



## Concept Document for:



*"Black companies only get about three percent of the R515 billion that JSE-listed companies spend buying goods and services from other firms every year"*

— Vuyo Jack, EmpowerDex, 2004

The Johannesburg Empowerment Exchange (JEX) is an initiative about merging black economic empowerment and free-market thinking. It would organize itself like the brazenly capitalist Johannesburg Stock Exchange, but with a long-term aim of helping companies increase their purchases from black owned suppliers in a cost-effective way.

Companies that beat 'procurement equity' targets could sell credits on this exchange, recouping some costs to come into compliance with governmental BEE transformation objectives or mandates. Companies not meeting the mandates must buy the credits, giving them an incentive to improve. By being a member of the exchange, violators agree to any punishment that other members of the exchange may impose upon them.

The exchange will help price discovery by disseminating market information. According to several policy implementation specialists in the area of BEE, the current estimates of the cost of intensifying procurement equity are too high; we believe that the competitive forces of an exchange should help lower them, and mitigate concerns that support for BEE could distort markets.

The exchange will also help standardize the commodity because procurement equity may be increased and BEE supported in many different forms, ranging from direct purchases from black owned companies to engaging in joint ventures with black empowered companies. The exchange will facilitate the creation of the market infrastructure and institutions for the registration, clearing and settlement of contracts.

Data from the marketplace will help government officials determine what are reasonable levels for preferential procurement. The initiative is designed to complement charter processes.

AniCap Venture Partner's work on the concept over the last seven years stems from its passion that markets can lend themselves to solving social transformation problems.

The self-regulatory JEX is based on a set of principles, which will be agreed to by procuring companies during a pilot exercise in South Africa. During the initial stages of the pilot, a



## Concept Document for Johannesburg Empowerment Exchange

feasibility study will be conducted by University of the Western Cape, University of Johannesburg, and the University of Stellenbosch evaluating the viability of the exchange.

**“The Johannesburg Empowerment Exchange is one of the most innovative approaches to BEE that we’ve ever seen”**

—Ben Smit, Bureau of Economic Research, RSA, 2004

Already, JEX integrates substantial intellectual capital developed elsewhere. It’s design draws heavily on the over \$1 billion that was spent on Kyoto Protocol, Chicago Climate Exchange, and the UK Emissions Trading Scheme; furthermore, it’s obligate-and-offset model has been inspired by dti’s National Industrial Participation Programme.

Building on this, AniCap has invested considerable resources to develop stakeholder interest from the black business community, the financial sector (including the JSE), and various charter task groups. The initiative is well on its way toward being a black-owned and operated initiative.

### **Next Steps**

To take this initiative further, involvement from government is crucial now.

To unlock the non-government investment required to conduct the aforementioned feasibility study, bilateral and multilateral funding organisations like the IFC have requested a letter from Government, formalising their expression of interest to see the results of this study. And to commence with the pilot, we prefer to focus on a sector that adds the greatest value to government in demonstrating the potential of exciting new BEE initiatives like this one. All private sector representatives to which we have shown this initiative have agreed that they’d prefer to see Government’s (even conditional) support for this initiative before they commit serious resources to participate in a pilot exercise.

The aim of both the feasibility study and pilot exercise is to provide Government with information that it will find useful to best evaluate the policy and practical merits of the idea; it will also provide our consortium with the opportunity to design a more effective exchange solution that is in greater alignment with Government BEE policy directions and regulations.

We hope you’ll agree that this initiative could make a powerful contribution to South Africa’s economic transformation.

I wish to thank you for considering JEX, an innovative new approach to SME development and South Africa’s black economic empowerment.

Best regards,

**David Monkman**  
Managing Director  
AniCap Venture Partners



Article about Johannesburg Empowerment Exchange written in Maverick Magazine in 2006:

# capitalist musings of the socialist mind

**Carbon credits turn pollution into a tradable instrument, in the belief that an efficient market benefits everybody. So what happens if you apply the same logic to black empowerment? Well, your idea falls flat, for a start. BY PHILLIP DE WET**

SOME INDUSTRIES AND COMPANIES ARE better at doing empowerment equity deals than other industries and companies. You could say they are more efficient at it. True empowerment requires the creation of new black businesses; but, by definition, those involved don't have any money.

Now consider what happens if you turn empowerment into a tradable commodity subject to the usual market forces. Companies that really suck at the empowerment thing for whatever reason could buy their way out of trouble. If the whole empowerment thing is going well they could do so cheaply; if transformation is slow the price of the commodity rises and everybody has more incentive to try harder. And those black startups create an immediate asset to leverage.

It may sound like an idea dreamt up by true, hardcore capitalists who wanted nothing more than to exploit a socio-political intervention for profit. Actually, it was dreamt up by a bunch of semi-socialist liberals who saw it as a tool for good. Proof: they wanted to give away all their profits to further empowerment.

They failed, of course, as is evidenced by the lack of a tradable empowerment instrument. But the idea makes for a fascinating thought experiment. And if the Kyoto Protocol is a great success and the notion of offset credits becomes popular, it may yet be revived. Staid old white companies and under-funded black startups certainly wouldn't complain.

The idea came about thanks to a need for funding, says Barry Corbett, a South African

political science graduate who developed business ambitions and became one of the original team that tried to bring the concept to market as Anicap Venture Partners.

"We were initially looking at helping new empowered enterprises get the training they need to start training. But how do you pay for something like that, when the trainees don't have money? The answer is to 'monetise' their empowerment status, the one asset they all have."

David Monkman, a second member of the trio and the economist who Corbett credits as the father of the idea, was familiar with the early ideas that grew into the Kyoto Protocol. The same logic applied, he argued.

A target of, say, 30 percent black equity participation provides no incentive to set up a company or do a deal to achieve 70 percent or 100 percent empowerment. Set a floor, monetise any excess achieved, and good things can happen.

There is also some beguiling efficiency logic behind such a move. Black suppliers who need a hand up will logically be less efficient than the white equivalent, otherwise they wouldn't need a hand up in the first place. Strip the issue down to the money and it makes sense to stick with the most efficient supplier, no? Then if that supplier is white, load it with empowerment obligations. If it can meet the targets itself, then fine and well. If it can't crack the problem then give it the opportunity to buy its way out of trouble. That way you can encourage empowerment while maintaining efficiency.

Take it a step further and allow a supplier to pass its obligations down the supply chain, for a price. Eventually the obligations can all end up sitting at the lowest level – the nuts and bolts people who add the least value. In many instances this is the easiest point of entry for new black businesses, but it is often avoided because margins can be thin. But add more money and, hey presto, instant bottom-up empowerment.

Treating an empowerment credit like any other security has other implications. Futures markets and greater liquidity, for instance; the ability to hedge empowerment risk, which would damp down volatility, and economic certainty, which is almost always good for growth.

A complex market would open loopholes, and for the system to work it would need serious auditing that could be universally trusted. But that could have been achieved, Corbett still believes.

The originators shopped the idea around for a bit, raised some support for it and then watched it slowly peter out, as is so often the case with ideas.

But Corbett still likes to play "what-if" games with the basic concept. What if it was applied to environmentally friendly mining? Or company-level recycling? Or, if water becomes a scarce enough commodity, to community-level water consumption?

Could work, he muses. In fact, probably would work, because at heart it is an utterly simple concept. "You are just using an incentive to get something done rather than a sanction." ■