Review of small farmer finance and livelihoods in South Africa

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1. Introduction

This overview serves as a section of the background work for the Small Farmer Finance project. The project is based on the reality of the rural areas of South Africa. It recognizes that rural people mobilise income from a range of sources. In many instances farming plays an important role, but in terms of monetary contribution to the household income, not as important a role. It seeks to find adequate background material on which to base the next stage of the study.

In this background document we start with an overview of the microfinance market in South Africa. This provides an overview of the complete microfinance sector, including the finance of small farmers. Note that we concentrate on loans below R10000. However, we will also address larger loans (from R10000 to R100000) in a sub-section on small farmer finance. This overview is followed by a discussion and illustration of livelihood strategies in the rural areas of South Africa. This is then combined in a section on finance and livelihoods. Due to the importance of the impact of HIV/AIDS in South Africa we also include a relevant section followed by some concluding remarks.

2. Overview of the supply of financial services

2.1 Introduction

The demand for banking services by the lower income strata of the population is growing rapidly, due to a variety of factors. These include current low frequency of use of formal banking services by the poor and MSE[2] market; increased income of the lower income strata; income redistribution in favour of lower income people; urbanisation; rising consumer aspirations; the rapid growth of the informal business sector and, perhaps the most important incentive the last eight years, the relaxation of the Usury Act on loans below R6000 in 1992 and recently to loans below R10000. In reaction, there has been considerable growth in the micro-finance sector, and the biggest source of growth is from the micro-lending sector. The conventional formal banking sector seems inappropriately structured to satisfy this rapid growth in demand and choose not to engage directly. The "new" commercial banks, those that were formed recently through acquiring shells of banks with licences or by other methods are emphasising the micro-finance market, and are posting quite remarkable results in the process.

[1] Compiled by Sibusiso Moyo and Gerhard Coetzee, Post Graduate Student & Research Assistant and Chair of the Rural and Agricultural Finance Programme at the University of Pretoria, respectively.
[2] Micro and Small Enterprise (may include small farmers)

How big is the micro-finance sector in aggregate economic terms? The micro-finance sector is still quite small in comparison with the formal banking sector, but growing much more rapidly. Its contribution to the national economy is probably not accurately reflected in the national data, because of the informal sector nature of many of the industry members, resulting in an under-estimate of size and contribution to GDP. The finance, insurance, real estate and business services sector is a significant contributor to the South African economy, providing approximately 15% of total GDP in real terms in 1998. The total assets of the banking sector at the end of 1998 were R654 billion, with advances totalling R545 billion. In 1999 the size of the micro-finance industry was roughly estimated at R10 to R15 billion with advances at R10 billion (Econometrix, 1999). Recently, a comprehensive analysis of the sector estimated the size of the sector on the basis of current portfolio as R13 billion and the value of loans written per year at R25.8 billion (DTI, 2000). This analysis divided the sector correctly according to loan term and other characteristics, and then compiled an exposure on the basis of annualised figures.

However, any estimate of the size of the micro-finance market should also consider the definition of the micro finance market. For the purposes of this study the micro-finance market is defined as the market reflecting transactions on loans below R10 000 of poorer people in South Africa. Poorer people are considered as those described in marketing studies as people in and below Living Standard Measurement (LSM) Class Five. In the following table the 1998 results of an LSM classification is presented.

Table 1: Living standard measurement categories

LSM	*Number (16+)*	*%*	*Female (%)*	*Unemployed (%)*	*Monthly income (R)*	*Savings (%)*	*Biggest problem*	*People in household*
1	3,738,000	15	59	80	659	4	Unemployment	3.2
2	3,560,000	15	52	74	776	7	Unemployment	3.0
3	4,294,000	18	54	72	929	7	Unemployment	2.9
4	3,314,000	14	51	65	1,244	8	Unemployment	2.9
5	2,041,000	8	52	62	1,664	8	Crime	2.9
6	1,888,000	8	58	61	2,264	6	Crime	3.2
7	2,534,000	10	50	49	5,675	5	Crime	2.5
8	3,246,000	13	49	37	9,752	5	Crime	2.4

Source: Eskom Consumer Surveys, 1998.

Micro-finance also refers to the savings transactions of the poorer portion of the population. It is important to consider both savings and credit as this provide a far more comprehensive picture of the financial market within which poor people operate. Of course there are more financial products pertinent in this strata of the financial market. Most important after savings and loans would be the transmission facilities that are an integral part of the lives of poor people, where support systems and sources quite often do not resort within the same location as households. In addition, insurance products in many guises are also considered to be an important financial product that will be demanded by the poor.

The present usage of banking and financial services by MSEs is very small, with a minute section of the market presently being reached, estimated at less than 1 %. This is the most unbanked area of micro-finance, and an area that is still in the introductory phase in the micro-lending industry. No study exists which provides a comprehensive overview and analysis of overall supply to the lower income and MSE market. Existing studies provide an overview of the institutions active in this market, but do not quantify supply in terms of clients reached. This study necessitates an overview of outreach, and therefore an indicative (rather than exhaustive) summary is provided in Table 2. In the next section each institutional form noted in the table is then discussed in more detail, focussing on the future role of the institution in the lower income and MSE market. The purpose of this overview is to gauge future formal support to this stratum of the full financial sector. After this section an attempt is made to estimate the rural portion of clients served by each institutional format.

2.2 Aggregate supply

In the following table the present supply of micro-finance services in South Africa is described and presented. The assumptions and sources underlying the table are presented in the institution by institution discussion following the table.

Table 2: Summary of retail outreach in the micro-finance market in South Africa (1999/2000)

Retail institutions	Note	Source date	Loans Rm	Savings Rm	Outlets	Estimated % Rural	Loan accounts	Savings accounts
Public sector	**4.2.3**		**330**	**1,646**	**2,440**	**36**	**78,000**	**2,840,000**
Land Bank	i	Mar-00	30		25	80	43,000	
Provincial parastatals	ii	Jun-99	300	600	50	80	35,000	840,000
Post Office Outlets	iii	Jun-99		1,046	2,365	35		2,000,000
Private sector	**4.2.4**		**12,599**	**4,661**	**17,132**	**38**	**7,951,580**	**4,740,100**
NGOs	i	Dec-99	108	5	30	35	66,000	
Village banks	ii	May-00		1	10	100		1,100
Credit Unions	iii	Apr-00	9	10				6,000
Co-operatives	iv	Dec-99			1,200	80		
Commercial Banks	v	Dec-99	12	4,000	4,000	33		4,000,000
Retail stores	vi	Apr-00	5,000		1,000	35	2,173,913	
TEBA Cash	vii	Apr-00	130	600	172	40	86,667	700,000
Private sector	viii	Dec-99	40	45	20	100	25,000	33,000
Registered small loans industry	ix	Apr-00	7,000		5,700	35	5,600,000	
Pawn Brokers	x	Apr-00	300		5,000	35		
Informal sector	**4.2.5**		**400**	**1,760**	**1,150,000**	**35**	**0**	**14,750,000**
Mashonisas	i	Apr-00	150		25,000	35		
Burial Societies	ii	Feb-99		1,560	325,000	35		6,500,000
Stokvels	ii	Apr-00	250	200	800,000	35		8,250,000
Total			**13,329**	**8,067**	**1,169,572**	**35**	**8,029,580**	**22,330,100**

2.3 Public sector

i. Land Bank

The Land Bank has largely reformed itself in terms of its political positioning. However, the Bank's systems and products, as well as clarity on mandate, have not materialised as clearly. In the microfinance arena the Bank managed to launch their Step-up product successfully in April 1998. At the moment they are approaching 43,000 clients and the repayment level is around 80%. The product is being handled by the Start-Up group in Cape Town and the payments and accounts system is handled by First National Bank and the Postbank. The intention is to expand this product. It starts at R250 loans and the ceiling of the last repeat level has recently been increased to R20,000. The mere fact that the Land Bank is entrusting this product to an agent indicates its approach to co-operation and its use of third parties. They lack a service structure, since they have only 25 branches. These branches service their biggest income sources, namely individual farmers and co-operatives. The Land Bank does extend loans to emerging commercial farmers in their bronze range of products (maximum R50 000).

ii. Provincial parastatals

A wide array of failures and limited success is a good summary of the state of the provincial parastatal financial institutions (previously homeland institutions). We only concentrate on those providing financial services. The majority of the retail development finance institutions at provincial level are in severe financial problems, based on a combination of inefficiency, bad policy and strategy, and a severe decrease in government transfers.

At this stage the only successful institution is the Ithala Development Finance Corporation in KwaZulu Natal. This institution is the second biggest public sector mobiliser of savings (after the Postbank). Except for Ithala, the rest of the parastatals are in demise. This will leave a tremendous vacuum, and already now we can see the large number of clients with no access to services. In the Eastern Cape a small rural bank has been formed from the ashes of two conventional homeland agricultural banks that were closed recently. The problem with most of these institutions is a lack of physical premises and outreach (i.e. they have no branch network).

The reformed parastatal banks are increasingly similar in their approaches to the enterprise lenders, except that they have a far greater existing investment and base to build from. Some have savings as a resource (like Ithala with approximately 800 000 clients) and others have institutional investors, which provides them with cheaper access to capital. Some of the largest lenders include Land Bank (which now has a microlending portfolio of 43,000 clients, but an outstanding book of only about R30 million) and Ithala.

iii. Post Office Savings Bank

The Post Bank has the second largest reach to commercial banks on a national scale. However, not all branches of the Post Office provides saving services. Table 3 provides a summary of type and volume of savings held with the Post Bank.

Table 3: Summary of type, number and volume of accounts (Aug. 98)

Products	*Number of accounts*	*Share (%)*	*Balance (Rm)*	*Share (%)*	*Distribution Mostly*
Savings Bank	1,755,880	85.9	699.6	73.5	Rural
Telebank	224,173	11.0	43.6	4.6	Urban
Savings Certificates	63,507	3.1	208.7	21.9	Urban
Total	2,043,560	100.00	951.9	100.0	

The Post Bank has recently completed an investigation into the feasibility of providing loans to existing savings customers. This report has not been implemented yet. Rural people hold the majority of the Savings Bank account of the Post Office.

2.4 Private sector

i. NGOs

NGOs form an important part of the financial market fabric in rural areas around the world. The problems of conventional development finance policy have made NGOs appear to be a promising option in the field of financing small and micro enterprises. This view was based on a belief in the ability of the NGO to reach the target clients and their ability to capitalise on the vacuum left by the closure of many specialised credit institutions in developing countries. The NGO lobby became quite strong and has been elevated to the status of saviours of the poor. What has happened to NGOs providing financial services? Mostly, they needed continued subsidisation and this in essence is part of their inability to provide answers to the retail financial services problem. This does not necessarily imply that NGOs are bad institutions. They simply are not the right instruments to be applied in expanding retail financial services on a substantial scale. This view is echoed in the Strauss Commission's Final Report (Strauss Commission, 1996).

Table 4: Profitability of NGOs in South Africa compared with a Latin American Survey

	Small Enterprise Foundation	Get Ahead Foundation	Rural Finance Facility	Latin American Comparison*
Loan volume per staff member (R)	26,807	26,138	96,145	54,000
Interest earned/average portfolio	46	42	34	45
Interest paid/average portfolio	14	47	15	29
Gross financial margin	32	-5	19	16
Non-interest exp./average portfolio	134	153	120	72

*** Adapted from Schmidt and Zeitinger (1995) and Strauss Commission (1995). An exchange rate of R3.00 = $1 was used for the 1992 figures. The interest earned/average portfolio percentage is based on an assessment of interest in real terms. The use of the Latin American Comparison is indicative, and are averages based on a study of 15 NGOs in the region.**

Although the coverage of NGOs by the Commission was not exhaustive, they concluded that NGOs have very limited coverage in rural areas. The Strauss Commission also calculated that these institutions run at very high costs, which impacts negatively on their sustainability. When comparing local financial services NGOs with international surveys, as seen in Table 4,[3] indications of higher efficiency of the international institutions are visible.

Microenterprise lenders are a special group in the micro credit industry. Around the world, microfinance is associated with enterprise development finance, though in South Africa, microenterprise finance accounts for a very small portion of the microcredit market. Though some "consumption" lending may go towards financing productive activities, Microenterprise finance comes largely from NGOs and Trusts. There is very little overt microenterprise finance from the commercial banking sector in South Africa, which has put a floor of R50,000 on enterprise lending. Khula is the major financier of enterprise finance. A recent report indicated R80 million

[3] The information in these tables are somewhat dated. The Small Enterprise Foundation improved its performance while both Get Ahead Foundation and the Rural Finance Facility closed their doors recently.

outstanding by about 26 lenders, accounting for loans to approximately 45000 microenterprises. This is a tiny portion of the entire industry. Average loan sizes among the micro-enterprise lenders are generally in the R3000 to R6000 range.

ii. Village banks

In 1994 the first Village Bank in South Africa was established in the North West Province. This was the initiative of the International Fund for Agricultural Development (IFAD) and the African Rural and Agricultural Credit Association (AFRACA). A village bank is in essence a savings and credit co-operative. Two more Village Banks were formed until 1996 and thereafter the growth in number was dormant until 1999/2000 when two institutions started a concerted effort to increase the numbers of these village banks.

These two institutions, Finasol and the Financial Services Association (FSA) work independently with different sponsors and support groups to increase the number of Village Banks. FSA, is the original institution that was involved in the formation of the North West Province village banks (albeit in a much less formalised format). FSA is being financed by the Department of Welfare to establish the infrastructure to support Village Banks and to ensure more Village Banks are formed. The United States Aid Agency (USAID) financed Finasol to do in effect the same thing. Finasol had its origin in an endeavour of the South African Sugar Association to reform or restructure its Financial Aid Fund. The USAID financing of Finasol is in question after a recent evaluation of Finasol.

It seems as if there is a considerable demand for collective action formats at the grass roots level in South Africa. This is indeed the premise on which most of the activities of FSA and Finasol is based, and their recent success with the formation of more groups are evident of this local demand for financial services. They have assisted in the formation of nearly 30 village banks to date.

iii. Credit Unions

Credit unions have along history in South Africa. After a restructuring of the movement the Savings and Credit Cooperative League of South Africa (Ltd) has now been active in Financial Cooperative Development in SA for the past three years. Currently SACCOL has 21 Savings and Credit Cooperatives (SACCOs) registered with it. Our SACCOs have a combined membership of over 6,000 members with member's savings of just over R10 million mobilised. The loan book has a balance of R9 million. All loans are issued to members who are also saving. The development of the movement has happened with minimal donor or Government support. For the past three years SACCOL has received no donor support, which, while admirable, has constrained their ability and capacity to serve the "poorest of the poor", due to the high start-up and servicing costs involved in rural development. While SACCOL has not actively sort out rural area development, it continues to happen as requests for SACCOL's assistance in the development of Financial cooperatives keeps coming in.

iv. Co-operatives

The dominant form of co-operatives in South Africa is agricultural producer co-operatives. Most of these provide financial services to members, mostly commercial farmers and not entirely the focus clientele of this study. However, some 40 of these producer co-operatives initiated project-based endeavours to assist small farmer development. Some of these services encompass financial services in the form of production loans to small farmers.

The extensive infrastructure and existing member base of these co-operatives provide opportunities in the provision of financial services to members. One opportunity exists where commercial banks do not acknowledge the asset value of milk producer's quotas provided by a sizeable local dairy co-operative. It makes sense that the dairy co-operative attaches value to milk quotas and therefore this presents an opportunity for linking this asset value with other financial services. The interest in financial co-operatives goes wider as farmers in the Eastern Cape/Karoo area already expressed interest in the joining of nearly 1000 farmers in a financial co-operative with the objective to negotiate more favourable priced funds for production than is possible by individual farmers.

Due to the over emphasis of producer co-operatives and the retail financial services offered by commercial banks in the past very little attention has been given to financial co-operatives and its potential in commercial agriculture, and extending these services to developing agriculture. The declining importance of agriculture in the portfolios of commercial banks and the costs associated with the provision of retail financial services in rural areas may provide opportunities for collective action in the form of financial co-operatives in rural areas. In effect, the withdrawal of commercial banks in Canada from some farming areas gave rise to the formation of the strong Canadian Credit Union movement. This is something that may hold true for South Africa in the near future.

v. Commercial Banks

In the drive to high profits and growth many of the commercial banks entered into mergers and acquisitions with other institutions in order to grow market share. The five largest banks in South Africa (Standard Bank, ABSA, First National Bank, Nedbank, and BOE) presently hold over 80% of the market share. Although the mergers and acquisition approach is in line with international banking trends, closer analysis shows that for South Africa the bigger banks exhibit diseconomies of scale. The banking environment itself has changed significantly during the last few years, with a clear move towards ATM and internet banking, away from the brick and mortar approach of the past. Old delivery channels of service are on the decline. In the market for deposits the banks are losing ground to smaller niche banks, which are more flexible and which can target specific segments more efficiently than the larger banks.

Commercial banks only provide a limited range of services in rural areas, although they have the highest incidence of branches in the rural areas, together with the Post Office (Strauss Commission, 1996). South Africa also has a higher ratio of branches per population than elsewhere in Africa. However, this higher incidence of branches is skewed, with rural areas having approximately double the number of people per branch than urban areas. A sharp decline in rural branches is also evident. It is estimated that whereas in 1995 approximately 50 per cent of the South African population had easy access to commercial bank facilities, this number has declined recently to approximately 30 per cent.

South African commercial banks are comparable in terms of development and technology to the commercial banks of Europe and the US. Although there may be efficiency differences, South African banks are quite advanced in most aspects. It would therefore be possible to assess international trends in retail banking and expect similar trends from South African banks. Studies show that retail banking would change considerably in the future. Several issues have an impact on commercial banks. Little evidence exists to substantiate scale economies at a "macro" level for consumer banks and financial institutions. This explains the fragmented condition of the sector at present. The shape of retail banking at this stage seems to confirm that those forces pulling banks into smaller, more fragmented units appear to be relatively balanced with those that would naturally lead to consolidation. Consolidation is therefore slow, due to the fact that limited exploitation of scale economies is taking place. The number of products offered by banks is increasing, which drives up the total management cost. It seems that retail banking is inefficient in its current form.

Technology is providing a counter to this trend of inefficiency. Technology revolutionises the moving and storing of money and bank product distribution. In addition to decreasing the costs of current bank practices, new technologies are also creating alternative distribution channels for retail banking products. This result in far cheaper ways to reach customers than by retail branches (in the United States telephone banking is more than 50 per cent cheaper than branch banking), and these non-traditional channels are gaining market share. It is especially the younger customers that are abandoning conventional branches for the alternative technology driven outlets.

The question of the impact of these trends on rural finance also arises. The process and speed of adjustment and transformation of commercial banks will differ among countries. With increased globalisation, the main constraints on change will be country specific regulations and the ability to take up and apply technology. The banks that change the quickest will be recognisable in that they will sharply diminish their branch network, keeping only those branches with upscale or high net worth demographics. They will segment their client base and cross-sell only to those that clearly offer profit potential. They will increasingly interact with clients through electronic devices (the personal computer, the telephone, the Internet), and will clearly diminish the focus on rural areas, and especially remote rural areas. Areas without high net worth demographics, electricity and communication channels will not be part of the new way of banking. To all intents and purposes no major expansion of commercial bank activities should be expected in rural areas. One would only expect banks to show more interest in rural communities, once technology has been made accessible to rural people.

Small farmers and rural people in general will still save with commercial banks, however it will become increasingly costlier to do this as bank branches decrease in number in rural areas. Commercial banks do invest in the micro-finance market, however indirectly through purchasing shares in banks with micro-finance portfolios (the case of ABSA and Unibank) or by striking strategic alliances with commercial banks with micro-finance portfolios (the case of Standard Bank and African Bank).

To summarise –

- Conventional commercial bank presence in rural areas will decline at an increasing rate,
- the farming portion of the commercial bank portfolio will further decline over time,
- emphasis will be on the agribusiness sector and larger producers,
- financial services to farmers will be provided by the broad retail sections of banks and farm specific portfolios will decline. This will be based on the diverse income sources of future commercial farmers.

vi. Retail stores

The furniture and retail store lenders are the latest entrants to the micro-finance market, primarily arriving since the creation of the Micro Finance Regulatory Council (MFRC).[4] The furniture industry is already a R15 billion industry per year in South Africa, with about R10 billion of that being sold on credit. Historically, furniture sales have been made under the Credit Agreements Act, which restricted interest rates to the ceiling of the Usury Act, while allowing the seller to retain ownership of the goods sold as collateral. However with the advent of the MFRC and a clearer more transparent regulatory environment for micro-lending, many of the furniture lenders, as well as other retail stores such as Woolworths, have also entered the market. They have registered branches as micro-lenders and are actively promoting micro-loans to their regular, well-known clients. These lenders have a solid credit history on their clients and rely on a credit scoring methodology to assess risk and do not require debit orders or other deductions at the source. Most of their clients are salaried employees, however.

vii. TEBA Cash

Tea Cash is the institution responsible for handling the payments system of mineworkers in South Africa. They have 172 offices over Southern Africa. As they have a large compliment of savings accounts and an immediate market (the mineworkers), they recently applied for a banking licence, which has been granted recently by the Registrar. They provide over the counter loan products (very similar as envisaged for the Postbank) and have a loan book of around R130 million at this stage.

viii. Private sector agricultural firms

Started by the Financial Aid Fund of the South African Sugar Association 20 years ago, the trend for the private sector processors has recently been boosted by the cotton ginners and vegetable processors and agents. Farmers are provided with crop establishment capital and in some instances production credit. Some institutions also

[4] The MFRC was launched in June 1999. It has been tasked by the Department of Trade and Industry to regulate the microlending market. Microlenders must register with the MFRC in order to provide loans with no ceiling on interest rates.

provide extension services. This method of finance is quite common in non-farm MSEs and in contract farming. It has potential for development on a vast scale in the agricultural sector, especially if commercial farmers can be convinced to contract small farmers to ensure throughput and turnover.

ix. Registered small loans industry

The quick growth of the micro loans industry is a product of a gap in the market for small loans. It is active in making short to medium term loans available to individual borrowers that normally fall outside the formal banking network, due to the inability of the loan applicants to provide conventional collateral. This gap has been filled by institutions that combined easy access arrangements to homegrown collateral models. These operators provide credit services to clients who can provide them with proof of employment and a bank account. The small loans firm withdraws the payments according to the loan contract after each wage or salary deposit made by the employer into the borrower's bank account. This is an urban-based product that does not fit the profile of rural people, who often have inconsistent income patterns. It is not seen as a major growth industry in rural areas, except in larger rural towns.

There are major drives to organise this industry. Several associations have been formed and registration with the newly established Micro Finance Regulatory Council (MFRC) is compulsory, if operators decide ton conduct business within the exemption to the Usury Act[5]. It is expected that some of the larger more formalised operators (some of which already listed on the stock exchange) will investigate the formation of banks soon.

The available information in South Africa fails to differentiate accurately between rural and urban micro-finance. There are several different segments in the industry:

- Formal registered firms, which include commercial banks, financial institutions, section 21 (not for profit) enterprise lenders, developmental lenders, and the larger short term money lenders;
- Semi-formal money lenders, which include small unregistered money lenders who are doing it as their main livelihood and the pawnbrokers, who are not formally included in the money lending statistics (yet); and
- Purely informal moneylenders such as the township moneylenders (mashonisas) and stokvels, burial societies, and ROSCAs.

These different lenders can be regrouped into different categories based on the type of lending that they are involved in. The first four are focused on "consumption" lending and lend only to customers with bank accounts and regular salaries (thus urban orientated). The other lenders, either developmental or enterprise lenders, generally base their repayments on cash flow from the productive activity. The source of repayment is the main differentiating factor between the two groups of lenders.

Short Term Cash Lender

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[5] Government Gazette of Pretoria, 1 June 1999 (Vol. 408), Department of Trade and Industry, Notice in terms of Section 15A of the Usury Act, 1968 (Act No. 73 of 1968), No. 713.

The short-term cash lender focuses on loans up to 32 days, or the next pay period. On average, these lenders charge an interest rate of 30 percent per month, all fees included. They are the largest number of individual institutions, but each branch tends to be relatively small in size, with loan book of between R50,000 and R500,000. Their target market is clients with a net income of up to R2,000 per month. The average loan for these firms is about R500, as it takes into very strict consideration the capacity of the borrower to repay at the end of the month. Capital resources come mainly from their own sources, and occasionally from illegal loans from friends (illegal because this is not allowed under South African law).

It is important to note that the rate charged by 30-day cash lenders applies to all loans less than that period or which are repaid on a weekly basis. This raises the effective interest rate of the loan. Very important to note that even with the bank cards and pin numbers, the default rate on loans was in the neighbourhood of 2.5 - 5 percent. Now that the uses of bank cards and pin numbers have been eliminated, this rate has tended to double among the lenders.

Medium Term Cash Lenders

There is often a fair amount of overlap between firms that are lending between one and six months and the term lenders. They have a mix of products that are in majority 30-day loans, but also a range of slightly longer-term loans reserved for their better clients. Average loans in the 1-6 month category can increase to a multiple of the person's actual net take home pay, as they have more time to pay it off. Historically, these lenders have also used the bankcard with pin number as the repayment mechanism. With the restriction of the use of the bankcard, many of these lenders are experimenting with other forms of collection.

Interest rates will vary by the term of the loan, but are usually discussed as a flat rate on a declining balance, which effectively increases the effective rate. The nominal interest rate may be between 30 percent (for 30 days) and 12.5 percent (per month for the period), but the effective interest rate is always greater than 20 percent per month. Because these loans are made to better-known clients, the default rate is generally lower, about 2.5 percent, without the bankcard.

Since the short-term cash lenders and the medium term cash lenders are often lumped together into the same category, since branches often do both, it is difficult to differentiate between them. Overall, the estimates from the credit bureaux specialising in cash borrowers are that there are now roughly 3,500 – 4,000 storefronts in the country. This figure is down from an estimated 6,000 storefronts two years ago, and is expected to continue decreasing this year to a ceiling of 2,500 storefronts by the end of the year.[6]

Term Lenders

The term lenders make loans for periods between six months and 36 months. The industry started through the use of Persal, the government's central payroll system,

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[6] Conversations with Compuscan and MicroLenders Credit Bureau (MLCB)

using debit orders to get repayment at the source, before the borrower actually had a chance to see the money. Now that these lenders are saturating the market, they are branching out to the larger private companies to establish credit service relationships with them. This is the most rapidly growing segment of the industry, but which has often been restricted by cash to lend. The commercial banks are becoming increasingly involved in this segment of the market, buying up the large term micro-lenders to develop their access to the market, while reducing the financial constraints on their lending partners.

Housing Lenders

Housing lenders are closely associated with the term lenders. Most long-term mortgage loans are greater than the ceiling set for micro-loans and fall outside of the exemption. But there are a lot of micro-loans made in the name of housing, as it is the basis of access to a Persal code, which greatly facilitates repayment. Housing loans can also be secured by provident funds, effectively bringing the risk to near zero. Large banks are involved in housing finance, as well as small specialised lending boutiques. The National Housing Finance Corporation (NHFC) has a number of programmes to assist retail lenders to access finance to on-lend to borrowers for housing improvement.

The NHFC promotes both urban housing as well as rural housing. Lenders in the housing industry include micro-lenders, small banks, social housing programmes, and non-bank financial institutions (NBFI) such as NGOs. Methods of securitization include: none (unsecured), provident fund, payroll, and mortgages. The Rural Housing Loan Fund (RHLF) programme works with micro-lenders doing housing in the rural areas with unsecured loans, for which interest rates of 40 percent (on a declining balance) are common. For provident backed loans, margins above the cost of money are typically between four and five percent.

x. Pawn Brokers

Pawnbrokers comprise one of the oldest industries in South Africa. Pawnbrokers use durable and semi durable goods as collateral against money that they advance to individuals in need of short-term (generally less than 30 days) funds. These are often used to finance emergencies, or short term cashflow deficiencies in their daily lives and businesses. The advances are made against the pledged item(s) at a rate of 25-30 percent per month, and the borrower has up to three months to reclaim his items by paying off the advance, or else he forfeits the items that he has pledged. Between the time the pawnbroker has made the advance until the time the client comes to reclaim the item, the pawnbroker must store and maintain the item in original condition. If the client forfeits the item, the item then belongs to the pawnbroker and he is free to sell it as a second hand good. Roughly 35 percent of all pawned items are not paid off and collected.

While there are many debates about the value that is applied to the items that are pawned compared to their real value, the pawnbroker must incur many costs. The pawnbroker must appraise the item, transport it to his shop, store it for up to three months (with the opportunity cost of capital), and, if the item is not collected proceed with the sale, which could take several months depending on the demand for the item.

There are roughly 5000 pawnbrokers in South Africa, according to the Association of Pawnbrokers, which officially represents 1500 of them. Pawnbrokers are registered under the Second Hand Goods Act, so are already regulated and pay VAT on all transactions. The cost structure for pawnbrokers differs radically from the cost structure for micro-lenders, due to their primary operation of storing and selling the second hand goods. Most loans are for one month or less. Estimating that the average portfolio outstanding is about R 60,000 per pawnbroker, there is an outstanding monthly balance of about R300 million. Taking an average term of one month (which may be too long), there is an annual turnover of R3.6 billion.

2.5 Informal sector

i. Mashonisas

The mashonisas are the informal sector lenders who operate completely outside of the formal sector. When there was no other alternative for borrowers, the mashonisas were their solution. The mashonisas specialise in short term loans, generally for 30 days. Interest rates run in the range of 50 percent per month, though no additional interest is charged if the borrower is late, effectively reducing the cost of lending. Mashonisas are often women with no other means of support who try to earn a living wage out of this job. They will often have 15-20 clients, borrowing an average of R150 –250 at a time, so individually, they are extremely small players. However, there are many of them, estimated at between 25,000 and 30,000 around the country. Monthly earnings by a mashonisa are often quite small, in absolute terms, in the range of R2-3,000 per month. Interestingly enough, it appears that most mashonisas are very close to their clients and the clients are loyal to them. The borrowers' survey, referenced below, demonstrates that most clients of mashonisas look to make sure that they can afford the repayment stream before starting their payments.

The best estimates on the number of township moneylenders are approximately 30,000. This is the figure that has been developed by Du Plessis and is most commonly referred to by researchers. The research by Jimmy Roth on Township moneylenders in the Grahamstown area can be taken as a proxy for the average lender. This was confirmed by a recent survey in the North[7], which found similar statistics. The typical lender has about 15-20 clients with a total outstanding book of about R5,000. Therefore, using this as a proxy, the township lenders account for about 600,000 clients on a monthly basis, equal to the number from the formal moneylenders, but their outstanding book is significantly smaller, about R150 million. On an annual basis this comes out to R1.8 billion.

ii. Stokvels and Burial Societies

In this instance, we use Stokvels to refer to the various informal financial institutions that capture member savings and then either save them or on-lend them to some of the members of the groups on a rotating basis. These include the Stokvels, properly stated, burial societies, and rotating savings and credit associations (ROSCA's). According to the National Association of South Africa of Stokvel Associations

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[7] By Matome Kgowedi from the University of Pretoria.

(NASASA) there are an estimated 800,000 such institutions comprising about 8.25 million adults accounting for about R200 million a month in savings. They are governed under the Banks Act under the Stokvel exemption. This allows for stokvels, as member based organisations providing services just to their members that are members of the NASASA to be regulated by NASASA. Only 15,000 groups are officially registered with NASASA, but in actuality, as all Stokvels are only providing services to their own members, this is considered to be safe.

In terms of calculating costs associated with lending, there are very few. Management of the associations is voluntary, and most of the funds are normally distributed to members at the time of the group meeting and deposit of funds. Since all repayments, with whatever interest, if any, go back into the group fund for redistribution to the members, the interest rates serve more as mechanisms for forced savings for the members. Interest rates may or may not be charged depending on the group and its operating procedures.

The amount of savings and loans regarding stokvels reflected in Table 2 are merely estimates. Table 2 represents current portfolio. Stokvels, in the form of ROSCAs rotate pay-outs, and thus mostly has no funds in savings accounts and very little in loans outstanding. The estimates are considered to be conservative.

The ESKOM consumer survey of 1998 confirms the existence of numerous burial societies. The surveys estimate 6,5 million South Africans are members of burial societies. We have estimated on a conservative basis that if each one of the members contributed R20 per month for a year the accumulated total will be R1.56 billion. This is a severe under-estimate as many of these societies have monthly contributions per member far in excess of R20 (see survey results in section 7). However, we also consider the reality that much of these savings would be deposited with commercial banks, the Post Office Bank or other formal savings facilities. Thus, double counting may be possible and the total savings figure should be treated with caution.

2.6 Discussion

It is clear that the small loans industry (consumer lending) dominates the micro-finance loan market, while the commercial banks dominate the micro-finance savings market. This is not an exhaustive overview but rather an indicative overview. It relates coverage (outreach) with the high cost of intermediation as found by the Strauss Commission (1996). Table 2 indicates a substantial outreach at first glance. However, if these institutions and their clients are studied more carefully, the following observations can be made:

- More clients have access to savings and transmission facilities than to credit facilities.
- Micro and small entrepreneurs have only limited access to loan facilities.
- Consumer lenders provide the majority of loans.
- The majority of savings instruments are still informal.
- In general, there exists a dichotomy between providers of savings and credit services.
- The majority of the services, indicated by the lack of presence of providers in rural areas, are offered in the larger towns.

The analysis encapsulates the lack of services in rural areas and specifically those involving people not engaged in wage or salaried labour. However, in the rural context, individual incomes are not as important as household incomes, and thus households could participate in the market described above. It is also quite difficult to divide households into farming and non-farming households. This is illustrated in the next section.

2.7 Rural and small farmer finance

2.7.1 The recent history of rural and small farmer finance in South Africa

Recent history can best be summarised by the work of the Commission of Inquiry into Rural Financial Services, better known as the Strauss Commission. The Commission was active in 1995 an 1996 and made a range of recommendations of which the most essential are highlighted here. The detail including the methodology and approach is reflected in Annexure 1.

The Commission considered the major policy objectives of government and its brief, to contribute towards increasing access to financial services for rural people. These services were identified as transmission services, savings products and loan products for consumption smoothing and productive loans (for farm and off-farm activities). The Commission also identified that state grants would be necessary under certain circumstances. The Commission called for a detailed set of guidelines on the management of subsidies and grants, including their phasing out.

A role was identified for the state to facilitate as well as co-ordinate the provision of financial services, with special attention to the needs of women. In this regard the Commission proposed that the Land Bank be tasked to fulfil this role. The way in which the Land Bank, the state and other institutions act must be in support of the market. At the same time the inherent weaknesses in the existing institutional fabric must be acknowledged, as these institutions are not able to contribute to the aims of rural reconstruction on a national basis without appropriate and active support.

A review of the policies and activities of different state institutions, such as government departments and parastatals pointed to the dangers of lost development potential unless co-ordination takes place. The Commission therefore argued that the state must ensure that the improved availability of rural financial services is provided as part of an integrated rural development strategy. This programme must include the land reform and housing programmes, the upgrading of infrastructure such as the provision of water, electricity and roads and capacity building, especially at the level of rural local government.

The Commission also argued that the state must acknowledge the current gap in rural finance delivery, and an overlap in the prospective policy briefs of the state funded development finance institutions. International experience points to the success of multi-sector financial institutions at a retail level and a rich discussion exists on apex institutions internationally. However, there is very little experience, and little mention is made, of the advantages and disadvantages of multi-sector *versus* single sector wholesale institutions. The Commission accepted that all national development finance institutions have mandates to either continue or commence the extension of wholesale lending in rural areas: The National Housing Finance Corporation (NHFC) has earmarked dedicated funds; The Development Bank of Southern Africa (DBSA) will fund rural infrastructure projects; Khula Enterprise Finance (KHULA) intends to finance Small, Medium and Micro Enterprises (SMMEs) in rural areas. The Industrial Development Corporation's portfolio already includes large-scale agro-industrial investments. The Commission supported the need for a financial institution at national level, such as the Land Bank, with both wholesale and retail activities and the responsibility to dedicate special attention to the needs of land reform programme beneficiaries. The Final Report (Strauss Commission, 1996) of the Commission emphasised that the Land Bank should focus on only agriculture as a sector, while the Interim Report (Strauss Commission, 1996) looked at agriculture as the primary focus, but did not exclude a multi-sectoral approach. A focus on a single sector can contribute to increase risk exposure for the institution. Especially in the South African agricultural setting it may imply increased covariant risk.

The Commission recommended that the future role of each of the provincial development corporations should be the result of specific consideration and consultation. This should be a joint approach of the national Ministry of Finance, the national development finance institutions, the provincial departments and the provincial development corporations. The proposed development council should provide guidelines for this purpose, without attempting to design detailed blueprints for implementation at the provincial and retail level. This approach ensures that within a flexible framework, specific implementation strategies that reflect the reality of a specific setting or province could be worked out at provincial level, rather than being prescribed from the national level. Overall the same rules should apply; implementation should however be realistic and pragmatic.

At the retail interface with rural clientele, the Commission recognised the important role of the Post Office in satisfying the most basic financial service needs, especially of the poorest, less mobile segments of the rural population. Commercial banks have, however, increased their outreach, and are well-placed to offer savings facilities in the larger rural towns and respond to loan requests from small business entrepreneurs. The NGOs have shown themselves able to reach a micro-enterprise level that the formal banking institutions do not yet serve. The Commission proposed a multi-pronged strategy at retail level rather than a single institutional strategy. The purpose was to accommodate flexible approaches and reflects the reality that the diverse circumstances in the country require diverse institutional approaches. Furthermore, the analysis done by the Commission showed that none of the current institutional structures proved to be highly successful in reaching rural clients, especially deep rural clients, and therefore it will be short-sighted to choose a single institutional strategy in this regard.

In order to foster an integrated approach to both urban and rural development the Commission considered it essential to create an entity to co-ordinate and guide the activities of development finance institutions. This entity, referred to as the Development Council by the Commission, would be supported by a secretariat that could also play a part in structuring the reporting requirements for entities that make use of state support. All development finance institutions and other recipients of state financing would be obliged to conform to appropriate reporting and accounting standards, as the introduction of minimum disclosure requirements would enhance transparency and accountability. This function should be monitored and implemented by the Development Council's Secretariat.

The Commission also recommended that legislation governing agriculture, banking and land, presently in force in different areas of South Africa, should be harmonised as soon as possible. The Commission gave attention to legislation of the hitherto un-legislated sections of the financial market (for example, NGO financial service organisations, village banks type organisations, savings and credit co-operative type institutions) and proposed that these complex issues should be attended to by specialists in the field.

The Commission argued that a process actively guided by the state, should be launched as soon as possible to transform the rural financial services sector. This process should build on the strength of existing local level institutions in the private, public and voluntary sectors. The need for a wide range of service providers delivering different products and catering for the diverse rural financial needs was accepted. The Commission favoured fostering a much wider retail financial services network. However, the Commission was concerned about longer term sustainability as well as outreach.

The Land Bank's wholesale function will be geared to fostering, nurturing, supporting and co-ordinating local and provincial level rural financial institutions, be they NGOs, development finance institutions, co-operatives, commercial bank branches, local authorities, or any other kind of institution seeking to render agricultural and agriculturally-related financial services. Essentially the Land Bank's "wholesale" function should reach those "retailers" who seek to serve the individual and small group agrarian needs of people in the "deep rural" areas, e.g. small scale individual farmers, groups of female vegetable gardeners and small scale poultry producers who are far away from the relatively limited retail branch network.

The responsibility of the Department of Agriculture to promote agricultural development is acknowledged. The Commission, however, recommended that the Department terminate the ACB and suspend current policy initiatives, which would lead it to the role of a direct (central) wholesaler.

The Commission identified female farm workers; male farm workers; landless, unemployed rural poor; pensioners; small-holders; contract farmers; rural businesswomen; rural businessmen and small scale employers and large scale rural employers, including commercial farmers as requiring special support measures to gain access to financial services. The Commission also drafted guidelines on the application of subsidies and institutional transformation.

These recommendations of the Commission were put forward against the background of a set of guidelines, based largely on comparative international experience. The set of guidelines is important for this study and includes:

- views on the access to financial services;
- the application of commercial principles;
- diversification in terms of different financial services and sectors;

- ensuring that existing capacity is not eroded and refraining from the formation of new structures (rural areas in South Africa are characterised by a plethora of institutions with overlapping competencies and a lack of co-ordination - existing structures should be adapted, rationalised and co-ordinated to serve the needs of reconstruction);
- flexibility where locational differences are acknowledged and incorporated in policy and strategy;
- incentive based approaches;
- improving information flows to ensure better decisions;
- the management of risk and the structuring of the rural finance system in order to minimise the impact of covariant risk; and
- the detrimental effect of direct intervention by the state in retail financial markets.

Discussion of the Strauss Commission reports

The Commission Reports emphasised a paradigm shift and a movement away from the supply-led approach, rather than a detailed programme for implementation in order to increase access to financial services in rural areas. This shift is indeed necessary as most of the South African parastatal institutions follow a supply-led approach, as proved by the Commission. Although the Land Bank has been tasked to fulfil certain functions, no point exists where these functions can be co-ordinated with activities in the provinces. As the provinces have constitutional responsibilities, and the provincial governments are the only shareholders of the respective provincial development finance institutions, they should change their approach and transform these supply-led-type institutions. At this level a number of different activities are underway. It is not clear, though, whether these activities will get adequate political support, neither is it evident that they are co-ordinated, and no overall actions are taken to solve the core problem – namely, access to retail financial services.

The Cabinet of the Republic of South Africa accepted the Strauss Commission proposals in August 1997 (Agricultural News, 1997). The Land Bank, which previously reported to Cabinet through the Ministry of Finance, now reports through the Ministry of Agriculture (Agricultural News, 1997). This continues the distinct agricultural emphasis of the Land Bank. The shift in thinking on the role of the Land Bank in the development finance system, but more specifically, as rural financier, also changed between the publication of the Interim Report of the Strauss Commission and the Final Report (Strauss Commission, 1996). In the Interim Report of the Commission it was emphasised that the Land Bank should provide wholesale financial services to retail institutions in rural areas across the whole spectrum of sectors, not only for agriculture. In the Final Report (Strauss Commission, 1996) this recommendation was narrowed to include financing of agricultural activities only. This, of course, increases the exposure of the Land Bank to covariant risk, and is a contravention of the Commission's own guidelines, specifically the guidelines regarding the minimisation of risk.

The lack of clarity in the Final Report (Strauss Commission, 1996) on co-ordination of rural financial issues aggravates the overall lack of clarity in the field of rural development co-ordination in the country. Between the Interim and the Final Reports the Commission changed its views on the responsibility to co-ordinate rural finance issues, which contributed to this lack of clarity.

Lastly, the Commission gave a clear proposal on how the overall development finance system should be co-ordinated. It did not provide any indication of the relevancy of the structure of the development finance system in South Africa. Although this was not included in the brief of the Commission, it did define a role for the Land Bank within this system, without questioning the system itself.

Conclusion

The Strauss Commission considered the reality of the rural areas of South Africa, the demand for financial services and the current institutional structure and, against a set of guidelines, made a number of recommendations directed at different problems. Some proposals attended to the access problem and the expansion of retail financial services in the provinces. Another set of proposals addressed national level responsibility for providing capital and support to provincial level institutions. Legal issues were also addressed, especially the legal status of women. A further set of recommendations aimed to structure a national level support system for rural finance retail institutions in the form of the Land Bank. The Commission also proposed a structure to achieve co-ordination between national level institutions.

The most important paradigm shift brought about by the Commission was the rejection of a supply-led system of rural credit. Thus subsidised interest rates and credit programmes in which government decides what is best for the client were rejected. The Commission emphasised that a broad range of services should be accessible, namely saving and transmission facilities and credit products within a demand driven system. It further emphasised the importance of the retail network in rural areas to achieve access to these services. In this regard special mention was made of a role for the Post Office with respect to the provision of savings products, transmission services and other agency services. The Commission also stated that although subsidies are necessary, they should be implemented within strict rules and be finite in nature. The Commission supports an integrated approach, in which it is clearly stated that financial services on their own will be inadequate.

The Strauss Commission recommendations pose several challenges. The most important is not the structuring of the national level financier - the real challenge lies at the retail level. Many countries have failed dismally in this regard and few successes can be noted. The challenge is essentially to achieve success within a specific set of guidelines, the most challenging being to achieve sustainable institutions that impact positively on development by ensuring wide access to financial services. The second challenge lies in achieving co-ordination between government departments and a host of institutions to achieve a positive development impact. Co-ordination between land reform programmes, agricultural development initiatives, provision of infrastructure and basic services and the provision of communication and energy services is an essential requirement of successful rural development. To this should be added the challenge to make local government work.

Another prominent challenge is political commitment to meeting these challenges, one of which is to refrain from interfering in the rural financial markets. Past approaches saw the state using financial markets as a vehicle to distribute subsidies.

The challenge is to leave financial markets to their real role, that of allocating financial resources to viable investments.

2.7.2 The current supply of rural and small farmer finance

Table 2 provides adequate information on which to assess the scope of rural and small farmer finance. As stated, it would be virtually impossible to do a clear delineation between rural and urban microfinance. In Table 2 a column was added that estimated the number of outlets in microfinance institutions that one would find in rural areas. It is estimated that approximately 37 per cent of 19500 formal retail outlets are in rural areas where a client could enter into either a loan or a savings transaction. It is also estimated that approximately 35 per cent of the 1,150,000 informal "outlets" in South Africa can be find in the rural areas.

If we turn to financial services for small farmer agriculture it is even more difficult as it is expected that many diversions of loan funds do occur due to the general unavailability of sources of small farmer agricultural credit. Much of small farmer agricultural activity is also cyclical in nature and many "small farmers" will leave farming if economic conditions improve and wage income opportunities are more available. On the other hand, one can also assume that a sizeable proportion of small farmer credit also gets diverted, due to the simple fact that many "small farmers" are forced to obtain the credit for small farmer purposes, albeit that they have other needs than for agricultural production. We have to ask ourselves the question, what is a small farmer. Without entering the minefield of definitions Table 5 serves as an indication of the confusion around the concept of small farmers.

Table 5: Selected results from farm household and small business surveys in two provinces (1997)

Item (in %)	Small Farmers surveys		Small business surveys	
	NP (n=150)	KZ (n=152)	NP (n=270)	KN (n=225)
Agricultural income as % of gross income	3.4	2.8	1.0	8.5
Percentage who used loan finance to finance:				
• Durables/assets	4.0	9.9	14.0	16.0
• Farm inputs/other inputs	7.3	9.0	7.0	11.0
Savings at (in % of respondents):				
• Formal institution (average distance km)[a]	29.0 (60.7)	29.7 (45)	92.0	77.0
• Informal institution (average distance km)[b]	80.7 (0.0)	29.6 (19)	64.0	76.0
Sources of finance for establishment of business:				
• Personal savings			93	73
• Retrenchment package			30	12
• Pension			17	1
• Loan from family or friends			10	5
• Loan from development corporation			6	6
• Income from other business			4	13

a. The institutions with highest use.
b. Information not available for small business surveys

The table confirms the fact that rural people have diverse income streams that may include farming as a source. This is not entirely surprising as it represents one of the numerous ways in which poor people manage risk, i.e., by diversification of income sources. When we interview on the basis of stereotyped notions of small farmers, we may find that a "small businessman" has a higher income from farming activities than a "small farmer". We may also find that the majority of small farmers may be female.

However, it is assumed that since agriculture plays such a small part in the household income streams of most small farmers that loans for agriculture are quite scarce and targeted towards those that are fulltime farmers (ironically the higher risk farmers). To refer to small farmer finance may therefore be somewhat incorrect, whereas the concept of rural finance is non-sector specific and emphasises rural areas as the locality of financial transactions.

It is estimated that less than 1% of the portfolio of the Land Bank is for small farmer financing (loans below R10000 to keep with our definition of microfinance). Approximately 30% of the outstanding small business finance book of provincial parastatals will be for small farmer finance. This will decline and should not rise above 25% as most of these banks cap their exposure to agriculture after the restructuring of these institutions.

It is expected that there exist a leakage to farming activities in the portfolios of some institutions without specific farming loan products. These institutions include NGOs, Village Banks, agricultural co-operatives, TEBA Cash, stokvels and even the microlending sector. It is however very difficult to assess the magnitude of this leakage.

2.7.3 Access to financial services for rural households and small farmers

In the final analysis we are focusing on the access to financial services by rural people. In this section we reflect the expressed demand of rural people for financial services. Note that demand is equated to expressed demand since no comprehensive demand study with respect to rural finance have yet been executed in South Africa, barring the analysis of the Strauss Commission that qualitatively derived demand from a description of economic activities in rural areas. In Table 6 and 7 some results of a survey executed in 1997 are reflected to serve as an indication of the characteristics of rural households and their use of financial services.

It is clear from the tables that farming plays a small role in terms of income, although a major proportion of small farming and small business households (thus rural households) cultivates the land and produce crops. Very small proportions of crops or livestock are sold and the majority of the households are deficit producers (Van Zyl & Coetzee, 1990). The majority of households in all the surveys do not access credit (or are unable to access credit services) while most households are engaged in savings activities.

A rich fabric of informal financial arrangements was identified, although not at a comparable frequency with urban areas. Under the conventional approach clients would have been bombarded with credit, while in the circumstances outlined in the surveys they do not demand a high level of credit. The clients in these surveys accessed loans from the development corporations (or provincial parastatal financial institutions) and the informal markets. This may indicate an inadequate supply of formal credit either in the form of no access or inappropriate financial products on offer. Most people who save money have commercial bank accounts. This indicates an effort to deposit savings since the majority of rural branches of commercial banks are in medium to larger towns, which are normally far away from these clients. The

PostBank and NGOs did not feature in the survey results. In the case of the Post Bank it may be due to the fact that not all rural Post Office branches offer savings facilities. It may also indicate the inefficient services provided based on outdated savings product technology (this has recently been addressed by computerising the manual centralised processing system of the Post Bank). Very few financial NGOs are active in rural areas in South Africa and the penetration of the rural finance market by NGOs is therefore negligible.

Table 6 Illustrative profile of farming households based on recent surveys in two provinces

		Northern Province (N=150)		KwaZulu/Natal (N=152)	
Household characteristics					
• Male household head (%)		68.0		72.4	
• *De facto* female household head (%)		99.3		66.4	
• Household size		-		8.8	
Land tenure					
• Cultivate all land (%)		79.3		58.6	
• Leased land out (%)		8.0		9.9	
• Borrowed farm land (%)		9.3		13.8	
Services and energy use (% of households)					
• Use grid electricity		7.3		61.8	
• Use flush toilet		1.3		1.3	
• Cook with fire wood		95.0		78.9	
• Water source unprotected		83.3		66.4	
• Public standpipe		44.0		19.1	
Gross annual income (R)					
• From farming		394		637	
• From wages		9308		14157	
• From micro enterprises		149		1294	
• From remittances		974		4251	
• From pensions		1489		2667	
Farm assets - % of households with:					
• Car/Bakkie		5.3		22.0	
• Tractor		5.3		2.0	
• Trailer		2.0		1.3	
• Plough		4.8		6.0	
Credit used to purchase durables (% of households)	**Main source of credit**				
	Commercial bank - CB				
	Private supplier - PS				
• Car/Bakkie		3.3	CB	9.9	PS
• Generator		1.3	-	2.6	-
• Refrigerator		4.0	CB	32.9	PS
• Television		2.0	-	19.7	-
Savings facilities used (% of households)	**Distance to institution (km)**				
• Banks		30.0	60.7	48.7	45.0
• Money keeper		0.0	0.0	3.9	21.0
• Informal		80.7	0.0	29.6	19.0
Farm inputs financed on credit (% of households)					
• Fertilisers		7.3		9.0	
• Seed		6.0		5.0	
• Farm equipment hired		2.7		0.0	
• Chemicals		0.7		6.0	
• Veterinary medicines		0.7		0.0	
• Livestock feed		0.0		0.0	
• Ploughing services		0.0		9.0	
• Transportation services		8.0		10.0	
Credit source used to finance farm inputs and implements (% of h/h)					
• Local money lender		0.7		0.7	
• Friend or relative		4.7		3.3	
• Development corporation		10.0		0.0	
• Miller		0.0		0.0	
• Stokvel		0.0		0.0	
• Savings club		0.0		0.0	
• Input supplier		0.0		2.6	
• Commercial bank		0.0		0.0	

Source: Adapted from Ouattara and Graham, 1997

Table 7: Illustrative profile of small business househol ds based on recent surveys in two provinces		
	Northern Province (N=270)	KwaZulu-Natal Province (N=225)
Average age	26	46
Female (%)	21.6	22.9
Women who can sign contract without husband's permission (%)	33.0	70.7
Number of years in operation	8.3	10.0
Number of workers at start	3.2	4.5
Average value of business at start (R)	5 612	4 509
Number of current employees	3.5	4.6
Sector of operation (%)		
• Construction	37.8	35.5
• Manufacturing	26.3	26.7
• Services	35.6	37.8
Multiple sources of financing business at start (%)		
• Personal savings	93.3	73.3
• Retrenchment package	29.6	12.0
• Pension	17.4	0.9
• Loan from family or friends	10.0	4.9
• Loan from development corporation	5.9	6.2
• Income from other business	4.1	13.3
Sole ownership (%)	87.4	93.8
Registered business (%)	33.0	22.7
Place of work (%)		
• Home	37.0	34.7
• Adjacent to home	7.4	5.3
• Market	50.4	33.3
• Place of delivery of service	5.2	26.7
Selected income, input and output indicators (R)		
• Average wages received per month	1326	1 102
• Average remittances received per month	739	1 360
• Average pensions per month	414	438
• Average business income for business 1 per month	3 601	2057
• Average business income for business 2 per month	3 796	1 979
• Average business income for business 3 per month	7 721	2 800
• Average annual agricultural income	1 250	10 886
• Average value of physical assets on hand	17 913	12 995
• Average value of inputs per annum	1 067	12 703
• Average value of output per annum	92 031	58 044
• Average labour expenditure per annum	25 360	41 380
Use of loans (%)		
• Asset finance: Cash loans	10.0	10.0
• Asset finance: Hire Purchase	14.0	16.0
• Supplier credit	7.0	11.0
• Customer advance	16.0	29.0
• Customer loans	18.0	16.0
• Shopkeeper loans	56.0	-
Savings (%)		
• Formal : Mostly commercial banks	92.0	77.0
• Informal: Stokvel	26.0	76.0
• Informal: Burial society	64.0	22.0
Electronic banking	35.0	18.0
Handling of shocks or misfortunes (%)	21.0	52.0
• Main principle cause: Stolen equipment (% of shocks)	52.0	31.0
• Main fallback mechanism: Personal savings (% of shocks)	67.0	24.0

2.7.4 Conclusion

The present usage of banking and financial services by MSEs (including small farmers) is very small, with a minute section of the market presently being reached, estimated at less than 1 %. This is the most unbanked area of microfinance, and an area that is still in the introductory phase in the microlending industry. No study exists which provides a comprehensive overview and analysis of overall supply to the lower income and MSE market. Existing studies provide an overview of the institutions active in this market, but do not quantify supply in terms of clients reached. This study necessitates an overview of outreach, and therefore an indicative (rather than exhaustive) summary is provided based on an analysis of institutions active n the microfinance market.

South Africa has a vibrant microfinance sector that reflected immense growth over the last decade. It is however focusing on the wage and salary earners and comes mostly targeted as consumer credit. The sector's growth was phenomenal and the current size of the sector on the basis of current portfolio is estimated as R13 billion and the value of loans written per year is estimated at R25.8 billion. The majority of financial transactions however take place in urban areas.

Rural finance in South Africa received comprehensive attention at the policy level through the activities and reports of the Strauss Commission. Many of the recommendations have been implemented, but as we face reality, implementation is slow. The perception exists that, barring the activities of the Land Bank and the village banks, rural financial service offerings are decreasing. This is especially true of formal private sector services to rural people. Rural people make the most use of savings facilities and they save mostly at commercial banks. Even their informal savings activities eventually lands at commercial bank deposit accounts. Commercial bank branches are getting scarcer in rural areas. This increase the transaction costs of rural depositors and indeed contributes to less a less efficient financial market.

If we judge access to financial services on the basis of the presence of outlets of financial institutions in rural areas it is approximately 35 per cent of total outlets. This is much less than the total proportion of people living in rural areas in South Africa, however it is a fair reflection (even an over statement) of the proportional distribution of economic activity. Further, the outlets estimated in rural areas are skewly distributed, as most of the private sector outlets would be focused on larger towns and smaller cities in rural areas where a higher incidence of wage or salary earners prevail. This leaves a limited supply of financial services (judged on presence of outlets) in the rest of the rural areas.

With the withdrawal of the conventional formal private sector institutions from rural areas on the one hand, and an emphasis on wage and salary earners by the "new" formal private sector financiers it is not expected that financial service provision to rural people will improve. This is especially true for the self-employed rural entrepreneur and the unemployed in rural areas. The fact remains, if rural people do not turn to self-help organisations, no real volume of financial services will be forthcoming in rural areas. This emphasis on self-help schemes is evident from the rich fabric of informal financial groups in rural areas. These groups or collective action endeavours come in many guises and take place in many different locations. It ranges from the joint financial endeavours of the employed, to the joint efforts of the unemployed and destitute.

3. Rural livelihoods in South Africa

3.1 Defining rural areas and livelihoods

Rural areas have been very difficult to clearly define in South Africa due to the prevalence of various settlement regimes (homelands, etc) that were created as a result of previous government's policies. In some literature the term 'rural' has been vaguely defined as non-urban areas. Reference has also been made of rural areas as non-urban parts of the country that are not well served by physical and social infrastructure. According to the Strauss Commission report (1996a), available data does not allow a more accurate definition of the rural population in South Africa. This situation may be altered by a recent rural survey in South Africa by Statistics South Africa.

The main features of the rural areas are reflected in the Strauss Commission report (1996) as being that rural households are vulnerable to poverty risk and that there is a certain degree of migratory tendencies. It draws on both national data as well as case studies of rural localities, confirming that rural people of South Africa are at a significant risk of being poor. This risk is not only higher in rural areas than elsewhere, but almost three-quarters of the poor in South Africa live in rural areas. The risk of being in poverty in rural areas is also larger amongst women than amongst men.

There is a marked tendency by rural folks to migrate from one locality to another (not necessarily to urban areas). Migration means that one or more family members leave the resident household for varying periods of time, and in so doing are able to make new and different contributions to its well being (although such contributions are not guaranteed by the mere fact of migration) (Ellis, 1998). Most evidence points to the desire to diversify sources of income by the family as a major motive for migration. Intra-rural inequality, with economic surplus among the rural rich and labor displacement among the rural poor, is a powerful influence of migration. Much migration remains rural-to-rural. Selective migration by young rural men has caused large, but irregular remittances of savings and serious inequalities among the remaining, often aging rural, rural poor (Strauss Commission, 1996a).

The term livelihood has been used differently by different authors. With synonyms of the word being living, subsistence, sustenance, maintenance, support, keep, etc, it denotes the means needed to provide the necessities of life. According to a DFID (1998) report on sustainable rural livelihoods, a livelihood comprises the capabilities, assets (including both material and social resources) and activities required for a means of living. In the text 'Land, Labor and Livelihoods in Rural South Africa', by Lipton, Ellis and Lipton (1996) the term livelihoods is used in the place of jobs, because most farmers and farm workers work in agriculture only seasonally and often part-time. They elaborate this further by stating that, individuals and households create a living from various sources: farming, rural non-farm work and seasonal migration to work away from their homes. A livelihood is thus summarily defined as the number of days in a year sufficient to produce enough income to keep a worker (plus dependents) out of poverty, which in the particular text is pegged at 200 days per year.

In reviewing the livelihoods of small-scale farmers in South Africa it is therefore essential that there be focus on the farmers capabilities, their assets and the general activities that they engage in.

3.2 KwaZulu Natal Case study

May (1998) analyses the patterns of livelihoods that characterize rural households in KwaZulu Natal. He uses survey data collected in the 1990s to examine living standards and incidence of poverty in South Africa.

May differentiates households according to their resources and assets (access to physical and human capital), the activities from which they derive incomes, and the outcomes in terms of household and per capita incomes. In his work households are distinguished according to the dominant sources of income within their diversified livelihood packages. These include urban remittances, formal sector employment, and also encompass a wide range of other supplementary sources. The emphasis is that people in rural areas engage in a wide range of activities in order to generate a livelihood. Davies (1996) (in May, 1998), notes that the diversification of income sources is a key factor influencing the well being of households in rural areas. According to him, through diversification households are able to buffer against risk in agrarian environments. By engaging in diversified activities, households may be seen as trying different options, which they hope, will generate an adequate and sustainable livelihood that is resilient to shock. This constitutes what can be called a livelihood strategy, and is an outcome of decisions and conflict over use of the household's resources.

In trying to understand what influences households to choose particular livelihood strategies there is need to have an understanding of the environment in which the households live. KwaZulu-Natal is the province with the largest population in South Africa, estimated at 9.8 million in 1995 living in 1.6 million households. This population grew at about 2.3% per annum then, and was expected to reach 12.9 million by 2010. In 1995, 52% of the population were considered functionally urbanized, one third of which were living in informal settlements. Urbanization is expected to increase to over 60% by 2020. The size of the provincial population, however, will not continue to increase due to the influence of the AIDS pandemic. KwaZuluNatal's population growth rate declined to nearly 1% due to deaths caused by AIDS. This will have a major influence on the ability of rural people to ensure viable livelihood strategies and also need to be considered in any strategy put forward.

As stated earlier, assets are a very important aspect when analyzing the livelihood of a particular group of people. The assets available to rural people in KwaZulu-Natal include land, labor, human capital, agricultural capital, entitlements to pensions, and entitlements to intra-households transfers (May, 1996). Just over half of African rural households in KwaZulu-Natal (53%) have access to land for the cultivation of crops, which is more than twice the incidence of land holding by rural African people in the rest of South Africa. However land holdings vary by region within the province (Muller *et al*, 1987 in May, 1996). Studies carried out by the Southern African Labor and Development Research Unit (SALDRU) in South Africa in 1993 on incomes and expenditures reveal that average land size for households' access to land is similar in

KwaZulu-Natal to the national average, at two hectares per family. However, average land size per adult equivalent is smaller in KwaZulu-Natal, at half a hectare compared to with 0.8 hectares in the rest of South Africa. This reflects the population densities in rural KwaZulu-Natal, and is consistent with the smaller farm sizes found in the commercial sector (May & Amin, 1995). Livestock also represents a significant resource for the people of KwaZulu-Natal. Livestock ownership is highest in this province than in any other in the country with about 31% of the households owning a herd (May, 1996).

The SALDRU survey identified five main activities by which rural households in South Africa generate incomes. These include agriculture, non-farm self-employment, wage labor, claims against the state (old age pensions and disability grants) and claims against household and community members.

Quattara & Graham (1996) documentedic conditions and access to financial services among selected homeland farming communities in KwaZulu-Natal & the Northern province in South Africa.

Household surveys in the districts of Port Durnford and Hlabisa in KwaZulu-Natal revealed that people in these areas are relatively poor, and most are not significantly engaged in agricultural activities for commercial purposes. For households with a farming tradition, access to formal agricultural extension services was shown to be very limited (Quattara & Graham, 1996). Other important issues that the study dug out are that:

- Access to financial services by households was limited despite the fact that commercial banks were being used extensively in the area. So people were basically depositors, but banks were offering almost non-existent credit in return.
- Moneylenders, friends, and relatives formed the bulk of limited source of financing for the household.
- Only a very small amount of credit was associated with agricultural production activity with the bulk of it used to purchase consumer durables (television sets, refrigerators, etc) as well as food, clothing, education and medical services.
- Major source of income was outside wage employment.
- Wealthier people had higher chances of accessing loans.

KwaZulu-Natal alone cannot be used as a proxy of what the rural livelihood situation in South Africa is like, because the province seems to have a significant advantage in terms of access to agricultural and productive equipment compared to the rest of rural areas in the country.

3.3 Northern Province case study

Baber (1996), in his paper 'Current livelihoods in Semi-arid rural areas of South Africa', compares the patterns of livelihood in two Northern Province communities Mamone and Rantlekane. According to him the communities differ in respect to size, remoteness from employment centers, tenure system, landlessness, the origin of the community, and the length of time in which the households have been settled in the area. One community relies heavily in agriculture whilst the other is typical of many of the Northern province settlements in its meager agricultural resources and greater dependence on the outside economy. The author further stresses that the contrasting pattern of rural livelihoods that emerges in these two settlements helps to illustrate the nature of the rural economy, and can be used in assessing the livelihoods in the semi-arid regions of South Africa.

Data analysis results showed that remittances provided two thirds of total household income in Mamone, whilst 93% of households in Rantlekane count remittances as one of their income sources. Most of the remittances are from migrant workers. The greater role of remittances in Rantlekane is congruent with its higher migration ratio and a result of its weak local economy (Baber, 1996). Seventy four percent of the households in Mamone have agriculture as one of their sources of income, compared to 34 % in Rantlekane. The rest of the activities' contributions to the households are almost similar. The difference between the two settlements ability to provide locally based livelihoods is shown by the greater contribution made in Mamone by informal economic activities, informal employment, local businesses and in particular agriculture. In Mamone just less than half of total resident income at the community level is generated in the local economy, and roughly a quarter of this is in the form of agriculture. In Rantlekane, by contrast, only 30% of total resident income at the community level comes from local economic activity, and agriculture forms only one or two percent of this. The poor state of cropping in Rantlekane relates to landlessness, monoculture (reliance on maize only), the more arid climate and the tenure system (Baber, 1996).

According to the author, this hampers backward linkages with other activities, such as ploughing and transport businesses. Also interesting is the fact that in both communities pension income forms a significant proportion of total income, and plays an essential role in lifting some households out of the worst extremes of poverty. There is a tendency by the pensioners to distribute their pension even to those households other than which they live especially female-headed households, thus benefiting those households without remittance income.

A study was also done on the former Lebowa homeland, now part of the Northern Province. The revelations were that people were relatively poor, not well educated, and with limited access to public services. The majority of households were headed by a de facto female head, and at least one member of the household was either a full time farmer, or self employed. Just like the studies carried out in some districts of KwaZulu-Natal, household access to financial services and to loans in particular was shown to be limited, although savings were also held in commercial banks (Quattara & Graham, 1996).

Although caution must be exercised when projecting up to regional or national level from the results of handful of micro studies, they undoubtedly are good proxies of the reality of the livelihood situation in rural areas. Of notable significance is the fact that agriculture seems to be playing a limited role in the northern parts of the country. It is probably in this light that households there also have diversified sources of livelihood. It is therefore critical to policymakers that when they make available opportunities that overcome transaction costs faced by such communities like credit markets, they not only fund agriculture but other money generating enterprises as well.

3.4 Western Cape case study

In the Western Cape, Cousins et al (1996) carried out a study on rural livelihoods and small-scale agriculture. Theirs was an evaluation of developmental projects that had been in place in the province since the early 1980s. These projects were aimed at making land and support services available to would-be small scale farmers from the local colored community, who had been denied meaningful opportunities to engage in agricultural production other than as farm workers. The projects were community gardens and a farm whereby part time and full time small holders engaged in various enterprises.

The program had two community gardens, consisting of 10m x 15m allotment plots for about 40 members and used mainly for vegetable production, and whilst the farm was 136 ha in extent with six to eight small holders producing a mix of fruit and vegetables under irrigation on holdings ranging from 0.75 to 2 ha each, together with both intensive and extensive small livestock (Cousins, Cousins & Theron, 1996).

After enjoying a period of bliss, the project started experiencing problems, some of which are still being faced to date. Studies carried out by Cousins, Cousins & Theron (1996), give a detailed description of the exact nature of the problem as they followed the program from inception through the various phases that it went through. It is in this regard that they came up with lessons that ought to be considered when similar ventures are proposed.

Some of the recommendations that the authors came out with for future work on enhancing rural livelihoods are:

- They found out that members of the projects demonstrated that aspirant small scale farmers in the region possessed considerable agricultural knowledge and skills as a result of previous involvement in the commercial farming sector, mostly as laborers. This according to them confirmed de Klerk's (1995) assertion that "commercial farm employees were probably the largest pool of potential small scale farmers in the Western Cape", but also suggested that ex-farm laborers should be included the pool.
- Risk management strategies of small farmers must be taken into account when designing programs to promote agriculture as a source of livelihoods, and are likely to influence farmers' responses to institutional arrangements and financial, technical and other services. This is particularly the case when capital intensive enterprises with long lead times, such as fresh fruit growing, are established.
- Diversification came out to be an important risk management strategy.
- Adequate levels of financial support are a prerequisite for farming enterprises, and particularly so for capital intensive forms of productions such as fresh fruit.
- Support services providing appropriate technical advice, management support and possibly machinery and equipment hire services, are vitally important, particularly in the early stages of small farmer development programs (Cousins, Cousins & Theron, 1996)

Considering the fact that the evaluation process revealed that the above project was at crossroads with its future uncertain, the above recommendations ought to be taken seriously by policy makers whenever they are designing probable projects aimed at enhancing rural livelihoods.

It is clear that in rural areas of South Africa, as shown by Northern and KwaZulu-Natal provincial studies referred to above, farming on its own rarely provides a sufficient means of survival. What is apparent is that rural households depend on a diverse portfolio of activities and income sources, among which crop and livestock production feature alongside many other contributions to family well-being.

The five case studies mentioned here, although regional, reflect to a certain extent the means of livelihoods in rural areas in South Africa. It is clear that some provinces are better endowed than others with respect to resources, thus giving the rural folks more choices from which to generate their livelihoods. In a nutshell, people living in rural areas of South Africa use every means possible to generate incomes and thus diversification of income sources seems to be the prevalent way of making ends meet.

4. Rural livelihoods and finance

Having looked at the pattern of rural livelihoods in South Africa, we now integrate it with small scale financing of enterprises, so as to be clearer on the need for financial services in rural areas. The characteristics of rural areas, which make them unfriendly to business, become a central issue here.

4.1 Obstacles to rural finance

Coetzee et al (1994) highlight some of the constraints that ought to be alleviated for the rural finance markets to work. These constraints are imperfect information, collateral requirements, lack of infrastructure, spatial distribution and covariant risk. According to them, imperfect information is the main reason formal financial intermediaries do not operate in rural areas. A lack of information increases risk, and therefore the transaction cost to the lender. Financial intermediaries manage their risk according to the information they have available. Adverse selection can be made because of inadequate information about borrowers and the lenders therefore need to add a risk premium to the interest rate charged. Stiglitz and Weiss (1981) argues that this can lead to lower risk borrowers being discouraged from borrowing and increased adverse selection since lenders know that sourcing higher interest from good borrowers can result in adverse selection so they opt for credit rationing.

This is applicable to all rural areas of South Africa where lenders often have minimal information of the repayment capacities of entrepreneurs, and rather than go the adverse selection route they prefer to ration credit. This has implications on the reduction in welfare and potential losses in probable livelihoods that would have been generated if informational setbacks were to be taken care of.

Another significant characteristic of rural areas is the limited availability of collateral that can be pledged. Rural areas often lack assets or a track record to substantiate their loan application. Commercial lenders, whose mandate is to get a reasonable return on investment on bankers funds, tend to shy away from these people as they realize that in cases of default they have nothing from that borrower that they can sell to recover their money.

Complementary infrastructure also influences the performance of financial markets in rural areas. This refers specifically to the availability of other supportive markets, such as an insurance market, and technology to facilitate the flow of information. Poor road networks and telecommunication facilities exacerbate the problem.

Settlement patterns that are prevalent in most rural areas make the delivery of financial services costly. The usually dispersed and haphazard nature of the settlements increases the unit cost of delivering financial services to both the lender and the borrower.

An equally crippling feature of rural areas is the prevalence of covariant risk, which is basically that individuals in rural areas tend to experience correlated shocks to their incomes. These include weather variations and changes in commodity prices affecting groups of farmers. Covariant risk has great implications for lenders and is of great concern to them since it implies that a whole group of farmers would be unable to pay at the same time.

All these constraints have an effect of increasing the transaction costs of delivering financial services to rural areas. In the end the rural population is left with little or no access to services that would otherwise have complemented their means of livelihood and probably led to increased welfare.

In South Africa there is a definite need to travel an extra mile if there is to be an effective delivery of financial services leading to sustainable financial markets in rural areas. Minority governments of the past had deliberate policies that favored particular population groups at the expense of others. The reality of the situation is that people who were worst affected by the discriminatory policies are those who reside in rural areas. This therefore adds on to the already burdensome characteristics of rural areas already mentioned above.

Large numbers of rural entrepreneurs and households in South Africa experience limited access to financial services. Past political and economic interference resulted in disempowered rural communities. Apartheid policies prevented black people from building up an asset base through land and property ownership. It prevented blacks from owning businesses in white areas, and from settling where they chose. Thus millions of South Africans where not able to meet the set of conventional conditions required by formal financial intermediaries such as commercial banks, to provide finance in this market. These political and economic interventions led to increased market failure in other words government failure led to market failure. The market itself cannot rectify these inefficiencies without an optimum allocation of resources. For the market to intermediate efficiently certain constraints must be must be alleviated (Coetzee et al 1994).

One of the more disturbing characteristics of the South African economy is the presence of untapped human resources and underused natural and physical resources in the face of abject poverty. This contradiction is most visible in South Africa's rural areas. In part they are overcrowded and unproductive; in part capable of producing agricultural surpluses, yet, overall, incapable of sustaining adequate rural livelihoods. The rural areas represent an opportunity for releasing South Africa's creativity. The provision of financial services in these areas could be one of the more important mechanisms in a rural development strategy for unlocking this potential (Strauss Commission, 1996a). The bone of contention would therefore be how financial services can be extended to rural areas effectively to achieve the greatest possible outreach.

4.2 Demand for credit in rural areas

Despite all the major setbacks mentioned above that seem to be facing the country, there has been use of financial services by the rural population. The Strauss Commission report (1996a) is again handy with this kind of information. When the characteristics of debt were aggregated for rural and urban households, the following came out:

- Rural households have had disproportionately few loans. Rural households owed 43% of all debt outstanding, even though 50% of the households were classified as such. 57% of rural households are without debt compared with 45% of urban households.
- Rural households have disproportionately small debts. The average loan of a rural household was R4 249, and compared to R32 299 for urban households. Although rural households controlled 25% of household expenditure in South Africa and represented 43% of the number of households, they owed only 9% of the outstanding debt.
- Many rural households use hire purchase agreements and loans from shopkeepers. Hire purchase agreements or debt with shopkeepers accounted for 73% of the number of loans incurred by rural households and for 22% of the amount of debt, compared to 39% and 4% respectively for urban households. The amount of debt owed by rural areas to these sources is roughly half that owed by urban households to the same sources. Thus while large numbers of rural households have hire purchase agreements and loans from shopkeepers, the amount of such debt is disproportionately small.
- Informal lenders are important sources of credit in rural areas. About 22% of the rural households with debt have their largest obligations to informal lenders. (Strauss Commission, 1996a).

4.3 Government effort

The South African government has also been making headways in a bid to assist rural populations' move out of the poverty trap that they have been embroiled in for years. This commitment has been shown by some of the initiatives that it has taken to try and make up for the lost decades. One of such initiatives is the Reconstruction and Development Program launched by the majority government in 1994.

The South African government in its Reconstruction and Development Program (RDP) white paper of 1994 put across the strategies that it laid for the future of the country which were aimed at addressing some of the issues the Strauss Commission report refers to above. The program sought to mobilize all the people and the country's resources toward the eradication of the results of apartheid and the building of a democratic, non-racial and non-sexist future. With reference to the rural population, the program sought to formulate an integrated and sustainable rural development policy in consultation with rural people, their organizations and various stakeholders. In particular, attention was to be given to the broadening of access to services and support to small-scale agricultural producers by ensuring access to land, appropriate markets, credit facilities, training and support (RDP White Paper, 1994).

To achieve sustainable rural livelihoods where it is shown that there is need for financial injection, it is paramount that rural communities be part of the process from the outset. In the past there has been a tendency by donors (governments included) and other would be financiers of projects globally, to treat the rural folks as beneficiaries in what has been termed directed credit schemes. Huge sums of money were just channeled into projects mainly because there was a felt need to make sure there is fairness in the allocation of resources and also to address market failure related concerns. Proponents of the directed credit schemes ignored voluntary deposit mobilization as they had a strong feeling that this could lead to funds flowing out of rural areas. Also external sources of funding are perceived to be less costly than deposit mobilization (Vogel & Adams, 1997). This way of thinking is being revisited, as there are many problems that are starting to surface because of it.

4.4 The way forward

The micro-finance sector has learnt a lot through decades of continuous funding but little development in rural areas of the world. The sector, globally, now seems to be moving into a scenario whereby the rural folks are now taking a more participatory role leading to a paradigm shift. People, at whom projects are directed, previously referred to as beneficiaries are now being looked at as clients. There has now been a switch in paradigms to one, which embraces financial markets. The financial markets paradigm stresses transaction costs as the dominant problem in financial markets. This includes costs incurred by both providers and users of financial services. These costs are particularly large in rural areas, in the provision of micro-financial services and are seen as the primary factors constraining the expansion of formal finance. Proponents for this paradigm also argue that a combination of interest rates and the transaction costs imposed on users of financial services, not interest rates alone, determine the demand for financial services (Vogel & Adams, 1997).

One critical aspect that is advocated for by the financial markets mechanism is that it stresses voluntary deposit mobilization. Unlike in directed credit schemes where money was siphoned from outsiders, the dominant circulation of money in financial markets paradigm is horizontal. Institutions involved mobilize from depositors the vast amounts of money that they lend. This is a very interesting and seemingly practical means of creating strong relationships between the financial institutions and the borrowers. Only this way can funds be continuously available when borrowers need them. Rural people gain more from such arrangements leading to upliftment of rural living standards.

If such an approach could be encouraged in developing countries, the donor syndrome that has been said to be characteristic of people from this part of the world could be a thing of the past, and we could be envisaging greater participation in self development by rural communities.

5. HIV/AIDS and livelihoods

5.1 Introduction

When reviewing rural livelihoods in South Africa it is critical also to look at the various possible opportunities and threats that the human population is faced with. One such threat that is currently a national menace is the HIV/AIDS pandemic. HIV/AIDS is a big threat as it undermines all the efforts that government and the rest of the population could be working towards to uplift the standard of living of the South African people. When planning developmental projects it is therefore important for policy makers and all relevant stakeholders to realise the extent of the disease, its possible consequences, and how it can be minimized. This is crucial as it enables the planners to factor it in their plans, so as to come up with programs that really benefit the existing population. This section thus summarizes its demographic, economic and social implication nationally as there are few studies that are rural area specific.

5.2 History of HIV/AIDS in South Africa

The first two cases in South Africa were diagnosed in 1982 with the first recorded death occurring in 1985. There were undoubtedly others before that went unnoticed. It is possible that the disease might have already been there, dating back to the 1970s. By the end of 1990 the heterosexual pattern was fast becoming the dominant means of transmission. By February 1993, all but two of the 46 cases diagnosed as AIDS from 1982 to 1986 had died. At the end of 1995, some 9000 cases had been reported of whom some 8000 were still alive. However, estimates from component projection models suggest that barely more than 5% of all cases were reported and only slightly more than 1% of AIDS deaths were recorded. It was estimated that over 1.8million people were infected with HIV at that time. Women were more vulnerable to infection with 73% of all the reported cases in 1996 being female (Department of Social Welfare, 2000).

In 1996, the Department of Health estimated that up to 3% of the total population and 7.5% of the sexually active population had been infected by HIV. By the end of 1996, approximately 700 people were becoming infected each day with the rate of new infections doubling every fifteen months. By 1998, these projections had become too modest, the estimated figure now stands at 3.6 million. It is estimated that by 2009, South Africa will reach of figure of six million deaths from AIDS.

5.3 Demographic implications of HIV/AIDS

The impact of HIV/AIDS on the population structure is both dynamic and dramatic. There will be decline in the number of people in specific age groups, namely 0-4 year-olds and 25-34 year olds. Since HIV is primarily spread through sexual transmission, the majority of people will be infected during periods of peak sexual activity in their late teens and early twenties and will fall ill and die in their late twenties and early thirties. The concentration of HIV/AIDS in these age groups has important consequences. Over time, the reproductive age groups will move up the population pyramid and so, with increased mortality and deferred births, the structure of the population pyramid will visibly change. Significant gashes will be on the female side of the pyramid and the base will taper inwards due to lowered fertility.

Life expectancy for South Africa is definitely being affected by the prevailing AIDS pandemic. Life expectancy is particularly sensitive to AIDS because deaths occurring among young adults, young children and infants result in a large number of years of life lost. Those born with the virus can expect to live for an average of 2.5 years, those born free of the virus but contract it in their youth or early adulthood have a life expectancy of 25 years, and for those who never catch the virus are expected to live into their late sixties.

5.4 Social implications of HIV/AIDS

The social impact of HIV infections within households increases certain kinds of long-term expenditure. If infected persons are income earning, their illness and possible death will reduce the household's income. Special nutrition and medical treatment and the inevitable funeral costs constitute a major financial burden on the household budget. This leads to a further degradation in the household economic status, adversely affecting the living standard and quality of life of surviving members. We differentiate between the infected and the affected members of the household. The affected are the household members that will care for the infected. We argue that the impact of HIV/AIDS is mostly underestimated as only the loss and cost of care of the infected is considered. However, when one consider the loss of income (and possible decline in income) of the affected, and the decline in purchasing power thus impacting on the market, the effects of HIV/AIDs are obviously disastrous.

5.5 Policy implications on strengthening the household's coping capacity

Several policy options arise out of literature that can be taken to strengthen the capacity of rural households to cope with HIV/AIDS. The overall aim of these policies should be to improve both the short and long-term well being of the households in ways, which do not create dependency, and at the same time minimize the risk of members being infected with the virus. According to a 1999 UNAIDS report various policies are proposed to help fight the epidemic and make sure that the welfare of rural communities is uplifted. Part of these recommendations relevant to this work are improving agricultural production and promoting income generation and diversification of income sources.

- Improving agricultural production
  Since the majority of rural households dependent on agricultural production for their livelihood, strengthening the household's agricultural production capability is one way in which the impacts of AIDS can be mitigated. Agricultural production ability of the household can be reinforced by improving their access to labor, land, capital, draught power, and management skills, promoting use of existing labor, and capital saving technologies, and by developing technologies that can make use of the available limited resources.

- Income generation and diversification of income sources
  - Programmes, which help improve and diversify the sources of income of affected households, help mitigate the impacts of AIDS. Such programmes help maintain household expenditure patterns and thus help the household avoid further losses in welfare. According to Donahue (1998), quoted in the UNAIDS 1999 report, the first line of response should be to mitigate the impact of AIDS on households by improving their income earning capacities. The aim is to maintain household expenditure patterns and promote savings. This, according to the author can be achieved through micro-credit projects that are typically small, short-term and rapid turnover in nature.
  - Promoting income diversification can strengthen household's coping capacities. In risky agricultural climates, households with more diversified off-farm income are less vulnerable to food insecurity. Another strategy is to encourage crop diversification and promote a reduction in external input requirements.

5.7 Conclusion

This sub-section clearly highlights that great care has to be taken into consideration when planning rural development projects for South Africa. Assuming that rural areas are affected by the disease at the same rate as the rest of the country, this implies that in the long term the population structure will be such that there are a lot of young orphaned children being kept by their grandparents as their parents would have been swept away by the pandemic. So there would be a serious shortage of active labor in rural areas with a capacity to contribute to the welfare of particular households. This implies that whatever effort by developmental agencies to prop up agriculture for instance must be done on the background that there are labor shortages. There are a lot of implications from such an incidence. A typical result of such an occurrence could be an increased failure by rural households to payback the seasonal loans that they could be getting from various agencies, since their productivity levels would definitely be lowered by the AIDS scourge, due primarily to labor shortages.

A lot of other issues arise due to widespread AIDS related deaths and they have a huge effect on how rural life moves forward. For example some members of the family within which a member has passed away due to the disease might feel the need to migrate to other places and if this was to happen on a wider scale, it could jeopardize a lot of developmental projects already going on. Hence the need to look at the pandemic with great concern.

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