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Creative destruction or just a reshuffle? Why business turnover in South Africa has not sparked growth

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Business churn is usually the sign of a healthy, growing economy. South Africa compares well globally in terms of firm turnover. The puzzle, though, is why these shifts have not been accompanied by more dynamic economic growth and job creation.

The entry and exit of businesses generally signify healthy competition and economic vitality.

In theory, new entrants introduce fresh ideas, products, and techniques that spur economic modernisation, diversification and sustainable employment creation.

This is the idea behind Joseph Schumpeter's concept of 'creative destruction', in which firms must continually reinvent themselves to remain profitable, often at the cost of jobs, products, and industries that become obsolete and disappear.

Lack of churn can cause economies to ossify and stagnate.

The World Bank's recent diagnostic report points to precisely this problem in South Africa. It states that too few new firms have been created and too many old firms have survived when they should have folded.

The strong assertion by the Bank is that "...many of South Africa's markets lack dynamism"¹ and that "creative destruction, the natural process of new firms entering the market and moribund ones exiting ... has been *largely absent*".²

¹ World Bank. (2024) 'Driving Inclusive Growth in South Africa: Overview'. Washington, DC: World Bank.

² World Bank. (2024) 'Driving Inclusive Growth: Priority 4 - Injecting Dynamism into the Private Sector'. Washington, DC: World Bank.

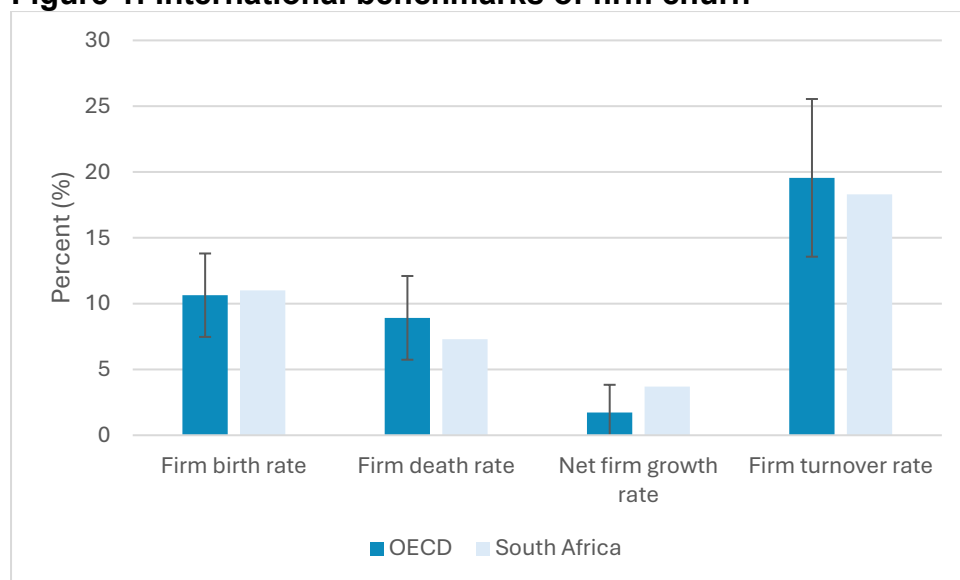
This view reflects the conventional wisdom that markets in SA are heavily concentrated with little change in ownership or industrial structure over time. Labour market rigidities, monopoly power, and overregulation have shielded incumbents from competition and produced inertia, thereby preventing more productive new entrants from reinvigorating the economy.

In fact, the evidence to support these views is thin and questionable. It may also be a mistake to assume that concentrated ownership necessarily means few new entrants and exits. Using a new and more comprehensive spatial tax panel database, we have monitored business and employment flows in much greater detail than hitherto.³

How does the evidence stack up concerning South Africa’s level of business and labour market churn?

Contrary to expectations, South Africa performs relatively well when measured by conventional metrics of business dynamism, such as rates of firm entry, exit, and firm turnover (see figure 1).

Figure 1: International benchmarks of firm churn



Source: OECD: *Structural and Demographic Business Statistics (SDBS)*; South Africa: authors’ own estimates from tax certificates available in the National Treasury: *Secure Data Facility*

Notes: The bars represent the standard deviation for the sample of 39 countries reported by the OECD

We estimate that more than 10% of firms were new entrants in any year with a reshuffling of 18% of firms over the period 2014/15 to 2019/20. This is similar to the OECD average, and calls into question the idea that business turnover is a major problem.

³ See: Visagie et al. (2025) *Creative destruction or simple reshuffling? Turnover among businesses and jobs in South Africa*. ERSA Working Paper 907.

Analysing openings and closures at the branch-level pushes these statistics even higher. We estimate that almost 33% of establishments experienced a change each year— either opening or closing a branch, or experiencing a firm birth or death.

Therefore, it seems wrong to characterise the internal workings of the South African economy as stagnant, dormant or lifeless.

A similar conclusion is reached when looking at job turnover in the labour market related to business changes. We find that almost a quarter of jobs were reshuffled between establishments in any year. Previous work by Kerr reports similar rates of job reallocation for South Africa, which is considered sizable when compared with other countries.⁴

The implication is that the South African labour market might not be characterised by as much inertia or rigidity as often perceived.

A big puzzle is why all these shifts and shake-ups in economic activity have not been accompanied by more substantial economic progress, increased productivity and stronger employment growth?

For instance, total jobs growth was only 1% per annum over the period 2013/14 to 2019/20, which is less than population growth. In other words, job creation from new births, branch openings and in-situ expansions were matched by job destruction from firm deaths, branch closures and in-situ contractions, so there was limited net growth.

Similarly, all these flows did not lead to any noticeable diversification into new tradable industries. Hence business churn did not support structural transformation, although the time horizon may be too short to see the sprouting of sizeable new shoots.

Similar concerns emerge when looking at the role of cities in firm formation.

Cities are particularly important incubators of entrepreneurship and new firms due to the wide range of suppliers and support services available, as well as their large, diverse customer base. The strength of these entrepreneurial ecosystems means that cities worldwide tend to house a disproportionate number of new and expanding firms.

Yet the metros did not emerge as strong incubators for new firm formation. In fact, jobs lost from firm deaths outnumbered jobs gained from firm births, characterising metros more as graveyards than nurseries.

So what is going wrong with South Africa's process of creative destruction?

⁴ Kerr, A. (2018). Job flows, worker flows and churning in South Africa. *South African Journal of Economics*, 86, pp.141–166; Kerr, A., Wittenberg, M. and Arrow, J. (2014). Job creation and destruction in South Africa. *South African Journal of Economics*, 82(1), pp.1–18.

There could be many underlying reasons why high levels of business entry and exit, and labour reallocation did not translate into better outcomes.

First, it may be necessary to distinguish between different types of firm entry and job creation. There is an important difference between business churn that leads to genuine 'creative destruction' as characterised by innovation, upgrading and economic renewal as opposed to a simple 'reshuffling and substitution' among undifferentiated competitors.

Firms should not be supported by economic policy simply because they are 'small' or 'new' but because of their potential to innovate, raise productivity and grow over the longer term.

Second, it may be that South Africa's relatively small, stagnant and geographically isolated domestic market is saturated and offers little room to grow. Of course, firms can try to export goods and services into new markets but this has proved difficult to achieve in practice.

The birth of so many new firms, especially in the context of mass unemployment, suggests that many factors of production could be underutilised and the economy is operating well below full capacity. If this is the case, the appropriate policy response may be to stimulate demand using instruments such as lower interest rates or increased public spending.

Beyond this, it is widely understood that there are deeper structural obstacles to economic growth, such as basic infrastructure deficiencies, inefficient logistics systems, unresponsive public services, cumbersome regulatory frameworks, and major governance shortcomings.

These economy-wide barriers to growth and investment tend to stifle the generative effects of both business reorganisation and labour turnover. They limit the potential of all firms – new and old, large and small, efficient and inefficient – to grow and prosper.

A final, more troubling possibility is the abuse of power by dominant firms. Large incumbents may use their financial resources and market influence to actively suppress the emergence and growth of new competitors. This can occur through legal yet socially undesirable mechanisms such as lobbying for favourable regulation or the manipulation of preferential procurement. Another possibility is the existence of anti-competitive and unlawful behaviours including predatory pricing and collusion despite the punitive authority and enforcement powers of the competition commission. These practices can entrench incumbents for the wrong reasons.

In summary, the challenge of business change in South Africa may be less about the numbers of business births and branch openings, than about the quality of new entrants, i.e. the level of investment they embody, the technology adopted, the novelty of their products and services, and the capabilities of their management and workforce. Equally important is the extent to which markets function competitively to

promote and reward disruptive and high-potential firms with opportunities for future growth.

This calls for a focus on fostering competition based on innovation and productivity rather than on ruthless cost-cutting, alongside efforts to lower barriers to entry and curb anti-competitive practices that entrench incumbents and stifle dynamism.

Future research should focus on how firm-level productivity is related to firm entry, exit, age, size, and employment growth. An important question is whether dominant firms maintain their market position due to superior products and services, or because of barriers that prevent new entrants from advancing. Policymakers need a deeper, dynamic perspective of business formation, competition and growth.

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