50per cent owned by black people, the BBBEE status of that enterprise will be at the level immediately above the level at which its actual score is evaluated		

Source: Department of Trade and Industry (2005)

2.1.2.1 The broad-based objective of the codes

One of the most common misconceptions about BEE is that it refers only to the transfer of ownership. The intention of the codes, however, is to be broad-based by including other areas or opportunities for transformation and upliftment. The outcomes of BEE must be far reaching and sustainable. This process is not without problems because some players abuse it by selling a significant percentage of the equity to a single individual black partner and therefore claim substantial compliance in this way.

These areas are further segmented into seven sub-sections or pillars. Each has been allocated a specific value on a scale of 100 – representing its level of importance and influence in relation to the goals of BEE. Figure 2 reflects the seven pillars.

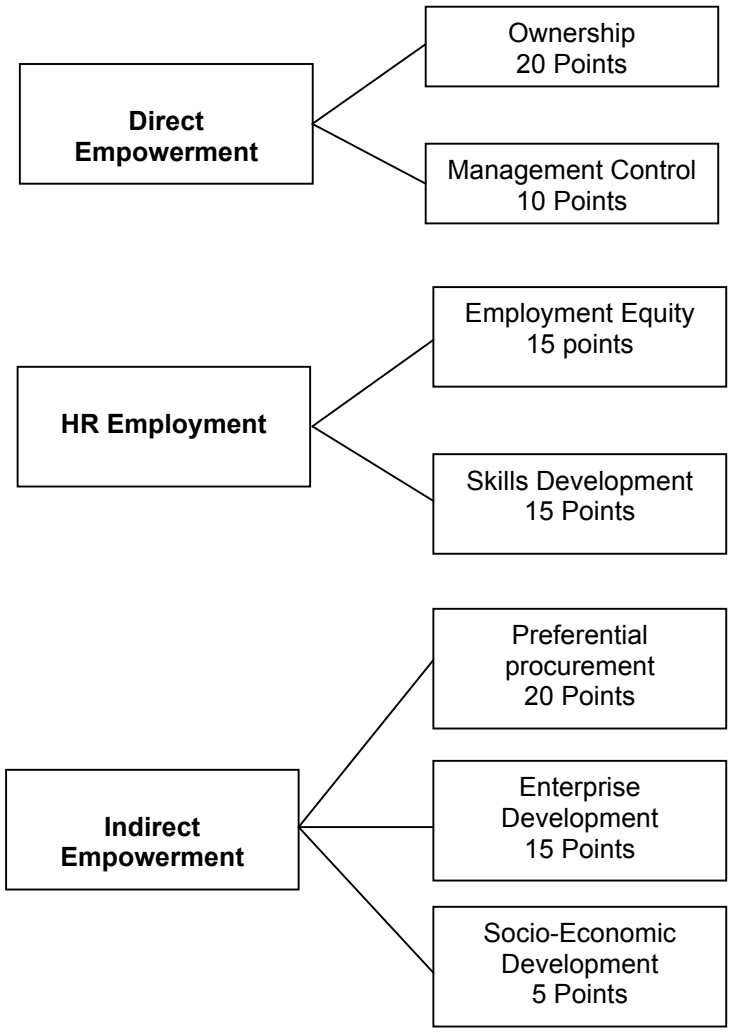


Figure 1.2: Empowerment scorecard Source: FNB (2009)

The codes have been designed to address these seven areas and provide detailed guidelines on how transformation should be implemented. From the allocation of the values, a score is calculated and a BEE rating is derived.

2.1.2.2 BBBEE Scorecard: 7 Pillars Explained

1. Ownership - 20 points

The transfer of ownership has long been a headline snatcher – possibly because the restructuring of corporate ownership has until recently been the *sole focus of corporate BEE efforts.*

2. Management - 10 points

The Codes highlight the need for the hands-on involvement of black people at the most senior level, giving them the right to drive not only the direction of a company, but also the implementation of strategic and operational decisions.

3. Employment Equity - 15 points

The employment equity element of the Codes is strategically aligned to the Employment Equity Act. If a company has proactively sought alignment with the Employment Equity Act, it is likely to score points in terms of this statement of *the Codes.*

4. Skills Development - 15 points

Having acknowledged that the skills shortage is a major constraint to economic growth, the government anticipates that renewed attention on skills development could deliver greater efficiency, increased productivity, and higher levels of competitiveness.

5. Preferential Procurement - 20 points

Preferential procurement has long been considered one of the most potent mechanisms to drive BEE. It has the potential to be one of the most effective and efficient ways of 'spreading' BEE compliance because of its multiplier effect.

6. Enterprise Development - 15 points

Government has singled out small, medium and micro enterprises (SMEs) as vital in the fight against poverty and unemployment.

7. Socio-economic Development - 5 points

Socio-Economic Development or Corporate Social Investment (CSI) is one of the most established routes used by companies to 'give back' to the society within which they operate and benefit, while building brand loyalty.

2.1.2.3 Explanation of the steps to follow for a successful BEE deal

Figure 3 reflects each pillar and its own area of focus:

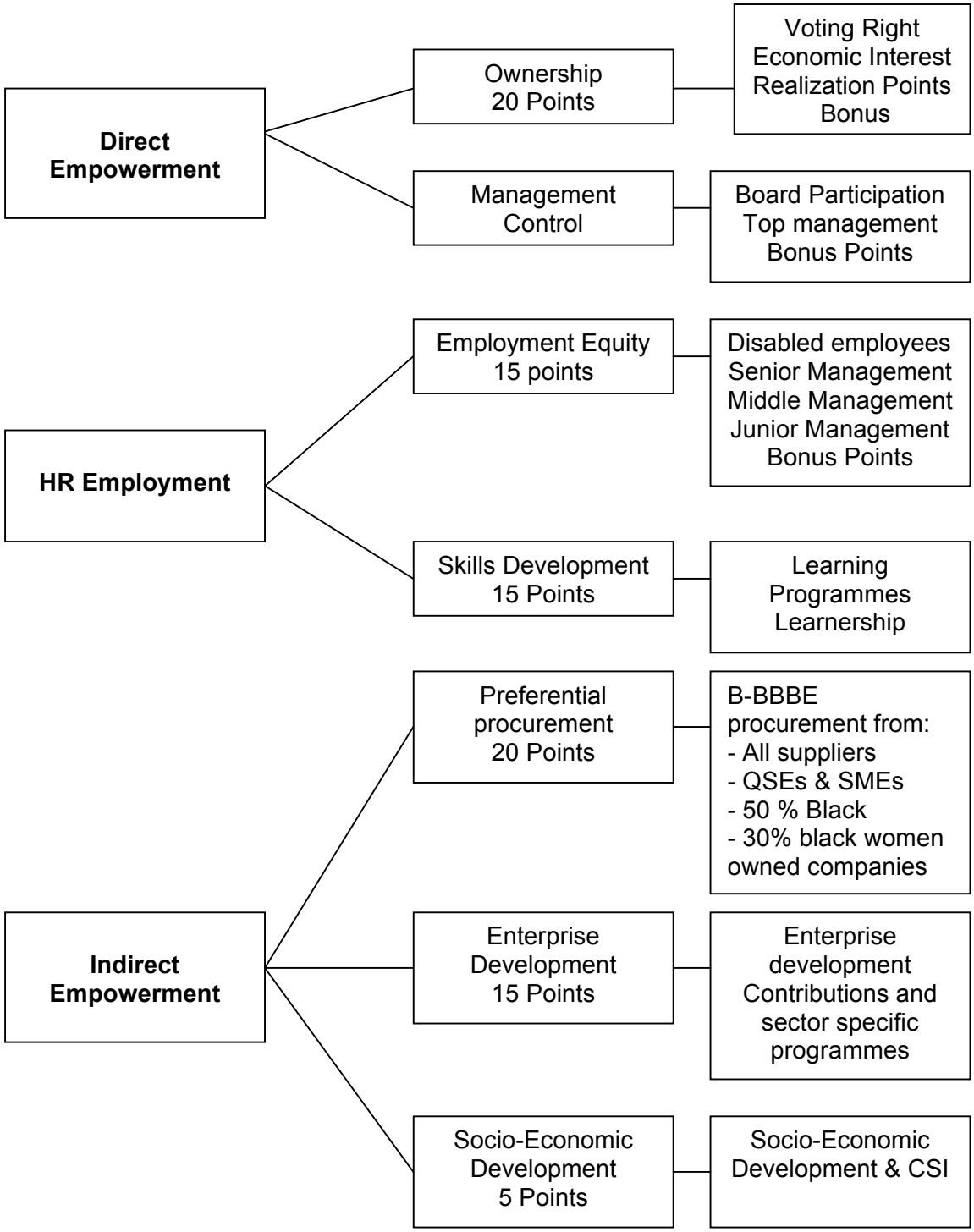


Figure 2.2: Pillars of BEE success Source: FNB (2009)

One of the most common criticisms of BEE, prior to the introduction of BBBEE, has been a lack of equality between its beneficiaries (Fine & Levin, 2005). Indeed, some black individuals have amassed huge wealth through BEE dealings whilst the remainder of the black population has barely benefited. The emergence of this trend is counter to the spirit of BEE and steps to counter it have recently come into existence (Fine &Levin, 2005).

In fact, many firms are engaging in subsequent BEE deals, usually with more advanced structures. These so called “broad based deals” include benefits to the community, women and the firm’s staff and are more in line with the Act (South Africa, Broad-Based Black Economic Empowerment Act, 2003)

It is possible that BEE deals that are broad based in nature may be viewed differently, as their risk of failure is very minimal since their role players are involved in the operations of the deal

2.1.3 Property Charter

2.1.3.1 Definition of charter

The charter, which is a voluntary process, once gazetted as a code of good practice will bind all enterprises in the property sector including but not limited to all property– owning enterprises (and / or the assets they) and property services enterprises.

2.1.3.2 Reason for Property Charter

The reason for the Property Charter is to adopt BEE and transformation in ownership, control, skills development, employment equity, procurement, and development of untapped areas. The Property Charter supports the commitment of all stakeholders within the property sector to strive for the transformation of the industry

The Charter can play an important role in unlocking the obstacles of property ownership and the effective participation of all South Africans in the property sector.

The Charter strives to encourage the investment in rural and under resourced areas. The development of commercial and industrial properties in which blacks participate, own, and control promotes the skills development of young people across all levels and, subsequently, their employability.
The DTI codes of Good Practice framework and measurements apply to the Property Sector Charter:

1. Ownership;
2. Control;
3. Employment Equity;
4. Skills Development;
5. Preferential Procurement;
6. Enterprise Development; and
7. Corporate Social Investment.

2.1.3.3 Process of the Property Charter

Figure 2.4 presents the process for the property charter.

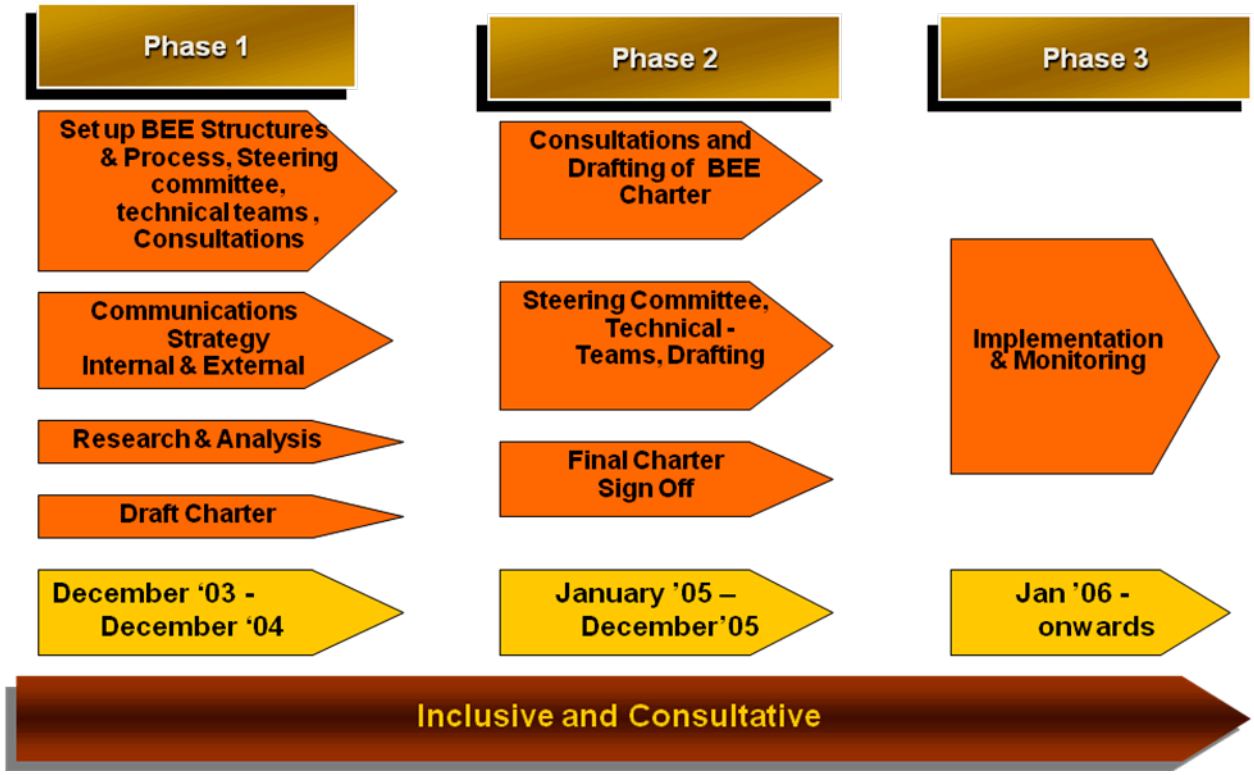


Figure 2.3: Process of the Property Charter. Source: www.propertycharter.co.za (Accessed, 16th Octobre 2011)

2.1.3.4 Participating organisations

- South African Institute of Black Property Practitioners – SAIBPP
- South African Property Owners Association – SAPOA
- Estate Agents Affairs Board – EAAB
- Association of Women in Property – AWIP
- Women's Property Network – WPN

- South African Black Technical and Allied Career Organisation – SABTACO
- SA Council of Shopping Centers – SACSC
- Institute of Estate Agents of South Africa– IEASA
- South African institute of Valuers – SAIV
- National Department of Public Works – NDPW
- Property Unit Trusts Association – PUTSA
- Property Loan Stock Association – PLSA

Source: www.propertycharter.co.za (Accessed on Novembre, 17th 2011)

2.1.3.5 The Charter Council

Table 2.2 presents the charter council and its stakeholders.

Table 1.2: The Charter Council

Composition and Seats of the Charter Council (Proposed)		
Stakeholder	**Representing**	**Number of Seats**
Nedlac / Organized Indirect Stakeholders	Women	**4**
	Youth	
	Labour	
	Communities	
Public Sector	All tiers of Govt.	**5**
	SOEs	
Property Services	Facility Managers	**5**
	Property Managers	
	Brokers	
	Estate Agents	
Owners	Institutions	**5**
	Private	
	PLS	
	PUT	
Regulatory	EAAB	**1**

Other relevant interest groups participating in the property sector as decided by the Council. e.g. Users	Proposed by the Council, approved by the Minister	Proposed by the Council, approved by the Minister

Source: www.propertycharter.co.za (Accessed on Novembre, 17th 2011)

2.1.3.6 Property sector scorecard

The table below presents the property sector score card.

Table 2.2: The Property Sector Scorecard

Element	***Indicators***	***Proposed Weighting***	***per cent Year Target***
OWNERSHIP (20 Points)			
Voting	*Voting Rights in the enterprise in the hands of black people*	*5*	*25 per cent plus 1 vote*
	Voting Rights in the enterprise in the hands of black women	*2*	*10 per cent*
Economic interest	*Economic interest to which black people are entitled*	*5*	*25 per cent*
	Economic interest to which black women are entitled	*2*	*10 per cent*
	Economic interest to which broad-based / designated groups are entitled	*1*	*2.5per cent*
Realisation points	*Ownership fulfilment*	*1*	*No restriction*
	Net equity value	*4*	*10 per cent - year 1* *20 per cent -year 2* *40 per cent - year 3 & 4* *60 per cent - year 5 & 6* *80 per cent - year 7 & 8* *100 per cent - year 9 & 10*
CONTROL (10 Points)			
	Members of the Board who are black people as a per cent of the board	*3*	*40 per cent*
	Members of the Board who are black women as a per cent of the board	*2*	*20 per cent*
	Executive Management who are black people as per cent of Executive Management	*4*	*40 per cent*
	Executive Management who are black women as per cent	*1*	*13 per cent*

	of Executive Management		
EMPLOYMENT EQUITY (10 Points)			
Senior Management	*Black Senior Management as per cent of total Senior Management*	*2*	*30 per cent*
	Black Women Management as per cent of total Senior Management	*1*	*15 per cent*
Middle Management	*Black Middle Management as per cent of total Senior Management*	*2*	*37.5 per cent*
	Black Women in Management as per cent of total Senior Management	*1*	*20 per cent*
Junior Management	*Black Junior Management as per cent of total Junior Management*	*2*	*40 per cent*
	Black Junior Management as per cent of total Junior Management	*1*	*20 per cent*
Property brokers / estate agents	*Black practitioners as per cent of total practitioners used*	*3*	*37.5 &*
	Black women practitioners as per cent of total practitioners used	*1.5*	*20 per cent*
	Black people in Management as per cent of total Management	*33*	*30 per cent*
	Black women in Management as per cent of total Management	*1.5*	*15 per cent*
	Compliance	*1*	*Yes*
SKILLS DEVELOPMENT (15 points)			
per cent of Skills Spend on black people as a per cent of payroll over and above the Skills Development levy		*7*	*1.5 per cent*
Learnerships – Black Learnership positions (as per cent of employees) (18.1 and 18.2)		*4*	*2.5 per cent*
Mentorships – Black staff on mentorships programmes as a per cent total staff (adult learnerships subject to verification)		*4*	*2.5 per cent*
PROCUREMENT (20 points + 2 bonus points)			
Procurement from BBBEE suppliers		*15 for 60 per cent 2 for 70 per cent (inc 1 bonus point)*	*70 per cent*
per cent Spend on Property Services Enterprises (Level 1 – 4) of total Property Services spend		*3*	*40 per cent*
Preferential procurement policies in place & mechanisms which verify BEE status of suppliers including the use of DTI approved verification		*2 (incl 1 bonus point)*	*Yes*

agencies.		
ENTERPRISE DEVELOPMENT (15 points)		
Proof of enterprise development programme in place	*1*	*Yes*
Disposal of assets to BNBBEE enterprises (Level 1 - $) as a per cent of total over 5 years	*9*	*35 per cent*
Quantifiable non-monetary support to BBBEE SMMESs (level 1 – 4) over 5 years	*3*	*3 per cent of net profit before tax*
Quantifiable non-monetary support to BBBEE SMMEs (level 1 – 4) over 5 years	*2*	*2 per cent of net profit before tax*
RESIDUAL (10 POINTS)		
CSI as a per cent of net profit after tax	*2*	*1 per cent*
Development investment in under-resourced areas as a per cent of total annual investments	*8*	*10 per cent*
Total	*102 points*	

Source: Department of Trade and Industry (2005)

2.1.3.7 Application of scorecard

Table 2.4 presents the application scorecard for property owners and services. See the calculations applied within the scorecard below the table.

Table 2.3: The application of scorecard

Elements	QSE	Property owners	Property service	Primary codes reference
Ownership	20	20 points	20 points	Code 100
Control	20	10 points	10 points	Code 200
Employment Equity	20		10 points	Code 300
Skills Development	20		15 points	Code 400
Procurement	20	20 points	20 points	Code 500
Enterprise Development	20	15 points	6 points	Code 600
Residual	20	10 points	2 points	Code 700
Total	100 points	75 points	83 points	

Source: Department of Trade and Industry (2005)

$$A = \frac{B \times D}{C}$$

Where:

A is the achieved score

B is percentage in the hands of black people

C is the charter compliance target

D is weighting allocated to the element

2.1.3.8 QSE Threshold

The table below presents the QSE threshold

Table 2.4: QSE threshold

		ASSET BASED	SERVICE BASED
Micro and very small enterprises… whichever is higher	GROSS ASSETS	R 30,000,000	R 3,000,000
	GROSS INCOME OR TURNOVER	R 4,200,000	4,2,000,000/ 1,000,000 (estate agents/property brokerages)
	NUMBER OF EMPLOYEES	20	20/5 (estate agents/property brokerages)

Source: Department of Trading and Industry (2005)

2.1.4 Financial Charter

First in a multi-sector suite of BEE charters, the Financial Sector Charter (FSC) is a policy document that aims to address issues of equity in the financial services arena.

2.1.4.1 Objectives

Aligned with the DTI's BEE Code of Best Practice, the FSC sets out a list of targets to be achieved by 2008 and 2014

Compliance with the FSC is measured using a scorecard that is used to track the progress of both signatory organisations and the sector.

A company's contribution to empowerment is measured against:

- Black ownership and management;
- A demographically representative workforce, i.e. employment equity;
- Investing in skills development and education;
- Level of investment in South Africa's infrastructure, housing, agriculture, SMEs and empowerment transactions;
- Preferential procurement in support of black-owned SMEs;
- Creating non-discriminatory workplace that embraces diversity;
- Facilitation of access to financial services across the socio-economic spectrum through education and product development; and
- Direct investments into community development projects.

2.1.4.2 Challenges facing the Financial Charter

In most economies the financial sector plays a central role in enhancing growth and development. The South African financial sector is generally recognised as world class in terms of its skilled workforce, adequate capital resources, infrastructure and technology, as well as a conducive operating, regulatory and supervisory environment.

However, the financial sector is confronted by a number of challenges which include the fact that:

- It is characterized by the presence of a few very large institutions, with many of the smaller and foreign institutions having exited the market in recent years;
- There are low levels of black participation, especially of black women, in meaningful ownership, control, management and high-level skilled positions in the sector;
- There has been an inadequate response by the sector to the increasing demand for access to financial services;
- The sector has not effectively provided credit to entrepreneurs, particularly black businesses;
- The national level of savings and investment is inadequate to support sustained economic growth and individual financial security;
- There is insufficient investment of the savings pool under the control of the sector into targeted investments of national priority;

- A large pool of funds circulates outside the formal financial system, including but not limited to funds held by stokvels, informal traders and in other forms of short-term savings;
- There has been limited support for new black firms in the financial sector by Government and the private sector.

By addressing the abovementioned challenges, the financial sector will make a significant contribution towards economic growth, development, empowerment and the reduction of inequalities and poverty in our society. The initiatives envisaged will also promote growth in the financial sector.

The growth and development of the financial sector is central to the successful implementation of BEE and is an overriding principle and objective of this charter. In order to enhance the financial sector's global competitiveness and to address BEE, the following imperatives must be satisfied:

- The long –term financial stability and soundness of the sector and its capacity to finance economic growth and to facilitate domestic and international commerce must be maintained;
- The sector's ability to provide appropriate and effective access to financial services for a greater segment of the population must be substantially enhanced;
- A savings culture must be developed in South African society;
- The pool of intellectual capital in the sector must be improved by focusing on attracting new entrants and continually investing in the skills development and training of existing and new black professionals and managers;
- The development of black strategic and operational leadership must be fostered within the sector;
- Diverse organisational cultures must be promoted to cater for a wide range of customers and to reflect the principles of inclusivity;
- The financial sector must promote triple bottom line accountability, including principles of good corporate governance;
- The representation of black women and black people living with disabilities in the sector as employees, managers, suppliers and owners of equity must be increased;
- Champions who understand and are committed to transformation are required at the highest level within each organisation;

- The number and quality of black firms providing services and products to the financial services industry must be increased and competition amongst domestic firms improved;
- Entrepreneurial development must be promoted and enhanced by supporting black entrepreneurs;
- The financial sector, which controls significant pools of savings, must be cognisant of the impact it has on directing savings towards targeted investments of national priority; and
- The regulatory environment and architecture of the sector must promote the empowerment objectives of this charter, lower the barriers to entry and facilitate competition.

2.1.4.3 Application of the financial sector charter

This charter applies to the South African operations of the financial sector. The targets in this charter will be applied from 1 January 2004 (the "effective date") until 31 December 2014.

In 2009 (based on the reports for the year ended 31 December 2008), the Charter Council will undertook a comprehensive mid-term review and make decisions regarding the implementation of the charter in its second term. The ownership provisions will be reviewed in 2011 to address identified shortcomings. The ownership provisions will be reviewed by the Charter Council in 2011 to decide what further steps (if any) to address identified shortcomings should be taken at individual financial institution, sub–sector, sector or national levels.

The parties to this charter agree that the principles contained in the charter will be relevant beyond 2015. In 2015 (based on the reports for the year ended 31 December 2014) the Charter Council will undertake a second comprehensive review of progress in terms of the charter, and draw conclusions as to the impact of the charter on the sector and the economy. The Charter Council will also make decisions as to what further steps (if any) to address identified shortcomings should be taken at individual financial institution, sub–sector, sector or national levels.

All the provisions of the charter are to be achieved in a manner consistent with sound business practice.

Certain provisions of the charter will not apply in the same manner to all financial institutions.

2.1.5 Codes of Good Practice

The Codes of Good Practice were released for comment in December 2004 for 60 days. All relevant parties gave their comments to the Industrial Development Corp (IDC). The purpose of the Code is to standardize all industries' Charters, especially the industries that have not finalized a Charter. Furthermore, the purpose of the Codes is to "assist and advise both the public and private sectors in their implementation of the objectives of the BBBEE Act" (Thale, 2005: 30). The Codes contains a detailed Scorecard that includes clear targets, weightings and indicators, all of which can be measured.
The Codes are meant to guard against fronting. Charters that do not reflect the Codes will be illegal.

Kevin Lester, a director at the firm Cliffe Dekker, estimates that there are currently 13 pieces of legislation that "impose ownership, control and management requirements upon enterprises". The difficulty is that their definitions are vastly different and that only the Act itself narrowly defines empowerment. Lester says that there are two possible solutions to the definition problem. The first, which is almost impossible, is for Government to amend every single empowerment instrument to align with the Codes and the Act, and the second is for the DTI to gazette specific Codes relating to each of the existing empowerment instruments (The right BEE mix, 25 May 2005:3).

Table 2.6 presents an index to the Codes of Good Practice.

Table 2.5: Index to the Codes of Good Practice

Code	Description
Code000	Framework for the measurement of broad-based black economic empowerment (BBBEE)
Code100	Measurement of the ownership Element of BBBEE
Code200	Measurement of the Management Element of BBBEE
Code300	Measurement of the employment equity Element of BBBEE
Code400	Measurement of the skills development Element of BBBEE
Code500	Measurement of the Preferential Procurement Element of BBBEE
Code600	Measurement of the enterprise development Element of BBBEE
Code700	Measurement of the residual Element of BBBEE
Code800	Sector Codes as defines in Code 000 Statement 010

South African Government: 2005

The Codes are categorised from code 000 to code 800 and each Code has its own sub–sections. This research focuses only on Code 500, which is preferential procurement. This by no means trivialises the rest of the codes; they are merely beyond the scope of this research.

Bonorchis (2005) quotes Gertenbach (2005) as stating that "the Codes were incredibly sophisticated set of legislation". According to Gertenbach non-compliance with the codes will not be interpreted as breaking the law. Neither will there be fines or jail terms (Bonorchis, 2005). This might undermine the significance of the Codes.

Three Codes and six Statements were released on the 31 October 2005. As stated by Bonorchis (2005), Code 000 will be covered in the seven Codes still to come; where the General Scorecard and the need for verification of empowerment credentials are set out. Companies have a year to become accredited.

Code 000 Statement 010 shows the gazetting procedure for the transformation process. It also shows that the Codes take precedence if there are any uncertainties about sector-

specific codes. Negotiable parts of the Codes are targets and weightings of the seven pillars of BBBEE, but sound economic principles could justify the difference sector specific codes.

Code 000 Statement 020 deals with the process of approving accreditation agencies by the Minister of Trade and Industry. There will be two categories of accreditation, broad-based and narrow-based. Verification certificates will only be valid for one year. Approval by the Minister is required at every step. Code 100 Statement 100 deals with an Ownership Scorecard and advocates the use of flow-through principle. There are numerous formulas to deal with ownership arising from the sale of equity instruments.

Code 100 Statement 101 shows what type of transaction qualifies as empowerment. Formulas are also provided here. Code 200 Statement 200 shows the scorecard. The Codes are in line with those from the King 2 Code, on corporate governance, and the Employment Equity Act.

Bonus points will be awarded for black independent non-executive directors (Bonorchis, 2005:5) The Codes have created uncertainty and many empowerment deals have been put on ice because under the current Codes of companies earn fewer empowerment points for all factors on the Scorecard (Singh *et al*. 2005:18).

Introduction of the Codes will mean that companies will need new accounting systems, new internal processes, and that they will generate large reports annually. This could be perceived as a negative aspect of the Codes (Bonorchis, 2005).

The purpose of the Codes of Good Conduct is to assist and advise the public and private sectors in their implementation of the BBBEE Act. The Codes of Good Practice provide principles and guidelines that will facilitate and accelerate the implementation of broad-based BEE in a meaningful and sustainable manner.

2.1.6 BEE Scorecard

The Scorecard is designed to facilitate the application of the Charter in terms of the Mineral and Petroleum Resources Development Act requirements for the conversion of all the "old order rights" into new rights within a five year conversion window period, but recognising the full ten-year period. The following are important notes on the Scorecard as identified by Mordant (2003).

1. Mining companies commit to offering each employee the opportunity to become functionally literate and numerate.
2. The mentoring of empowerment groups refers to that mining company's historically disadvantaged South Africans (HDSA) employees and HDSA linked partners at the levels of ownership and procurement.
3. The inspirational target for HDSA participation in management in a five year period. If companies want to convert licences within a much shorter time frame, then a phase-in approach will be adopted with companies to a 40 per cent HDSA participation by the fifth year.
4. The inspirational target for female participation in mining is a five-year target and the phase-in approach will be used.
5. Stakeholders' commitment to ensuring non-discrimination against foreign migrant labour.
6. In terms of the company's measures for improving the standard of housing, the company will be required to indicate what has been done to improve housing and to show a plan implementing and outlining the issue over time.
7. Companies have to implement measures for improving the standard of nutrition.
8. In terms of procurement, the mining company should commit to an increase of procurement from HDSA companies over the three-to-five-year time frame and agree to a monitoring system.
9. The Scorecard represents the five year targets and it has been agreed that within ten years the level of HDSA participation will rise to 26 per cent.
10. In terms of beneficiation commitments and the offset option, the key issue is to capture the actual beneficiation activities of a company and to convert it to the same unit of measurement of ownership.

The Generic Scorecard was formulated for the Codes of Good Practice and assigns the following weightings to the indicators. All seven of the pillars for BBBEE are visible with a clear indication of points that a company could earn if indicators are met.
Deviations in excess of 10per cent from the weightings contained on the Scorecard are not permitted. The Scorecard sets a target comprising 40 per cent for black persons in

management and allocates a weighting of 10per cent to management control. Based on overall performance in terms of the Generic Scorecard, a company will be evaluated and categorised into one of the following BEE (See Table 2.7) statuses and recognised at the corresponding BEE recognition level.

Table 2.6: Contribution and BEE recognition levels

Contribution Level	Qualification	BEE recognition level
Level one Contributor	≥ 100 points	135per cent
Level two Contributor	≥ 85 points but < 100 points	125per cent
Level three Contributor	≥ 75 points but < 85 points	110per cent
Level four Contributor	≥ 65 points but < 75 points	100per cent
Level five Contributor	≥ 55 points but < 65 points	80per cent
Level six Contributor	≥ 45 points but < 55 points	60per cent
Level seven Contributor	≥ 40 points but < 45 points	50per cent
Level eight Contributor	≥ 30 points but < 40 points	10per cent
Non complaint Contributor	< 30	

Source: Department of Trade and Industry (2005)

All the points shown in the qualification column in Table 7 are points on the Generic Scorecard. It is apparent from the table that if a company has more than 100 points on the Generic Scorecard that it will then receive a 135 per cent BEE recognition.

As points on the Generic Scorecard decline under the qualification column, so also do the percentages of BEE recognition percentages that a company would receive. The danger of the Scorecard is that it gives more weight to ownership and control than it does to skills development, which in turn will lead to companies only diversifying so as to not lose state business (Jammine, 2004). The rationale behind ranking organisations according to the Scorecard is to distinguish between what is described in the Codes as “narrow based BEE”, which focuses solely on ownership and management, which may lead to fronting, and BB BEE that covers all the elements of the Scorecard. In terms of the Scorecard, companies that comply with the criteria will earn 20 points for preferential procurement.

2.1.7 Similarities between the Property Charter and the Financial Charter

South African firms are obliged to report their financial results to the International Financial Reporting Standards (IFRS). “The aim of the IFRS is to create a single, cohesive set of accounting standards that can be applied worldwide” (Whitfield, 2005: 14). The problem arises when an employer gives shares or options to employees, because this must be put through his books as an expense on his income statement. However, it must now be decided whether options given to employees in empowerment deals be accounted for in the same way. The accounting standards, which will be issued soon, will govern the financial statement effect of empowerment deals, which could reduce the earnings of companies that complete such transactions (Right BEE mix, 25 May 2005:7). There are number of different ways that empowerment deals can be financed. The National Empowerment Fund (NEF) was established in terms of a 1998 Act of Parliament to create a trust for the promotion and facilitation of ownership of income-generating assets by historically disadvantaged persons. A commitment of R10 billion from the national treasury for empowerment has been set aside.

Other forms of funding are the Industrial Development Corp (IDC) and the Public Investment Commission (PIC). BEE approvals amounted to a third of the IDC’s total funding, or R2.1 billion, in 2004. Since 1990 the IDC has financed more than 625 empowerment deals worth more than R5.6 billion (Mahabane, 2004: 81-82). If a new entrepreneur needs to raise funds the IDC makes it possible; entrepreneurs only need to raise 2.5 per cent of their own capital to ensure funds of R1 million from the IDC (Finance Week March 2004:81-82).

The Public Investment Corp (PIC) entry into BEE financing has been controversial, as the PIC was using Government employee pension funds to invest in BEE deals. The PIC’s aim is to promote empowerment deals where BEE partners are operational and to ensure that those partners can sustain their businesses in the long run. Mr. Peter Schmid, managing partner at Actis is concerned that empowerment financing structures that attract high financing costs are in fact a form of disempowerment (Right BEE mix, 25 May 2005:14). These high financing costs are problematic as ordinary entrepreneurs will not have access to the necessary capital, and if they were in the position to acquire financing, paying off a huge capital outlay with exorbitant interest repayments would be detrimental to the initial decision to embark on an empowerment deal.

2.1.8 Obstacles to BEE

The following issues were identified by the ANC as obstacles to achieving real economic empowerment.

- A lack of commitment to real change by all parties;
- Opportunistic dishonesty, which tends to ride the wave of Government redress, for self interested parties;
- Black individuals or groups fronting for white establishments that wish to do business as usual;
- Rent-a-black schemes for the specific purpose of securing Government contracts or business;
- Black audited companies obtaining Government contracts and immediately selling them; and
- Blacks using whites for economic benefits and visa versa.

All these points defeat the real goal of empowerment and diminish the foundation for genuine transformation.
Obstacles to real empowerment are to be avoided.

2.1.9 Financing BEE

It is important to note that for BEE deals to be sustainable and viable; all parties involved should pay for the portion of the black economic empowerment deal being awarded to them. Without this, there are no profitable business opportunities that will be created and the economic growth of South Africa can not be ascertained.

One of the major limitations to meaningful transformation is the fact that very few people can afford to start their own business, as they lack the capital. Four sources of domestic funding support BEE initiatives in South Africa. They are the (NAMF), (IDC), (IFC) and the (NEF).

The NEF was set up eight years ago and, up until recently, has been labelled as the DTI's most dismal failure due to poor investment records, mismanagement and corruption. The NEF receives 1000 applications a month for financial support. At the end of the financial year, 31 March 2005, a mere R25 million was committed to 11 investments, but never disbursed.
The Financial Services Charter has ensured that financial institutions make funds available at affordable rates, but whether this will be successful is questionable (Booysen and Bouche, 2005b:57).

The researcher believes that if funds were more accessible and entrepreneurs were in a position to start their own business or start a joint venture with an existing company, fronting would decrease.

2.1.10 'Fronting'

In a recent article that appeared in the Engineering News, the Department of Public Works stated that it plans to submit the names of 15 companies to the National Prosecuting Authority (NPA) for criminal investigation following a probe into BEE fronting activities. A probe by the empowerment verification firm Verify Solutions found that over a two–year period from, 2003 to 2005, more than R440 million had been awarded to at least 15 companies that presented themselves as black owned or empowered companies.

A firm has been charged with fraud after it was discovered it had secured a multi-million rand deal to supply sirens to the police service. It listed a black woman who sells sweets and cakes from a backyard room as a 49 per cent shareholder in the company. The woman was paid a sum of R1, 000.00 for spending seven days at the company's offices.

Fronting poses a serious problem in the sense that it falsifies the BEE credentials.

2.1.11 Key success factors for implementation of BEE

Lusengo (1993:43) is of the view that in order to enhance Black Economic Empowerment, a consortium of employees and management who are now owners and co-owners of the company should implement the following:

- The adoption of a strategy to implement affirmative action;
- The establishment of trust funds to give employees financial assistance with health, education and housing;
- Active involvement in social enrichment programmes; and
- The formulation of guidelines for employment creation

During a Business Map presentation on 31 March 2004, the following six key success factors, as depicted in Figure 2.5 are required to make transformation work, these are:

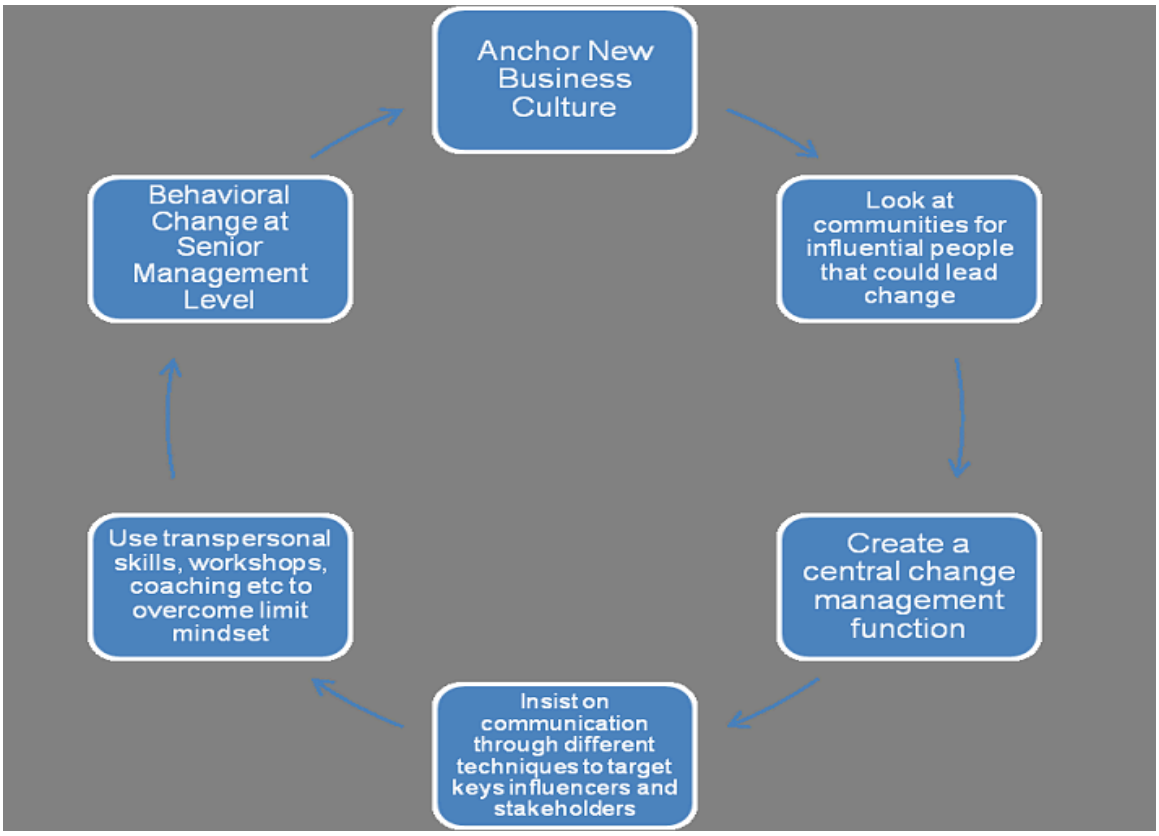


Figure 2.4: Six key success factor for BEE

From Figure 2.5 above, it is evident that the success factors needed for BEE are all linked together in a cyclic manner, and that all impact on one another. For BEE to be successful a new company culture needs to be established and agents of change need to be identified. Clear and open understanding will improve the chances of successful BEE. This can be achieved by having numerous workshops on BEE with the urgency of change.

The SME sector will be the engine for future economic growth. SME are also possible targets for many BEE players seeking equity deals. Pressure comes into play when companies need to procure goods and services from empowered companies to meet their own empowerment requirements. SME are then often faced with costly ultimatum of either transforming or losing their business (Booysen and Bouche, 2005a: 46). Additionally, these authors point out those forcing SMEs to give up control or sell is a “bitter pill” to swallow.

Recommendations made to ensure that SMEs remain meaningful contributors are that SMEs should be educated regarding black empowerment, and that assistance must be provided on how to introduce a black empowered partner (Booysen and Boucher, 2005a: 47).

Points highlighted by Booysen and Bouche (2005) should be taken into consideration to ensure that the right BEE partner is chosen.
The partner should:

- Be in the same industry;
- Understand the industry in which the SME operates;
- Know what challenges and opportunities are faced by the industry;
- Bring synergies and possible diversification opportunities;
- Have the potential to grow the organisation;
- Possess the necessary qualifications or industry experience;
- Have business acumen;
- Be able to add long term value;
- Bring other competitive advantages;
- Assist in transforming the SME;
- Identify new growth areas and strategies; and
- Contribute at management and operational level.

If these points are adhered to, SMEs will have a very positive future in South Africa.

From the literature review, it is clear that BEE and the Codes of Good Practice are hotly debated topics and that many authors have voiced their opinions. The literature review listed the history of BEE and then examined the current perceptions of BEE in South Africa.

There are numerous benefits and shortcomings to empowerment and this need to be taken into consideration. The Property Charter and the Financial Charter should work together harmoniously to ensure that empowerment deals concluded enrich of HDI. The different Acts that regulate this industry were discussed.

2.2 Risk management in financing BEE commercial and industrial property deals

Risk is defined according to Hertz and Thomas (1983) as to mean both uncertainty and the results of uncertainties. It refers to a lack of predictability about consequences in a planning situation.

The nature of commercial and industrial property investment in essence, is the improvement of interest in property that will yield expected cash flows in the future. This type of investment is long term in nature and it has uncertainties associated with its returns.

The primary task of any listed entity's management team is to create wealth for shareholders on a sustainable basis. It is through the creation of a sustainable value-adding business that all stakeholders can benefit and share in the wealth created (Cadle, 2004).

There are large risks in long term financing as it is subject to fluctuating interest rates. Investors determine the upper limit of such interest rates to hedge against these risks. Future trends point towards participation, accrual and convertible debt as investors' trade equity and cash flow in return for a lower debt service that results in lower carrying costs. Financiers, on the other hand, prefer to earn higher yields by equity participation.

The financial sector takes risks that it considers to be acceptable and at a price that will deliver an adequate return (Chicken and Posner, 1998:35).

The risks related to interim bridging finance relate to the amount of the loan, timing of loan proceeds, repayment schedule, and the cost of financing.

According to Wendt & Cerf (1969, p331) 'Portfolio decisions with respect to real estate investment must be made from the vantage point of the tax position of the investor, his knowledge and skills in Real estate analysis and management."

The researcher felt that in making a normal property financing decision, the financiers consider price, creditworthiness of the investors / partners, evaluation of the property, etc as the key determinants of financing commercial and industrial property deals. In evaluating BEE deals the financiers are supposed to identify measure and manage the risk associated with business operations, i.e. skill and knowledge of the industry, employment equity, ownership and control of enterprise and assets, indirect empowerment through preferential procurement

and enterprise development as the core components of BEE. These components should determine the financing of the abovementioned property deals and the sustainability thereof.

The implementation of the above demonstrates seriousness about employment creation which is the main objective of the South African Government.

2.2.1 Risk Management strategies

There are generic strategies, which include transferring the risk to another party, avoiding the risk, reducing the negative effect of the risk, and accepting some or all of the consequences of a particular risk.

Some traditional risk management strategies are focused on risks stemming from physical or legal causes (e.g. natural disasters or fires, accidents, death and lawsuits). Financial risk management, on the other hand, focuses on risks that can be managed using traded financial instruments, while business operating risk relates to general management, marketing ,personnel, accounting and cash management. The latter is the main focus of this research.

2.2.2 Property related risks

2.2.2.1 Business and credit risk

The concept of risk has three basic elements:

- the perception that something could happen;
- the likelihood of something to happen and
- the consequences if it does happen (Transfield Services, 2010)

In order to lower the risk of loans not performing the emphasis should be on quality loans and a risk portfolio not exceeding 5% (Dixon, Ritchie and Siwale, 2006:416). The quality of a loan is determined by the correctness of the credit decision when the loan is granted. As per Ojah and Mokoaleli-Mokoteli (2010:4), adverse selection arises when lenders cannot distinguish between safe and risky borrowers. Adverse selection as a component of information asymmetry is a problem of hidden information where the borrower has more information about the state of their affairs than the lender. Therefore, from the credit providers' point it is of utmost importance to obtain as much accurate information regarding the borrower to assist in the credit decision. Financial intermediaries, including banks, deal with the problem of information asymmetry in the following ways:

- rationing credit;
- requiring collateral;
- Screening applicants and monitoring borrowers.

There are principles to reduce financing risk in integrated financial systems that involve restructuring of internal management, improving appraisal of risk, developing tools for containing risk and some risk sharing procedures (Areyeetey, 2005:17).

Acquiring debt funding should be a process, not a goal and with optimal funding sources the property industry in South Africa can grow and be sustainable well into the future.

Reputation risk must be taken into account, as a bad reputation can ruin an entire investment deal.

2.2.2.2 Market risk

Marketability study has been defined as “a study to determine to what extent a particular piece of property can be marketed or sold under current or anticipated market conditions. It is inclusive of a market study of the general class of property being considered’ (Byrl 1975, p137) Marketability, in other words, is the ability of the market to absorb space with a specific use.

The estimation of annual income has risks to the extent that it does not fulfill market needs at the time or to the extent that there is oversupply in the market. Once the location and quality or environment criteria have been established, price becomes a major determinant. Price is a function of supply and demand of equivalent space and the structure, term and conditions of lease. The developer has to ensure that the effective net income covers all development costs to break even.

2.2.3 Risk analysis

Classical risk analysis provides a means by which the decision-maker looks ahead to the totality of possible future outcomes in evaluating whether a deal should go ahead. This evaluation decision is based on financial criteria such as Net Present Value (NPV) and Internal Rate of Return (IRR), or payback methods.

Risk analysis entails the identification, measurement and evaluation of risk associated in a decision-making situation. Risk analysis allows the manager to understand the uncertainties

surrounding the project in probabilistic terms. This is regarded as ‘better’ information compared to the single point best estimates that are employed in Basic Project Appraisal used extensively in current practice. The Decision Analysis `process includes the generation of risk attitudes, and is considered too complex to use. Thus, Risk Analysis `process can be considered the appropriated model to use in the appraisal of property projects. Empirical adjustments, more accurate forecasting, revising cut off rates, three level estimates and selected probabilities are some of the ways that decision-makers adjust for risk.

Risk analysis methodology includes the estimating of a range and the likelihood of occurrence of each value.

The underlying variables are to be structured in a tree diagram in a logical sequence to derive the project return. Problems in probability assessments include task and conceptual biases. The long term use of the model in practice can overcome some of the problems. The advantages of the model include the creation of a common base to evaluate strategic options, and a systematic and logical approach to decision-making. The model also sharpens the institution of the decision-maker when confronting risk, helps communication within the organization and allows itself to be tailored to specific situations.

2.2.4 Risk assessment

The recent financial crisis in 2008 / 2009 has proven that risk management practices are essential for small to large institutions and with Basel II the banking sector is advocating change in risk management policies. Effective risk management must be implemented in order to reduce fraud, stock losses and reduce overall company risk (De Andrade and Thomas, 2007:1577).

According to Cendrowski and Mair (2009:4), there are five steps in the risk assessment process, namely the enumeration of risks, qualitative analysis, and quantitative analysis, implementation of a risk management strategy and the assessment of the risk management strategy.

In order to complete a risk assessment one needs sound information to base one’s assessment on. This information should take on a strong future perspective and not only consist of historic information.

The fundamental difficulty in risk assessment is determining the rate of occurrence since statistical information is not available on all kinds of past incidents. Furthermore, evaluating the severity of the consequences (impact) is often quite difficult for immaterial assets. Asset valuation is another question that needs to be addressed. Thus, best educated opinions and available statistics are the primary sources of information. Nevertheless, risk assessment should produce such information for the management of the organisation that the primary risks are easy to understand and that the risk management decisions may be prioritised. Thus, there have been several theories and attempts to quantify risks. Numerous different risk formulae exist, but perhaps the most widely accepted formula for risk quantification is: Rate of occurrence multiplied by the impact of the event equals risk.

Research has shown that the financial benefits of risk management are less dependent on the formula used but are more dependent on the frequency and how risk assessment is performed.

2.2.5 Tools utilized by the financiers for efficient risk management

Cendrowski and Mair (2009:11) state that risk management strategy consists of the following:

a. Risk identification

This is the process of gathering information identifying possible risks then listing various problems related to potential risks.

b. Risk evaluation

In this phase, the consequences of each risk on the list should be determined especially for the different stakeholders, namely customers, suppliers, employees, directors, shareholders and so forth. The next step will be to evaluate the existing current control measures in place to mitigate these risks. Risk evaluation can be seen from the two perspectives of probability and magnitude.

c. Risk mitigation

After risks with their consequences have been identified and controls have been evaluated, a risk mitigation strategy should be implemented. Risk mitigation strategy focuses on risks that seem intolerable to the financiers. Following identification and evaluation, the implementation of risk mitigation then resumes. This process involves revising of new controls or the removal of factors that cause these risks. This section will therefore focus on decreasing the probability that an event occurs and the magnitude thereof if it occurs. If risk tools manage to combine the aspects of probability and magnitude, risks will be minimised effectively.

2.2.6 Risk management

The objective of risk management is to reduce different risks related to a pre selected domain to a level accepted by society. These objectives may refer to numerous types of threats caused by the environment, technology, humans, organisations and politics. On the other hand it involves all means available for humans or, in particular, for a risk management entity. In the South African context the focus is more on the organisation and politics.

A distinction between Risk measurement and Risk Management needs to be made. Risk measurement, be it market, credit or operational risk, is only the foundation for the process of managing risk. Once risk exposure has been quantified, the process of making decisions based on the measured risk begins.

Risk management developed from insurance-buying activity and for this reason risk managers had initially restricted their task to the handling of insurance risks only. But today risk management is viewed as a fully fledged management function that is beginning to move into areas that were originally considered unrelated.

One of these areas could be Commercial and Industrial Property industry and, therefore, this discussion will look at the concept of risk management with special reference to the property industry.

Chofaras (1990, 6) asserts that risk is no alien concept in the financial industry. However, today more than ever financiers appreciate that the position taken by the financial institutions must be controlled. One of the worrying elements writes Chofaras (1990) is the increasing number of defaults. Another source of worry is that in the middle of many risk calculations there are often one or two, mythical assumptions.

A precise definition of risk management would depend on the type of business under consideration, writes Nielsen (1988 p, 16). For an insurance company, risk management is essentially the management of physical risk, as well as procedural risks such as errors and omissions. Banks face procedural risk too and the more automation encroaches upon the dealing process, the more such risks will increase. Banks use consultants to take an overall view of managing the totality of risk. Looking at risk management from this point of view normal bank credit risk is replaced by looking at the dealing environment, moving from the fairly conventional and traditional environment to swaps, options, Fixed Rate Agreements (FRAs) and so forth in a more complex environment, and then to asset liability management.

2.3 Mortgages bonds

Property finance loans are usually secured by a mortgage bond registered over fixed property or other long-term assets owned by the borrower. Most commonly they are registered over specific properties, but collateral bonds may be registered over many assets (Ross, Westerfield and Jaffe, 1990). Notarial bonds may be registered over movable assets.

In South Africa, most mortgage bonds are passed by the owner of a property (the mortgagor) in favor of a creditor (the mortgagee) over a specific property (Scott and Scott, 1987). Only the registered owner pass the mortgage bond, and there must be a cause or actual debt incurred. A mortgage bond is a real right, and a conventional security. The real right cannot be created by agreement, but arises following upon an agreement, by registration (Gibson, 1966).

A first or senior mortgage bond has prior claims on assets and earnings over subordinate liens such as second or third mortgages. Moreover, most mortgages are limited open–ended mortgages, where additional mortgage loans can be registered, but the senior mortgages are fully secured creditors for the full amount owing them, (Weston and Brigham, 1968). Consent for the registration of subsequent mortgages must be sought from all prior ranking mortgages, in order of seniority

A popular South African property vehicle is Participation Bonds where participating investors are assigned to specific property loans. This method is tightly prescribed by the Participation Mortgage Bonds Act (No. 55 of 1981) and may only be carried on by registered (1990) schemes in terms of the Act. Other lending institutions providing property finance are subject to the Deposit Taking Institutions Act (No. 94 of 1990) and the Companies Act, where appropriate .These institutions are supervised by the Financial Services Board, under the Department of Finance. Private persons or companies may also provide mortgage finance, and these bonds would be registered in the normal way.

2.4 Services

The provision of property finance is a service. Bendixen (1991) summarises the research conducted by the students of the University of the Witwatersrand's Graduate School of Business Administration on the evaluation processes of goods and services. Bendixen (1991) concludes that the distinction between goods and services is not simple. He criticises suppliers who emphasise low price where price and image may compromise quality. He also criticises financial institutions for advertising lofty corporate images and specific products, where the consumer evaluation process is in fact characterised by staff, premises and word

of-mouth recommendation as cues to quality. The research on the property financing industry examines whether the perceived quality of property-financing services is in fact related to the above factors, such as pricing, quality of staff and reputation.

Lovelock (1981) developed a paradigm of the service operations system, service delivery system, and service marketing system. Lovelock (1981) maintained that “a whole host of features “in a service business are evident to one or more of a consumer’s senses. The service marketing system represents all the ways in which an organisation touches customers. In a property finance industry context, these service industry systems are easily identifiable The service operations systems exists in the financing supplier’s back offices; the service delivery system is usually a consultant, valuer or representative or a branch officer like a branch manager, as well as the customer. The marketing system is manifested in the persons representing the institution plus all additional materials and image factors presented to the customer.

The nature of services as distinct from goods is addressed by Zeithaml (1981) who concludes that unlike goods, services are intangible and nonstandard and have inseparable production and consumption processes. Zeithaml proposed eleven hypotheses concerning the differences in the evaluation of goods versus services by the consumers. Subsequently Venegas (1990) tested the hypotheses in the office supply market, but found that only four of the hypotheses were supported. Tal (1991) researched service quality in process engineering, and found only two of the eleven hypotheses supported. The production and consumption of property finance services are inseparable, and the product is intangible and nonstandard, corresponding to Zeithaml’s original conclusion.

Booms and Bitner (1981), like Zeithaml, aver that services are different from goods, demanding a different marketing approach for services. Brown and Fern (1981) also examined the differences between goods and services, but concluded that whether the core offering is a good or a service is not relevant. What does matter is that the total offering be properly marketed. Property finance is undoubtedly a service, displaying the overt characteristics described above. Nevertheless, the core offerings of the property finance product have valid marketing implications regardless of whether it was a service or a commodity.

Parusanaman, Zeithaml and Berry (1985) examined perceptions of service quality, identifying gaps between the perceptions of service company management, and the perceptions of

customers. From this, they identified ten determinants of service quality, covering reliability, responsiveness, competence, access, courtesy, communication, credibility, security, understanding / knowing the customer, and tangibles, all of which can be applied to property financing services.

Zeithaml, Berry and Parasuraman (1988) further developed the “Servqual” instrument for measuring perceptions of service quality, operationalising the ten dimensions above to the following five dimensions: tangibles, reliability, responsiveness, assurance and empathy, which they held to be generic to all services. In the property financing service, tangibles are factors like price and rates ;reliability relates to initial processing and particularly the backup service, responsiveness is a vital component of initial contact; assurance relates to the integrity of the institution and its representatives, and the trust that the customer has in the company, people and process; and empathy is contained in the personal factors both in the beginning and the ongoing relationship, as well as the feeling that the company understands the needs of the customer.

Carman (1990) tested the ‘Servqual” instrument on retailers and concluded that, although useful, it was not entirely generic or applicable to all industries. He concluded that it needed modification to suit different industries.

Bitner, Booms and Tetreault (1990) researched what they termed the “service encounter”, maintaining that the encounter is in fact the service, as perceived by the customer. These authors concluded that the five generic “Servqual” dimensions referred to above relate directly to the human interaction element of service delivery. Property financing initially consists almost entirely of human interaction dimensions. In later stages of the process more automated elements are introduced in supplying the service, but human interaction remains a feature for the duration of the relationship.
In contradiction to the abovementioned efforts to evaluate goods and services, Enis and Roering (1981) maintain that from a marketing perspective, a bundle of benefits is in fact marketed, and that the issue of whether they are goods or services is not relevant. Bendixen (1991) writes that there is a substantial body of research indicating that a simple distinction between goods and services is inadequate, and that the concept of a “bundle of benefits” should be taken into account.

In property finance the framework of time involves the responsiveness in the initial application for finance, and the time it subsequently takes to register a mortgage bond. Fault freeness is a vital feature of the legal documentation, valuation and loan proceeds paid out, as well as

identification of the correct property, town planning considerations, risk assessment and many other aspects of property finance. Flexibility, and the “soft” dimensions of style, steering and safety are important features of property financing services, and were all examined in the research.

Dwyer, Schurr and Oh (1987) developed a model describing the relationship development process between buyers and sellers. They identified five major phases in the process: awareness, exploration, expansion, commitment and finally dissolution. They contrasted discrete transactions with relational exchanges for both situational characteristics and process characteristics and process characteristics. The property financing transaction is not a discrete transaction but exists over a long period. This would seem to indicate that the five phases of the relational exchange should be manifested by this service as well.

2.5 Conclusion

Black Economic Empowerment as a subject has been defined by the BEE Commission as a strategy aimed at sustainability as well as increasing black participation at all levels in the economy. BEE has been identified as a strategic priority by many businesses. It is believed that the future business success and the maintenance of enterprise viability will to a large extent depend on a successful implementation of the codes of good practice within the empowerment programme.

In making a normal property financing decision prior to the implementation of the BEE Code of Good Practice, the financiers would consider price, creditworthiness of the investors / partners, evaluation of the property, etc as the key determinants of financing commercial and industrial property deals. Factors such as ownership, control and operational involvement remain the key priority of financing BEE deals as the absence thereof pose the risk to sustainability of these deals.

The use of risk analysis both as a decision making and a monitoring tool allows user to increase their awareness of the behaviour of variables. The model has great potential if it becomes an accepted part of operational management and if there is commitment on the part of the top management of the empowered partners as to the intention of the model.

Out of the primary variables such as Value, Building, Finance, and land, Value has the highest degree of risk associated with it followed by land then Finance. The building variable has generally the least variability about the best estimate because of the planning effort that is

involved prior to decision making. In a situation where land is still to be purchased, the planning effort is minimal and therefore this variable is less certain.

The variables of price unit/ space and vacancy are considered the most uncertain of the selected variables because of the impact of the dynamic environment in which these variables are being assessed, and the uncertainties inherent in the future period of assessment. Developers often hedge the risks in these variables by preleasing where possible. Value at the end of economic life is considered to be highly uncertain, but because the event is based in the distant future the net present effect of this variable is minimized.

In the situation where the land has to be competitively purchased, the purchase price is subject to uncertainty and the therefore, must be described in probabilistic terms in a model. The uncertainties in the cost of finance relate to fluctuations in interest rates and the occurrence of cash outlows based on construction progress.

The contingency variable is specifically designed to cushion the downside risks in building construction. It is a variable that by itself is subject to lesser uncertainty

The preliminary risk analysis framework is based on the residual method of valuation of commercial and industrial property which is extensively used in practice.

In current practice Internal Rate of Return (IRR) is the commonly used criteria for the measure of worth in property deals although decision –makers are generally aware of the Net Present Value measure, it has been found not to be the norm in financing decision – taking NPV has the clear advantage over other approaches. It gives an unambiguous measure of value of the individual project thus enabling proper comparison. If the project is accepted a positive NPV, indicates the size of the expected increase in the value of the firm. Further research and testing in practice need to be carried out before conclusions on its applicability in the field can be made

Ownership is meaningless without a translation into profit. Focusing on ownership alone without adding operational value decreases the chances of generating profit and operational success subsequent to the BEE transactions. It is also often important that the BEE transactions extend its influence in ensuring that operationally the BEE partners and their representatives are involved. The acquisition of skills that will be associated with the

traditional business combination would be irrelevant in a BEE transaction as the transaction takes place at the ownership level and not in operational level. The attendance at Board meetings and shareholders meetings by the BEE partners could compromise the potential operational efficiency that a business combination could bring. The financiers for BEE deals need to guard against the increase sensitivity related to black ownership but white control and management as risk factors to financing the BEE deals. The perception of empowering black people is becoming more and more important in winning new business and is therefore a success factor for BEE transactions.

The importance of people's understanding of BEE as well as the value added by the participants was highlighted while defining business risk and its management and that has demonstrated that implementation of the core components of BEE have effect on the sustainability of such deals. This has provided the framework for further investigation.

CHAPTER 3: RESEARCH METHODOLOGY

This chapter covers the methodology applied within this research study. A combination of different methodologies was utilised for the study and covered both the secondary and primary data collection and analysis methods.

The reason for combining multi-methods in this study is to enable triangulation or greater validity to take place and therefore ensure that the data used is consistent and the results are both valid and reliable (Bryan, 2012). Smith (1975) argues that each method, tool or technique has its unique strengths and weaknesses. All methods have different effects. Therefore this combination will cancel out the method effect.

Figure 3.1 below illustrates the research process used in this study. The process was divided into four main phases which are as follows:

1. Qualitative exploratory research
2. Problem re-conceptualisation and questionnaire development
3. Sampling and quantitative data collection
4. Analysis reporting

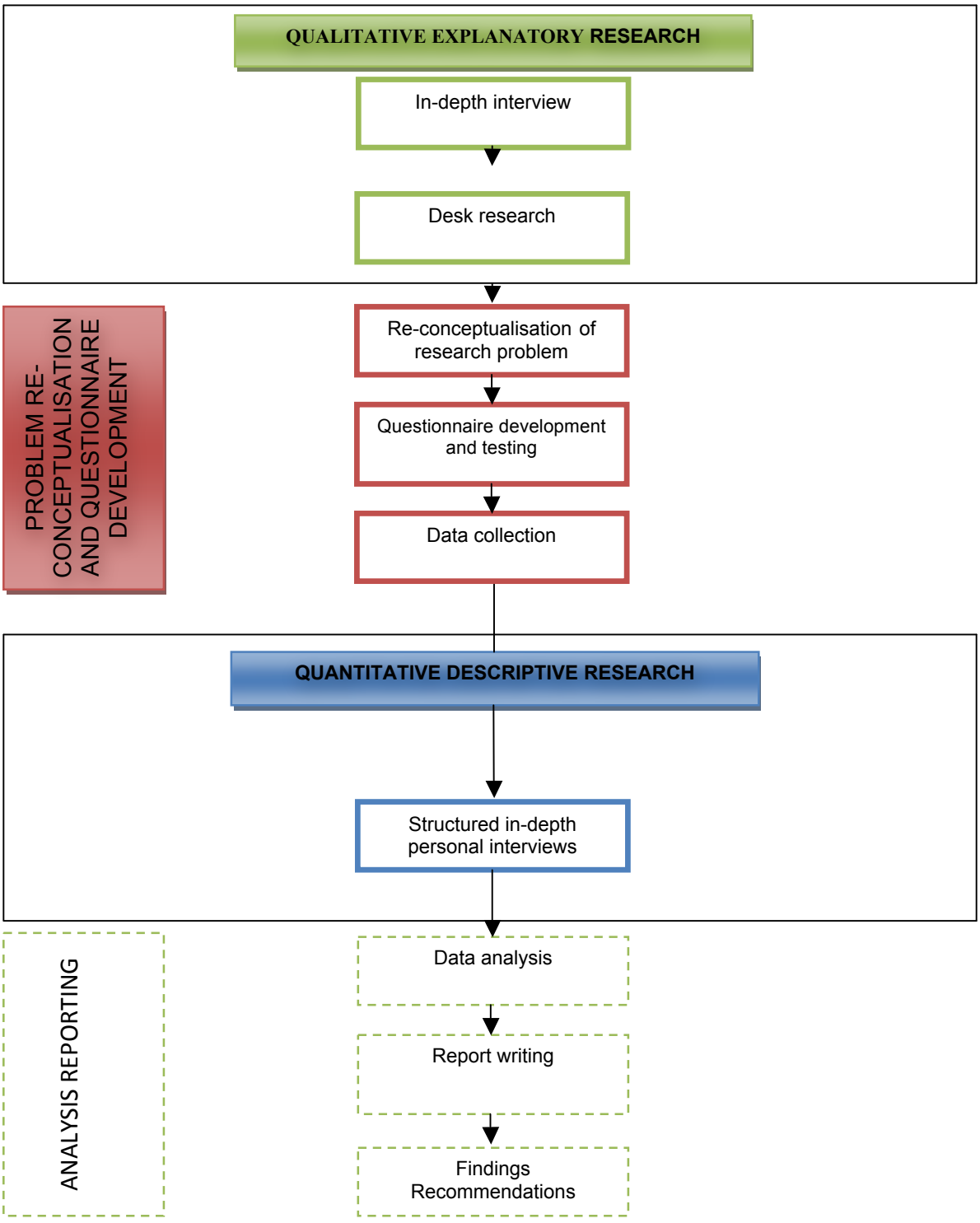


Figure 3.1 Research methodology process. Adapted from Access Market International Working Document [cited in Le Roux (2003)]

3.1 Phase one: secondary research methodology

The secondary research consisted of desktop analyses of all relevant documents, previous research carried out and existing reports on BEE, specifically within the property sector. The starting point was to gather and analyse historical and background information on the BEE legislation and to understand different aspects of financial and property charters.

The sources of secondary analyses included:

- Documentation from various support services institutions
- Publications
- Electronic journals
- Journal articles
- Books
- Internet searches

Specific Government documents such as Charters, Codes and Acts were also analysed to ascertain Governments' thoughts on BEE and to understand what the Government has envisioned for the future. Other government—related legislations and documentation from the DTI were also reviewed to understand which policies and structures have been put into place, and to gain insight into how these policies have been implemented.

Archives and related documentation and reports from the participating companies were also accessed and analysed for more company—specific data. Over and above the highlighted intentions for this phase, the process was aimed at understanding these companies' past approach to and behavior in relating to the implementation of BEE and gain an overall understanding of companies' cultures and their perceptions on Black Economic Empowerment and the Code of Good Practice.

3.2 Phase Two: primary research methodology

The secondary data analysis methodology formed a base for phase two of this research. The data analysed from phase one provided guidance on key themes and questions to ask in phase 2 of the research – the primary research methodology. Primary data collection combined three different types of methods for both data collection and analysis purposes.

These were:

- The Delphi technique
- The qualitative method
- Some quantitative and observational data collection methods

The reason for combining all four methods was to make sure that the data collected was rich enough and that nothing was missed and also to supplement the findings from each other in yielding different information needed for key questions raised.

3.2.1 Delphi technique

The Delphi technique is defined as a judgmental forecast that is very useful for generating ideas about unstructured or relatively less developed subject areas (Swanepoel, Erasmus, van Wyk & Schenk, 2003). It was developed as a way of obtaining experts' opinions without necessarily bringing the experts together face to face.

Furthermore, this method enabled the researcher:

- To achieve "oneness of mind" through a three step process of thesis, antithesis, and synthesis. In thesis and antithesis, all participants presented their opinion or views on a given issue or question, establishing views and opposing views. In synthesis, opposites were brought together to form the new thesis.
- All participants were then encouraged to accept ownership of the new thesis and to support it, changing their own views to align with the new thesis. Through a continual process of evolution, "oneness of mind" was then supposedly achieved, specifically around the issues intended for this particular research.

The entire thesis identified within this method then provided a further base for the other two main research methodologies and their analysis processes.

3.2.2 Qualitative methodology

The main aim of qualitative method was to enrich and expand on the data collected from the previous method and to provide the kind of contextual factors not easily captured in the Delphi technique and a brief quantitative research methodology. This method was chosen based on the study purpose, the research strategy and the background of issues under investigation, i.e. BEE legislation, its implementations, and the risk and challenges experienced (Mehmetoglu and Altinay, 2005: in press). According to Peshkin, (1993) and Leedy and

Ormrod (2005: 134), qualitative research methods typically serve one or more of the following purposes, hence their use within this specific research:

- To enable a researcher to gain new insights about a particular phenomenon;
- To develop new concepts or theoretical perspectives on the phenomenon, and/or
- To discover the problems that exists within the phenomenon.

The qualitative methodology further revealed the nature of certain situations, settings, processes, relationships, systems or people. For this specific study current status of BEE, applicable legislation, key players, risks and the management of them, challenges and processes of implementation were revealed in the report and analysed. This method also provided a means by which a researcher judged the effectiveness of particular policies, practices or innovations. BEE policies and instruments of implementation were analysed and their progress determined.

3.2.3 Quantitative data collection

Quantitative data collection was also incorporated, especially within the questionnaire developed for data gathering. This method assisted with the development of a questionnaire that contained both structured and semi-structured questionnaires. It facilitated the processes of asking the same questions to all participants (See Appendix A).

Structured and semi-structured questionnaires or schedules were used for both individuals and/or company representative's in-depth interviews among the key role players in the property sector in order to gain a detailed understanding of the topic under investigation.
Furthermore, the questionnaire covered both the closed—ended and open—ended questions, which were posed during face—to—face interviews and was verified during the discussions with experts with the field. (See Appendix A for a schedule of questionnaire utilised). The questionnaire consisted of specific items that are asked of all participants, and responses were initially restricted to a pre-defined range of themes (Page et al 2004:111).

Although the main objective of the interviews was to gain an in-depth understanding of BEE and its risk—related challenges in the commercial and industrial empowerment deals, the participants were also encouraged to add or offer their opinion and perceptions about the current business situation (Yin, 2002) for the purpose of enriching the data being gathered.

The process of collecting data was two-fold. Firstly, a letter was sent to the targeted population explaining the purpose and scope of the research and formally inviting them to participate. Secondly, the developed schedule or questionnaire was also sent to participants who responded positively. This second process also served as foundation for the interviews conducted afterwards.

3.2.4 Observations

The observation method was also used to supplement findings from the above mentioned research methodologies. This enabled the gathering of the non-verbal information or participant's behaviour during the interview processes.

3.3 Research sample

The non-probability sampling methodology were used to select the sample for this research study, mainly because not all participants had a known chance of being included in the sample (Lind, Mason and Marchal, 2000), In support of this, Pirow (1990) emphasises that "the major requirement of non-random sampling is that the onus is on the researcher to prove the fact that the units chosen are in fact truly representative of the population being considered". In the case of this research the population was selected for their opinions on BEE and the selection was based on the judgment of the person conducting the research.

Therefore, the non-probability sampling included both the purposive and snowball sampling methods. A purposive sampling method was used to select the targeted audiences and key informants and/or key stakeholders interviewed. Key informants included identified group of experts from the insurance industry, financial institutions, and stakeholders in empowerment property deals and government institutions. Since the unit of the research study was the commercial and industrial property sector, a total of 20 company representatives — managers — were interviewed from these two South Africa industries.

A snowball sampling method, through discussions with some of the experts within the identified industries, further enabled the referrals and identification of other relevant companies to be included in the study.

The research sample comprised of directors / managers and senior managers who are employed by companies and private and public institutions dealing with Black Empowerment in South Africa and insurance companies involved in the empowerment property deals. These included companies like SASFIN, Old Mutual, Investec, Credit Guarantee Insurance

Corporation, Liberty Life, SANLAM and AIG. The financial institutions and banks involved in the deals included Rand Merchant Bank, Investec, Standard Bank, First National Bank, ABSA, NEDBANK, and venture capitalist like Quick Berry, SAVCA, HBD and IDC.
Other stakeholders like PIC, BEE partners, Empowerdex, security companies and the Black Management Forum and Government Ministries dealing with empowerment deals also formed part of the sample. In selecting all these institutions and/or their representatives, it was assumed that the abovementioned group would elicit the true reflection of what was intended to be investigated. Furthermore, the literature reviewed with regard to the Delphi technique indicates that the information gained from these participants was as good as the selection of the experts.

3.4 Data analysis

As highlighted earlier in this chapter, data analysed was from both secondary and primary data collection methodologies, with the latter collected mainly through structured and semi structured interviews. The collected data was further grouped (from the Delphi technique and the qualitative method) into key themes, transcribed, and translated with quality control checks done on all interview data.

The transcribed data was then analysed, in relation to the themes and the contents of the responses. As part of the Grounded Theory for research, a content analysis of the data gathered was applied. According to Kassarjian (2001), content analysis is a systematic technique for analyzing message content and message handling and for observing and analyzing the overt communication behavior of selected participants.
Again, the content analysis method within this study enabled the measurements of the semantics within the content of messages from the respondents (Cooper and Schindler, 2003) and, as a flexible and wide-ranging tool, it also helped with the identification of specific problem, key objectives and a systematic quantitative description of the content (Berelson, in Cooper and Schindler, 2003). Once the content and concepts were analysed and grouped per different themes, they were then narrated and codified, given meaning as per the key questions asked and summarised as key research findings (Coffey and Atkinson, 1996; Mehmetoglou et. al. 2005). For this research the interview findings were then analysed as per the Grounded Theory approach (Burnard, 2003).

3.5 Data quality control

The quality control method was applied throughout all the research methodologies or processes highlighted earlier. For instance, after every interview, the recordings were

immediately transcribed to ensure that the researcher recalled all the responses provided and any particular behaviour observed during the interview process. The transcribed interviews were then sent back to each of the company representatives for verification and approval. This was done not only to ensure the correctness of the findings, but also because of the sensitivity of this research.

The final outputs on the data analysed and the judgments made by the researcher informed the next two chapters of this research report.

CHAPTER 4: PRESENTATION OF RESULTS

The objective of this chapter is to present and discuss the results of the in-depth, semi-structured interviews conducted with the respondents. Comments from the interviews are used to seek meaning in the results as well as to obtain insight into the determinants of success for BEE transactions.

The research conducted involved the analysis of both the secondary and primary data collected. This incorporated public documents, reports and literature reviewed on issues under investigation and the direct discussions and interviews with BEE stakeholders and participants. The purpose of this chapter is, therefore, to provide a summarised overview of the outcomes of the responses from institutions dealing or partnering with BEE— i.e. insurance industries, banks, trading houses, the property valuation market as well as property investment companies. As highlighted in the previous chapter the results also reflect a combination of analysis from various sources that provided a perspective on the general understanding of BEE, measures used and the precautions to be considered in financing these deals as a form of risk management in an effort of ensuring their sustainability.

The first round of open—ended questions facilitated a clustering of different responses into key research themes gathered from the questionnaires emailed to the respondents. All the common themes were then used to formulate structured questionnaires that guided the respondents in providing structured responses guided by different options provided.

A total sample of 20 company representatives were selected and interviewed for the purpose of this study.

The Broad Based Empowerment scorecard has been used as business risk measurement tool to promote the sustainability of BEE deals. The South African government also introduced the Broad Base Black Economic Framework which includes three core components i.e direct ownership, human resources development and indirect empowerment. “The key focus of the direct empowerment component is its economic impact on the equity stakeholders, executives and other owners and managers of economic resources. The beneficiaries assume direct economic risk for their involvement and expect returns that are commensurate with that risk” (DTI, 2004a:13)

The main objective of introducing the scorecard method was to assist stakeholders in empowerment especially the financiers to identify as well as eliminate unsustainable economic empowerment structures. Its purpose was also to ensure that the allocated benefits would only be awarded to economic empowerment entities that were truly committed to the economic empowerment process, and furthermore that the economic empowement entities receiving the benefits would also contribute back to the process.Ultimately the mechanism of measuring and monitoring the economic empowerment process would be efficient.

4.1 Understanding and knowledge of BEE

In general, the findings of this research revealed that there is a fair understanding and knowledge of what BEE is all about. The most common theme that came from the three main sectors or institutions' representatives interviewed was that BEE is an initiative intended for providing all South Africans with equal opportunities towards economic and political participation.

The differences were, however, on the specifics of its applications. For example, the insurance companies, banks and financial institutions' representatives defined and understood BEE as an increasing economic activity, participation and prosperity of previously disadvantaged people and communities within South African borders. The government regulatory bodies defined and understood BEE as a mechanism initiated by the government to redress past economic and political imbalances and intending to achieve country economic potential for all in the coutry.

The private sector on the other hand, without differing much from the former group (insurance companies, banks and financial institutions') of respondents expanded their definition and understanding of BEE as a structured method of allowing broad participation of previously disadvantages groupings in the economy; a policy of the transferring country's economy and resources; ensuring management and participation of black enterprises in economic mainstreams; and a mechanism that is working for the few who are politically connected.

4.2 Factor for choosing or funding a partner

When asked to provide important factors within their institutions considered in choosing or funding an empowerment partner, the following highlighted in order of importance:

- Participant must not only be the investor but be involved in the day—to—day running of the business and must also have passion for business.

- Contribution or meaningful participation of the BEE Company. This was one of the major requirements on which financiers insisted after 1998 (Business Map, 2000).

The motivation from the company that shows that the BEE Company is also taking a portion of financial risk should the transaction fail. This was highlighted as separate from and in addition to the opportunity cost.

The skills and experience appropriate to the project and prove that on-job knowledge, skills and experience transfer is being implemented within the project implemented for the purpose of contributing to the sustainability of the deal / project.

Track record, industry experience and specific features of deal. This factor was mainly to make sue that funding was allocated to BEE transactions without sufficient business experience and not only because of the existence of the BEE Company. In an interview with one of the respondents, it was emphasised that “experience in the business by the individuals concerned was very important in determining whether or not they would fund a BEE transaction, and most instances they would also insist that the BEE company initially only acquire a small stake, and as they gained more experience in the business, they could increase their shareholding”.

The integrity or willingness of the company to empower others involved with further investment capabilities. This meant that BEE as social transformation in the economy needed to be achieved within the constraints of maintaining the integrity of the market as well as the environment attractive to foreign investment.

The existence of a good corporate governance principles and practices within the BEE companies. This was mainly to reduce the risk of perceived failure of BEE which had a poor corporate governance practice.

The risk management capacity: The financiers also insisted on risk sharing based on more commercially sound terms. The introduction of a BEE shareholding and a sense of realism were mainly to balance factors in managing risks. This factor was also considered for the company’s financial standing and its bankability.

4.3 Initiation of the empowerment relationship

When asked who would normally initiate the empowerment relationship in the property deal, the majority of the respondents indicated the government was the main initiator, followed by the empowerment partner and then the holding company. Only two of the respondents highlighted that they did not know who the deal's main initiator was. Although the number of interviewed individuals was not sufficient to draw statistical differences, Figure 4.1 represents the spread of the responses to this issue.

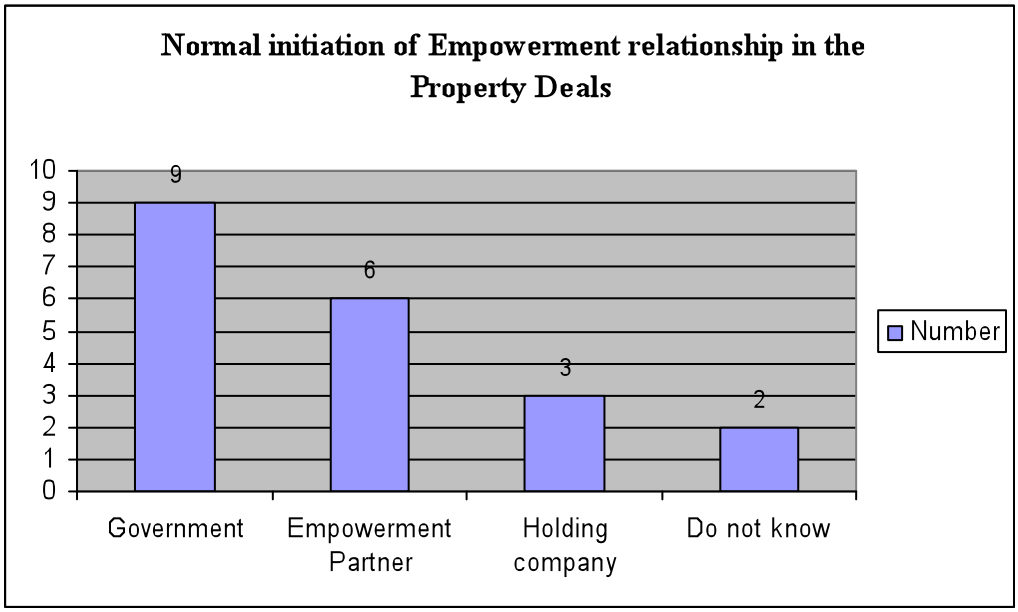


Figure 4.1: Initiation of the empowerment relationship in the property deals

4.4 Expectations from empowerment partnership

After the first phase of data collection and the clustering of the themes from different respondents, the following issues were provided as key expectations of the empowerment partnerships for the companies involved in property deals:

- Financial rewards;
- Improved returns;
- Access to more markets;
- Improved scorecard and charter points;
- Skills transfer, improve quality status of the company products;
- Compliance and transformation of the company;
- Added value to the company; and
- Delivery of results and sustainability

Although respondents indicated an understanding of what comes from deals' expectations and the fact that deals are very important for the prosperity of the partnerships, it was clear that the success of these deals was reliant on risk management. Respondents highlighted that empowering companies always chose partners that they believed would add the required business values and the management assessment of what was driving the environment.

4.5 The use of external agencies to determine the partner's potential

In the first phase of data collection, respondents were asked whether they use external agencies to determine an empowerment partner's potential and the majority confirmed to have used external agencies to ensure that the empowerment partner is really full of the potential the company is looking for. The agencies' roles were to:

- Contact financial institutions and banks which had a wide database for companies that needed to be empowered;
- Check the companies' financial track records to determine the empowerment partner;
- Check the accreditation of a company for the purposes of the charter guidelines;
- Conduct audits to ensure correctness of what was stated on the paper; and
- Prevent tokenism.

There were, however, some respondents that did not necessarily used agencies to determine the potential of an empowerment deal. The main reasons provided for this was that they did not have much faith in the existing external agencies and strongly believed in doing business with strangers.

4.6 The company's sustainability vision

Institutions' representatives were asked to state their institution's sustainability vision after the implementation of the empowerment deal. They were requested to give the three main ones (which led therefore, to 60 responses) and the list below provided findings in order of importance or the highest vision statement mentioned. The number next to the responses indicates the number of times respondents mentioned the issues.

a. Skills transfer on the operations of business and finance management (20)
b. Enlarge investment (12)
c. Access to the larger markets (08)
d. Capital availability (02)
e. Increase trade (02)
f. Corporate social investment (08)
g. Comply with good practice requirements (07)

Figure 4.2 below presents the split of response in a form of percentages for key sustainability vision needed for implementing the empowerment deal.

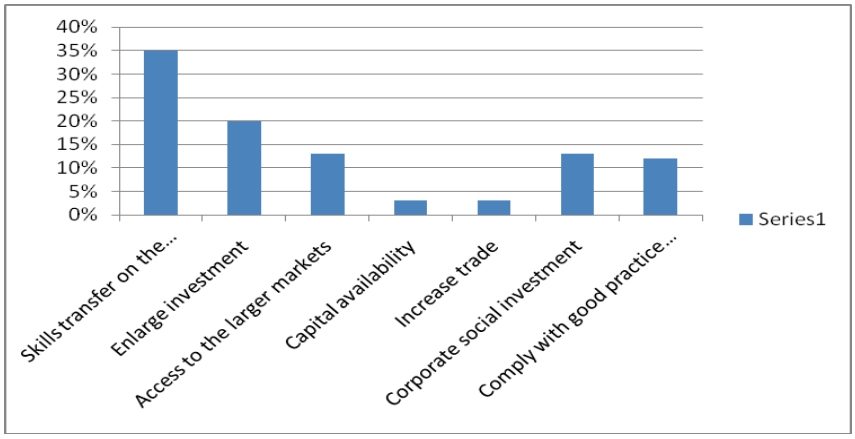


Figure 4.2: Sustainability vision for implementation of the empowerment deal

4.7 The duration for finalising an empowerment deal with less risk

When the respondents were asked to provide the duration needed for finalising an empowerment deal which had less risk, the responses varied from six months to just less than a year. There were also respondents that indicated that it can also take a longer time to allow the partners to ascertain each other. In general, the majority of respondents indicated that it depends on the value of the deal and could take up to six months to finalise. The list and the Figure 4.3 below present the overall findings to this question and they are presented in order of importance, with the first indicating the response with highest number of responses and the last with the least responses.

a. Depending on the value of the deal could be six months (12)
b. Shortest time (1 month) (03)
c. Less than a year (04)
d. Longer term allows the partners to ascertain each other (01)

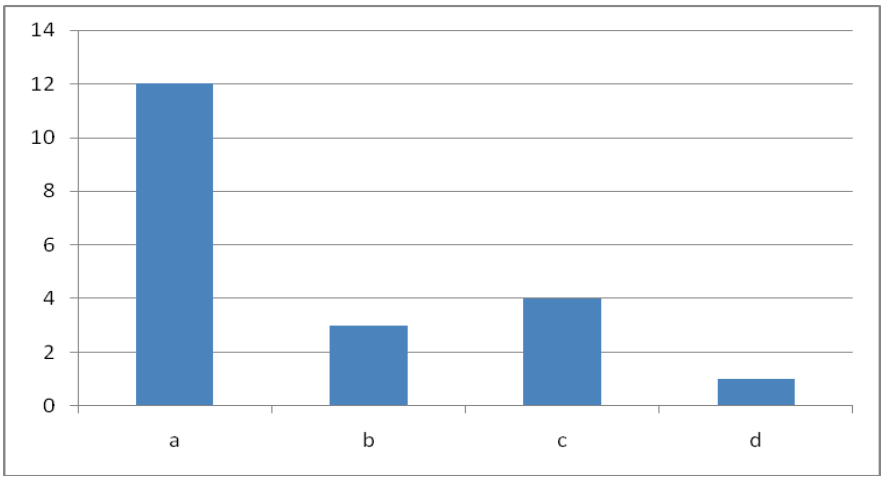


Figure 4.3: Duration for finalising an empowerment deal with less risk

4.8 Definition of a successful empowerment deal and reasons of its failure

4.8.1 Successful deals

The respondents were asked to describe a successful empowerment deal and most respondents described it as follows:

- The one with full participation of partners, who can also measure their contribution through performance;
- The honest deals where financial rewards are split equally;
- The one with transfer of management skills, the one where BEE suppliers are utilised;
- The one where there is corporate social responsibility;
- The one which achieves prescribed goals;
- The one with potential to deliver scope of work;
- The one with right financing model and equitable management model between parties;
- The one that is inclusive of the vision of empowerment;
- The one where there is implementation of transformation programmes; and
- The one with integrity of the parties.

A further finding, noted by the respondents, but not raised adequately in the literature review argues that BEE participants simply want to be wealthy and that the broad based principles of nation building and redistribution of wealth are often ignored.The need to be wealthy is usually a motive which can determine the conduct of a BEE participant and impact on the success of the transaction. This view was supported by the respondents.

Most respondents agreed that Broad –based empowerment schemes were ideal in concluding successful and sustainable transactions as they were not only to the black population but more acceptable to the white companies as well. These deals because of their nature of inclusivity they were more acceptable because they simultaneously reduce the level of resentment and increase the chances of success.

It was noted as a critical point that any BEE finance structure should be able to allow participants to make adequate returns, maintain a steady cash flow to ensure sustainability .The respondents highlighted that these finance structures could either lead to success and failure of transactions.In this instance the risk would be the lack of control, and skill to operate the new entity with the ability to generate expected returns.

4.8.2 Causes of failures of a deal

When asked to describe causes of failure to empowerment deals, the majority of respondents indicated the following reasons:

- The motive of companies that are not interested in empowerment deals but only in meeting the scorecard and being able to tender for government tenders.
- Fronting i.e using the small businesses for compliance purpose, without good corporate citizenship, promotion of uniformity and consistency in the application of principles contained in the charter;
- Participants are short changed, where debt is higher or immense in proportion to the anticipated profit.
- Non-congruency exists between the parties in the empowerment deals where financial rewards and investment horizons/periods are concerned.
- When the deal is done for wrong reasons; for example to score points on scorecard or to win tenders etc, while there is not enough focus on partners' contributions to the overall success and reward of those successful contributions.

More specific critical factors to consider as precautions for either success or failure of the BEE deals also included the following (DTI, 2004a:6)

- Lack of effective management
- Lack of financial management
- Lack of entrepreneurial management
- Lack of proper training
- Lack of resources
- Lack of technical, contractual and managerial skills
- Late payment for work done which are common with government contracts
- Inability to get credit from suppliers
- Fronting from established contractors
- Inability for a contractor to market him/herself among the industry role players

4.9 Availability of a document detailing the strategy for choosing the empowerment partner

All the respondents were also asked to confirm with a "yes", "no" or "unsure" responses on whether their company has a document detailing the strategy for choosing the empowerment partner. The majority (12) of the respondents indicated that they do. Only a few (six) indicated

that they did not have and two were unsure of the availability of such a document within their company.

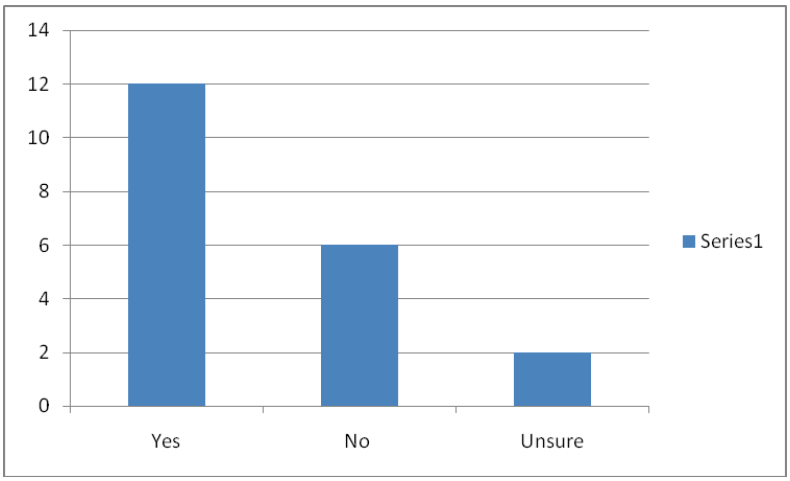


Figure 4.4: The strategy for choosing the empowerment partner

4.10 The bearer of the financial risk in the partnership

Respondents were further asked to indicate who would normally bear the huge financial risks in the partnership should it fail and the responses differed. The responses ranged from the empowering company (two respondents); the party lacking integrity in the deal, all parties concerned, to the financier.

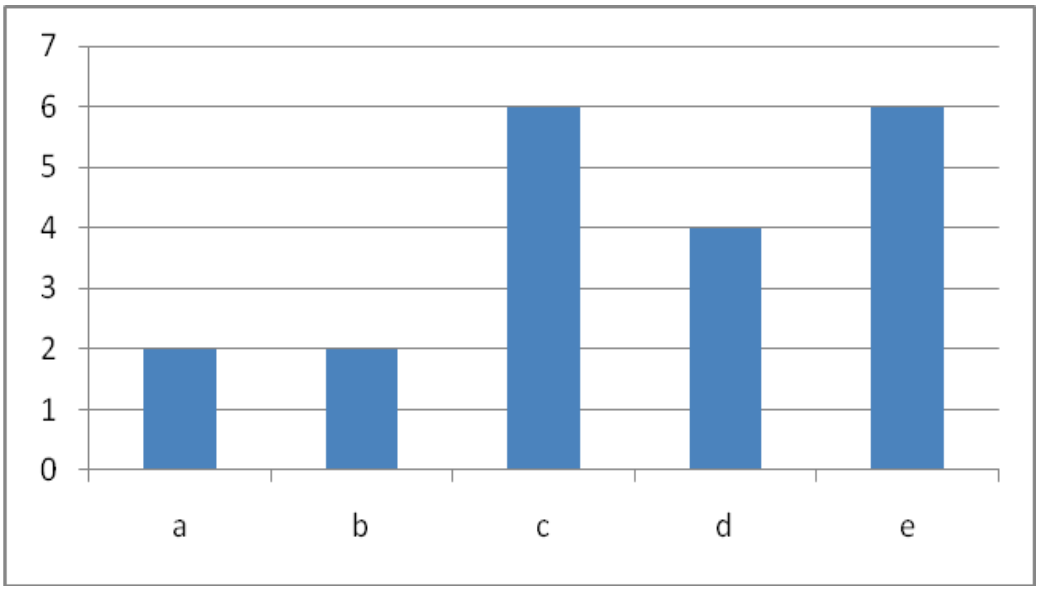


Figure 5: Extent of risk when the empowerment deal fails

CHAPTER 5: SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Summary and conclusions

South Africa has come a long way since its first democratic elections in 1994. Many milestones have been reached and many hurdles still need to be overcome. BEE was introduced as one of the Government's economic milestones for addressing the past imbalances. However, it must be noted that the BEE cannot and will not be achieved overnight. More and more companies and individuals are buying into this concept and past inequalities are being addressed.

The purpose of this research was to understand the management of risks associated with financing sustainable empowerment deals by understanding BEE partnerships and appropriate precautionary measures to be employed in measuring risks in such partnerships during the process of making financing decision. The evidence reveals that there is a fair understanding and knowledge of BEE. More respondents emphasised the importance of the experience in the business and operational by the participants in determining whether the transaction would be sustainable.

A combination of different methodologies was utilised in gathering and analysing the research data on BEE—finalize related issues among the insurance industries, banks, trading houses, property valuation market, as well as property investment companies.

The report findings reflects analysed data from both secondary and primary sources (interview questionnaires) on the general understanding of BEE, measures used and the precautions to be considered in partnerships (investigated as success and failures of the deals), risk management, and the sustainability of BEE deals. Specifically, a Delphi technique method was utilised for the different rounds of questionnaires developed and interviews conducted and the analysis of these. Experts from different sectors assisted in facilitating the formation of group judgments and in continuously refining the views gathered on different topics.

Therefore, this research report presented key findings on all the research objectives highlighted in the previous paragraphs. In general, almost all the key players had an understanding of what BBE is all about; with the most dominant understanding of BEE as an initiative from Government intended to provide previously disadvantaged people with equal opportunity to participate in economic activities. However, the private sector respondents expanded this understanding by adding that BEE is a mechanism that ensures structured management and

participation of black enterprises in economic mainstreams and is seem to be only being working for the few who are politically connected.

Among other factors used for choosing or funding a BEE partner or entity in a deal, participant's involvement in running of the business and having a passion for business were mentioned as key contributors to meaningfully partnerships. Other factors included: taking a portion of financial risk; possession of appropriate skills, experience and a good track record for the project; the willingness to transfer skills and empower others for sustainability of the project. The existence of good corporate governance principles and practices also played a role in selecting the BEE partnership.

With regard to initiating the BEE deal partners, government, empowerment partner and/or the holding companies were found to be the initiator. Once initiated, key major expectations of the empowerment partnerships ranged from the financial rewards, improved returns, access to more markets, improved scorecard and charter points, skills transfer, improve quality status of the company products, compliance and transformation of the company, to adding value, delivering good results and adding sustainability to the deal.

Although all these were the requirements and expectations needed for the deals, it was clear that the successes of the deals were also reliant on the risk management practices shared among partners—on which the financiers were also insisting. The implications from these findings are that, it is important for the empowered partners to be perceived to produce the most value for the least financial, strategic and operational risks. The empowering companies that would take shortcuts are therefore, doomed to failure.

Furthermore, the majority of the partnerships decisions were determined and guided by the external agencies used for spotting potential of a BEE deal. Their specific roles included investigations and assurance (confirmation) about the intended partner, the evaluation of their financial track records and accreditation of a company as indicated in the charter guidelines. Where necessary audits are conducted to ensure correctness of what was stated on the paper and to prevent tokenism. The reasons provided for those who did not use agencies were that they did not have much faith in the existing external agencies and believed strongly in doing business with strangers.

The most highlighted visions for the sustainability of implementing partnership were found to be skills transfer on the operations of the business and financial management, enlargement of investment and access to the larger markets, corporate social investment, and compliance to

good practice requirements. The duration for finalising an empowerment deal with less risks were seen to depend on the value of the deal and could be between six months to less than a year, with some taking even only a month.

While full time participation of the partner in the deal was emphasised as one of the expectations in the partnership, the same issue was highlighted as one of the success factors. Other success factors included: performance measurements and contributions to overall deal performance and deliverables or achievement of prescribed goals; an honest deal where financial rewards are split equally; transfer of management skills and the utilisation of BEE suppliers; one where there is corporate social responsibility; and one with the potential to deliver the scope of work, with the right financial model, equitable management model between parties, and is implementation of transformation programmes.

The main causes of BEE partnership failure occurs when the deal is done for the wrong reasons and the one partner is only interested on meeting the scorecard and tender submitting requirements. In August 2005, Business Unity South Africa (BUSA) acknowledged that BEE was plagued by fronting and window dressing, and that it intended to work with its members to stamp these practices out. ANC MP Ben Turok told a media briefing in parliament (June 2006) that fronting was of great concern to business and government. Another cause was seen to be a lack of integrity and greediness in using the small businesses for compliances purposes, without good corporate citizenship or the promotion of uniformity and consistency in the application of principles contained in the charter. Failure was also seen as a result of: participants being short change where debt is higher or immense in proportion than the anticipated profit. None—congruency there is non-congruency between the parties in the empowerment deals where financial rewards and investment horizons / periods are concerned was another reason for failure given. This might be due to different expectations with regard to key issues around the deal when markets/companies fail to perform— i.e. initial funding terms and heavy reliance on strong expected business / share growth driven by the deal / empowerment partner.

Almost all the issues revealed from this study were still causing challenges to implementing BEE in the 1990s. For example, a scarcity of black capital resources (Levin, 1994:3; Nyati, 1993:85), a lack of adequate managerial and technical and administrative skills among some managers (Riley, 1993:62). Therefore, there is still a need to address the challenges experienced in the 21st century.

Other precautions to take note of in BEE partnerships include: effective management in finances and entrepreneurial skills; proper training, sufficient resources, technical and

contractual managerial skills; follow-up on payments on the work done; the ability to secure credit from suppliers; and avoidance in the use of fronting from established contractors.

Although it is encouraged by the code of good practice, there are still some companies that do not have a document detailing the strategy for choosing the empowerment partner. Some interviews confirmed that companies that have guidelines for choosing an empowerment partner and the reasons for partnership were found to be more successful than those which did not. The guidelines need to be used as a route that should be religiously followed by the company to make sure it safely reaches the arrival point — targeted goals and can assist as one of the risk—mitigation processes for the deals. Risk taking is encouraged by virtue of having risk management techniques in place.

Those companies which did not have documented strategy or procedure for partnership are deviating from the straight way leading to the success of the empowerment deal. In most instances, they are exposed to becoming the victims of a none—risk management process and this will lead them to an inevitable failure. While they take “detours with the wish to reaching the summit” as stated by one of the respondent, ‘this brings them back to square one”.

In terms of bearing financial risks within the partnership, this research revealed that the risks are either carried by the empowering company or both parties involved. In some instances it is the party that is most likely lacking integrity in the deal and not practising good corporate citizenship or the financier that carries the financial risks.

5.2 Conclusions and recommendations

This research report highlighted key issues in the form of secondary and primary data collected and analysed on: issues around BEE in commercial and industrial deals, factors for sustainability and success and failures for the partnerships; and risk management issues.
This research focused on the appropriateness of risk management as the measurement tool of the correct establishment of sustainable property deals. There is a conviction that this complementary performance monitoring approach will assist in addressing the changing environment of the property industry in order to improve its competitiveness. This leads to the emergence of the new performance mechanisms, which have to be expeditiously implemented.

Risk management needs to be utilised as a persuasive tool that will ensure sustainability of BEE deals, Stakeholder management of either individuals or groups having interest or being affected by the property deal activity also needs to be considered. This would include potential

empowered companies, empowering companies, public policy makers, internal stakeholders and market players. This is in view of the changes in the institutional frameworks for gaining more responsibility and financial autonomy in a safer and sustainable environment.

The goals of this initiative are a better corporate and independent management structure and more responsibility. The effect is competitive co-operation, growing mutual understanding and a constructive climate.

The successful implementation of empowerment deals is relying more on the alignment of the objectives of empowerment and the broader commercial and business legal environment.

The past inequalities are still visible in South Africa's economic landscape, but more and more companies are realising the benefits of BBBEE and are more willing to comply with most requirements set by Government, as long as these requirements are reasonable. The key issue will then be to apply a well structured approach in implementing and following the guidelines provided. Specifically:

- There is a need to conduct audits that will assist in revealing more specific challenges and plans or strategies in address them. Such audits will also encourage more participation and interest of PDIs, since they will know what to expect and how to deal with the findings.
- BEE tokenism is still an issue, even after the implementation of the Code of Good Practices and the charter councils. For this to be addressed, it needs further stringent strategies that will completely eliminate BEE tokenism.
- Full participation of BEE partnerships needs to be encouraged, with equal sharing of performance goals, rewards and risks among partners. One of the key deliverables on this is to make sure that all parties involved hold appropriate skills; knowledge and experience needed and hold good track records. This will also clear the misperception that the international fraternity holds around the BEE; i.e. the IMF perception that BEE deals are mainly to enrich the chosen few.
- Structures and support need to be established for those interested in mentoring and coaching others around key success factors needed for sustainability, especially on the risk management issues and management and financial issues. Skills development programmes addressing the operational needs of the business are critical in ensuring all the players are on the same par with business experts. Job shadowing can be one of the strategies adopted.

- Lusengo (1993) suggests that the structuring of the social responsibility measures and the involvement of communities need to be considered as important factors while these contribute to sustainability of the deals it depletes enterprise control by new BEE participants. It is therefore very important to structure broad based BEE such that ownership of assets and control of enterprises always take a centre stage.

In summary, more should be done to provide education to other BEE players and all stakeholders to ensure that parties to any BEE transaction embrace the basic fundamentals of a well structured deal that operates under the code of good practice and all relevant guidelines. Risk management is cardinal in empowerment property deals and it should be encouraged as a persuasive tool that will ensure that BEE deals are sustainable. It is also important that the sharing of both the financial and managerial risks are well understood by all parties involved. BEE implementation will continue to be developed further and new ideas will continue to be debated amongst industry participants until the much desired levels of economic and social transformation are achieved.

5.3 Suggested further research

The framework for business operational management sets the stage for further developing the risk analysis model. As no precedents have been found no comparison can be drawn. There seems to be a need for a valuation model that will integrate more meaningfully the risk profiles of the various operational decision makers in a new venture.

Further research and tests in financing decision making practice are required to be carried out before conclusions on its applicability in the field can be made.

The following questions are therefore suggested for further research, since this research was based only on limited information and the qualitative nature of it makes it impossible to generalise the results:

- Can the workplace skills plans and employment equity reports be used as the only tools to measure the success of the BEE deals in Commercial and Industrial property sector?
- How best can they be used to achieve the South African government's Broad Based Empowerment objectives?

- How could be the functions of empowerment monitoring bodies i.e. Charter Council ,Empowerdex and the DTI be streamlined with the funding or financing institutions processes in measuring the Risk associated with the financing of the Commercial and Industrial properties deals?

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APPENDIX 1: DIRECTOR/MANAGER – LETTER

The Graduate School of **Built Environment**

University of the Witwatersrand

Dear Director/Manager

Research on: IS RISK MANAGEMENT; A DETERMINANT OF FINANCING SUSTAINABLE EMPOWERMENT DEALS OF COMMERCIAL & INDUSTRIAL PROPERTIES?

Your company or institution has been chosen to participate in this research. I am a student at Wits School of Built Environment completing my Masters of Science on Property Development Degree. As part of my studies, I am conducting research on the above mentioned topic. The information gathered will be used as a guideline to set up a reference guide for various stakeholders involved in property empowerment deals. Your participation will be of immense value.

What is required of you?
Empowerment experts in your company or institution, who have in-depth knowledge with regard to property empowerment deals, are required to take part in the research. Each expert or respondent will receive two rounds of questionnaires that he/she needs to complete and fax or electronically mail back to the researcher. Each questionnaire will take approximately 10 to 15 minutes to complete. It would be very much appreciated if you could provide me with the experts' e-mail addresses before 15 September 2010. So the questionnaires can be electronically mailed to them.

Please note the following:

- There is no right or wrong answer; the respondent has to honestly provide what he / she knows.
- The questionnaire is anonymous and the information will be treated as confidential, with no reference to company names in the research report.
- Respondents will either fax the completed questionnaires to (011) 431 03 70 or reply on the electronic mail sent to them.

It would be appreciated if you can email or fax the list of recommended experts to participate in this research to: milzet2001@gmail.com or fax to (011) 431 03 70.

Please do not hesitate to contact me if you require more information in this regard.

Ms Nomathemba Kubheka
MB Student – Wits Built Environment School
Mobile: 083 5856408

APPENDIX 2: QUESTIONNAIRE ROUND 1

THE GRADUATE SCHOOL OF BUILT ENVIRONMENT
University of the Witwatersrand

IS RISK MANAGEMENT A DETERMINANT OF FINANCING SUSTAINABLE EMPOWERMENT DEALS OF COMMERCIAL & INDUSTRIAL PROPERTIES?

1. How would you define Black Economic Empowerment within the South African context?

   _____

   _____

   _____

   _____

2. Indicate some main factors which will be of importance to your company / institution when choosing or funding an Empowerment Partner or entity in a property deal.

   _____

   _____

   _____

3. Who normally initiates the empowerment relationship in the property deals you have been involved in?

   Select or highlight one option.

a. Holding Company
b. Government
c. Empowerment Partner
d. Other
e. Unknown

4. What kind of results will the company/institution involved in the property deal be expecting from the empowerment partnership?

   _____

   _____

   _____

5. Have you as a company / funding institution made use of external agencies to determine an empowerment partner's potential? If so, why.

_____

_____

_____

6. What will the company's/institution's sustainability vision be, after the implementation of the empowerment deal?

_____

_____

7. What is the duration for finalising an empowerment deal with less risk?

_____

_____

_____

8. How do you describe a successful empowerment deal?

_____

_____

_____

_____

9. Why do you think empowerment deals fail?

_____

_____

_____

10. Does your company have a document detailing the strategy for choosing the EP? For each of the four items below please indicate if the **strategy document** includes the following by marking YES, NO or UNSURE.

Criteria	YES	NO	UNSURE
Framework or guidelines for Choosing an EP			
Reasons for Partnership			

11. Who will normally bear the huge financial risk in the partnership if should it fail?

_____

_____

_____

12. What are the critical failure and /or success factors for BEE deals?

13. Are BEE deals financing commercial and industrial properties sustainable in South Africa?

14. What has been the strategy used by the financiers prior and post the application of the BBBEE code of good practice?

APPENDIX 3: QUESTIONNAIRE ROUND 2

THE GRADUATE SCHOOL OF BUILT ENVIRONMENT
University of the Witwatersrand

IS RISK MANAGEMENT; A DETERMINANT OF FINANCING SUSTAINABLE EMPOWERMENT DEALS OF COMMERCIAL & INDUSTRIAL PROPERTIES?

1. Black Economic Empowerment has to do with:

- Offering for participation in the economy through shareholding in companies
- Policy of transferring country's economy to the previously disadvantaged
- Mechanism intended by the government to redress past political and economic imbalances to achieve country economic potential
- Increasing economic activity, participation and prosperity of the previously disadvantaged people

2. Factors which are important in your company / institution when choosing or funding an Empowerment Partner

- Transfer of skill
- Black participation in the management structure
- Level of black group's beneficiation
- Black percentage shareholding
- Credibility and financial standing
- Track record, industry experience and specific features of deal

3. What are the expected results by the company/institution involved in the property deal from the empowerment partnership?

- Performance as per agreement

- Financial rewards
- Improved returns
- Access to more markets
- Compliance and transformation of the company
- Improved scorecard and charter points

4. Using external agencies to determine an Empowerment Partner's potential helps in

- Yes, to ensure that the Empowerment Partner is the one the company is looking for
- Yes, for conformity of what is on paper and the real potential of the empowerment partner
- Yes, for accreditation purposes per charter
- No, we do not have confidence in external agencies

5. The company's/institution's sustainability vision, after the implementation of the empowerment deal

- Achieve empowerment expectations
- Enlarge investment
- Access to the larger markets
- Increase trade
- Comply with good practice requirement

6. Acceptable duration for finalising an empowerment deal with less risk

- No idea
- Less than a year
- Longer term allows the partners to ascertain each other
- Depends on the value of the deal

7. Description of a successful empowerment deal

- One which brings real rewards to shareholders through skill transfer and financial returns
- One with integrity of parties
- One where there implementation of transformation programmes
- One which has potential to deliver scope of work
- One where BEE suppliers are utilised
- Hones deal where financial rewards are split equitably

8. Main reasons for empowerment deal failure

- Non negotiation in good faith
- Divergent expectation and vision
- Irreconcilable personalities
- Fraud
- Lack of integrity
- Greed
- When debt is immense in proportion to profits anticipation

9. Document detailing the strategy for choosing the EP

- Framework or guidelines for choosing an empowerment partner
- Reasons for partnership

10. Bearer of the huge financial risk in the partnership when failure happens

- Depending on the structure
- Both parties
- Empowering company
- Empowered partner will suffer less as he/she is nominal represented

11. Critical failure and /or success factors for BEE deals

Lack of effective management

Lack of financial management

Lack of entrepreneurial management

Lack of proper training

Lack of resources

Lack of technical, contractual and managerial skills

Late payment for work done which are common with government contracts

Inability to get credit from suppliers

Fronting from established contractors

Inability for a contractor to market him/herself among the industry role players

12. Are BEE deals financing commercial and industrial properties sustainable in South Africa?

13. What are the management strategies employed by financiers in order to minimise risk while financing BEE commercial and industrial deals?

14. What has been the strategy used by the financiers prior and post the application of the BBBEE code of good practice?