RETAIL RURAL FINANCE IN SOUTH AFRICA: FROM POLICIES TO PRACTICE

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In South Africa a recent government study laid the foundations for improving access to financial services for rural people. More is however needed than simply stating the policies. It is argued that policies do not differentiate target groups adequately. This can result in inefficient implementation of policies. The concept of a broad range of institutional possibilities to improve access to financial services, none of which specifically provides a conclusive model, is considered to be realistic. The idea is to muster this range of possible forms into a co-ordinated effort to increase access to financial services for rural people in all rural areas. This paper emphasises the reality of the situation when choosing policy directions. NGOs, commercial banks and the Post Bank do not hold the primary key to improving access to financial services in rural areas in South Africa. Several studies discussed the broad range of possible institutional forms in the rural areas of South Africa. The role of decentralised financial systems has not been the focus point of any of these studies. It is argued that fertile ground exists in South Africa for decentralised financial systems to address access problems at the local level. Decentralised systems also cannot be the solution to all intermediation problems. A multi-pronged approach is proposed, harnessing all institutional forms into a comprehensive strategy.

1. INTRODUCTION AND OUTLINE

Financial transactions between rural people and rural financial institutions are the most important point of interaction in the rural financial market. This is the interface between specialised credit institutions and their clients, between commercial banks and their clients and between moneylenders and their clients. At this point the conventional approach missed most of its target market and it is here where the biggest effort is needed to improve access to financial services for rural people. This paper is based on the assumption that financial services matter in the lives of rural people. Financial services can make a difference. It is acknowledged though that financial services alone cannot make this difference in South Africa as many development gaps and backlogs exist that have to be attended to. The Strauss Commission (1996a; 1996b) laid the foundation for the reform of the role of the state in rural financial markets in South Africa. The Commission recommendations impact

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more on the national level. At the retail level the Commission did not provide the detail of how to achieve increased access to rural financial services.

In this paper three essential points will be argued. Firstly, that the client (or prospective client) should be the point of departure for the efforts of an institution to provide financial services. Secondly, that none of the current policy options in South Africa present a single institutional solution to increasing access to financial services in rural areas. Thirdly, that decentralised systems have largely been ignored as a possible strategy in the mainly supply led South African scenario. The paper is structured along these three points and has a final section as a conclusion.

2. THE RURAL CLIENTS IN MORE DETAIL

Most policies refer to rural clients as an amorphous mass. It follows that policies that address the well being of clients defined in this manner do not differentiate between target groups. Ghate *et al* (1996) argue that it is important to structure approaches in such a way that you do not fall between two stools - failing to reach the poor of the poor, while failing at the same to provide the comprehensive package of services necessary for enterprise development (or entrepreneurial development). The latest version of a rural development policy in South Africa (Rural Development Framework, 1997) differentiates between rural women, children, farm workers, the disabled and small farmers as specific groups that warrant support. It is argued that this provides and inadequate basis for policy differentiation. The Strauss Commission (1996b) made a more comprehensive effort and identified, women farm workers, male farm workers, the landless, unemployed rural poor, pensioners, small holder farmers, contract farmers, rural business women, businessmen/ small scale employers and large scale rural employers (including commercial farmers).

The categorisation of sub-groups in rural areas by the Strauss Commission (1996b) emphasises the source of income or/and gender as the most important differentiating variables (in all the categories except the landless, unemployed rural poor). Each group would have a specific demand for types of financial services and this should be the departure point of estimating demand for financial services and what type of services to provide.

In the case of small farmers several surveys question the emphasis in South Africa on the small farmer as a definable target group (Coetzee, 1988; Outtara and Graham, 1996). Small farmers are normally identified for small farmer surveys in terms of agricultural activity in whatever form. Very little information is normally available about these "small farmers" before hand. Two recent surveys in the Northern Province and KwaZulu-Natal prove the point (Outtara & Graham, 1996; Baydas & Graham, 1996). These surveys in the two provinces were divided into small business and small farmer surveys. In Table 1 the income from farming for both small business and small farming survey results are presented.

Table 1: Selected results from harm household and small business surveys in two provinces

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:				
• Formal institution (distance km)[a]	29.0 (60.7)	29.7 (45)	92.0	77.0
• Informal institution (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.

It is clear from the survey results that farming plays a small role in terms of income, although a major proportion of small farming households (and small business households) cultivate the land and produce crops. Thus very small proportions 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. The majority of the people surveyed made use of savings facilities rather than credit. 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. This statement on the demand for credit should be questioned as no survey or study in South Africa has attempted to assess demand for financial services. 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 credit from formal private sector sources. 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 a distance from these clients.

3. THE STATE OF RETAIL FINANCE IN SOUTH AFRICA'S RURAL AREAS

The first question that needs to be answered revolves around the current coverage of rural areas by financial institutions. Table 2 serves as a summary of the current information available. This is not an exhaustive overview. It relates coverage (outreach) with the high cost of intermediation found in South Africa (Strauss Commission, 1996a). More in depth discussions are provided in this section on institutions seen as potential *en masse* retailers in rural areas due to their physical presence.

Table 2 indicates a vast outreach at first glance. If these institutions and their clients are studied more carefully the following observations can be made:

- More rural clients have access to savings and transmission facilities than to credit facilities. However the transaction cost per client to use these facilities are quite high as indicated in Table 1.

- Rural small entrepreneurs have only limited access to formal loan facilities.

- The majority of the services indicated by the presence of providers in rural areas are offered in the larger towns in rural areas. Rural dwellers therefore have to travel distances and incur a range of costs to access these services.

The cursory analysis underlying Table 2 needs to be more focused. Therefore research is needed to provide more detail on demand and supply of financial services, the spatial location of services and the client strata targeted by.

Table 2: Summary of formal retail institutions and exposure to rural areas (and the agricultural sector) in South Africa (estimates dated between 1995 and 1997)

Retail institutions	Amount (Rmillion)		Number of branches and agencies	Rural coverage* in % of		Coverage in terms of clients reached /contracts	
	Loans outstanding	Savings mobilised		branches	clients	Loans	Savings
Land Bank	5 799	84	25	90+	90+	30000	?
Agric. Credit Board	1 331?	-	1	-	90+?	14000?	-
Provincial parastatals	196	458	70	50+	70+	35 000	720 000
Post Office Outlets	-	1 100	2365	?	60+	-	2 400 000
NGOs	8	?	17	?	35	10 240	?
Village banks	-	1	3+	100	100	-	871+
Co-operatives	4 404	?	1200	80+	60+	100 000+	?
Commercial Banks	7 909+	?	4055	33	?	?	?
Retail stores	1 500+	-	?	?	?	?	?
TEBA Cash	-	?	172	40	?	?	?
FAF	24	45	20	100	100	17 000	33 000
Private (to agric.)	3 164+	?	-	-	?	?	?
Small loans industry	10 100	-	20 500	20?	20?	6 150 000?	-
Informal sector	?	?	?	?	?	?	?

Adapted from Coetzee, 1997 and Du Plessis, 1997.
* Broad definition of rural areas as non-metropolitan areas.
? data unavailable or need further explanation or qualification.
+ means that the author is convinced that this figure represents an under estimate

different services. However, even though this analysis is in broad-brush strokes a problem exists with respect to access to a range of financial services

The analysis of the supply of retail funds and the reality of the South African situation leave a dismal picture regarding the prospects for increased access to rural financial services. Current endeavours seem to be inadequate. The market is not playing its role as we do not see formal commercial bank activities covering all the rural areas and it seems as if the trends are against rural areas. These trends are evident when comparing South African Commercial Banks to its overseas counterparts. Commercial Bank branches will only be justified on the net economic demography of the service area of a branch (Deloitte & Touch, 1995). State supported institutions, whether they are instruments of the state or of civil society, does not seem to hold the answers to increasing access to financial services for poor people. The same applies for NGOs. None of the NGOs analysed by the Strauss Commission (1996a) illustrated the ability and potential to achieve self-sustainability over the medium to long term. Further, their outreach performance does not justify the subsidy element in the NGOs analysed (see Reinke, 1997). Successful private sector smaller financial retailers tend to concentrate on the urban areas. It follows that not one of the actors discussed holds the institutional recipe for *en masse* increasing of access to financial services in rural areas.

4. PUTTING RURAL PEOPLE IN CHARGE

It is argued that one area of complete neglect in the formal conception of the supply of financial services is the concept of decentralised financial services. The decentralised concept refers to village level financial services that are organised by the local community. This is the essence and origin of financial intermediation. It emphases a savings first approach. Slow growth and social capital are implied in starting and organising such a system. It further implies local control, or member control over the activities of these institutions. Member control also includes mutual monitoring of activities by members. Activities refer not only to the handling of cash, but also to the management of investments by borrowers. In essence these systems address the core of all issues in financial transactions and markets; it improves information flows, thus improving the quality of decisions. It decreases adverse selection and moral hazard problems (Graham & Von Pischke, 1995).

Few examples exist in the formal literature about these endeavours. They are however varied in examples that range from the traditional stokvel (rotating savings and credit associations) to credit unions and savings and credit co-operative ventures. One example in South Africa is the village banks (Jazayeri, 1995 and Schoeman, 1996) of the Northwest province. Village banks are organised and owned by members. Their objectives are to provide appropriate financial services at the village level, and to link this service with the commercial banking sector. This is a savings first approach that includes credit services only when the volume of savings allows it. It is further operated on the basis that the savings of each member come in two forms, shares and normal savings. During the period in which loans are not provided the only source of capital is the savings and depositing these savings at the nearest commercial bank branch generates income.

The Motswedi Village Bank in the NorthWest Province started in January 1996 and has accumulated deposits in excess of R200 000 from 200 members (Coetzee, 1997). It is 75 metres from a Post Office branch that provides saving facilities. It is 35 kilometres (that is equal to R15 for a round trip by taxi and R10 per bus) from the nearest commercial bank branch. This village bank is situated in an area where a large proportion of the people recently lost their savings in a pyramid scheme. Against a range of odds it is succeeding. Its members cover all the economic sectors in the area, including farming (Coetzee, 1997). Unfortunately information could not be obtained with respect to the proportional savings in the bank according to member type. It is expected that the pensioners would have quite an influence on the bank due to their consistent access to cash funds. Since the start of the three functioning village banks in the North West Province rapid growth in membership has been experienced. Figure 1 indicates growth in membership since the inception of the first village bank.

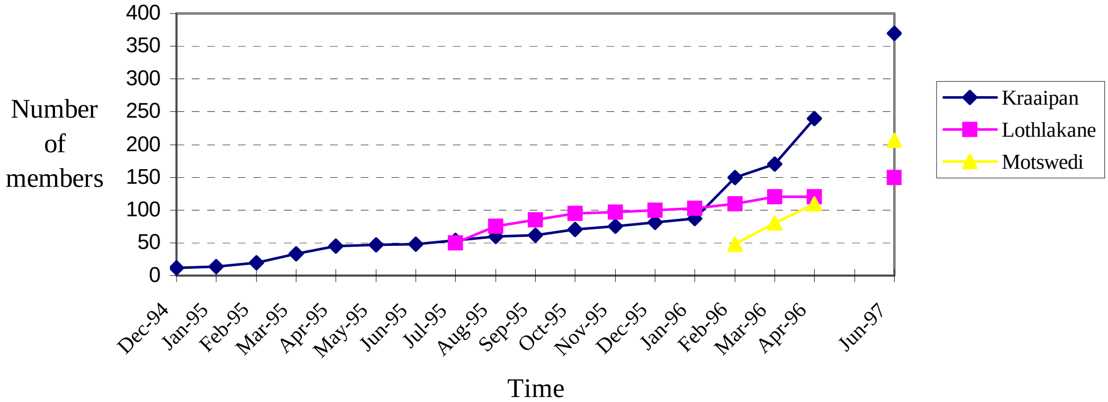

Figure 1: Growth in membership at the three village banks in North-West Province (Schoeman, 1996; Coetzee, 1997 and Vink *et al*, 1997

None of the village banks have yet decided to start extending loans. They do charge service fees for each transaction. Staff members who earn a basic salary and receive increases in relation to the growth in membership administrate them. A strong incentive therefore exists for a staff member to market the concept of the village bank. These banks deposit their savings with commercial banks in the area. The purpose of this short discussion is to illustrate that the concept has application value within South African circumstances.

Spio (1995) illustrated the relatively high propensities to save of people in the rural areas of South Africa and his work confirmed the earlier findings by other researchers (Coetzee, 1988 and Fenyes, 1982). The high savings propensity illustrates the potential for village bank approaches. The historic prototype, the stokvel, mobilises R83 million per month in the urban areas of South Africa (Markinor, 1993). The existence of these informal approaches and high propensities to save provide a fertile area for savings based decentralised approaches.

Cross (1997) shows how families cope when being turned away from commercial banks, how credit works to secure building loans without an employer guarantee, how households take part in savings and loan clubs and the risks they run when dealing with money lenders. The combination of these stories depicts an opportunity for intermediation between surplus households and deficit households in the form of a co-operative financial venture. The issue at stake is the facilitation needed to move from informal arrangements to more formalised relationships and possible links with the formal sector institutions. The commercial banks willing to forge these links with decentralised systems are called linkage banks. Numerous advantages exist for linkage banks. They mobilise savings at a very low transaction cost compared to interacting with each member of the village bank. If they provide funds for on-lending to members they make use of the information and monitoring arrangements within the village banks. However, a very careful approach should be followed not to provide on-lending funds at volumes that disturb the balance between member funds and external fund. This may have detrimental effects on control and management of the village bank.

5. CONCLUSION

The discussion of the client groups, formal financial intermediaries and the decentralised approach in South Africa had the purpose to introduce these concepts as an integral part of the broader financial system in South Africa. This discussion was not meant to be exhaustive, but rather illustrative. The concept of a broad range of institutional possibilities, none of which specifically provides a conclusive model, is considered to be realistic. The idea is to muster this range of possible forms into a co-ordinated effort to increase access to financial services for rural people in all rural areas. One purpose of this paper was to emphasise the reality of the situation when choosing policy directions. NGOs, commercial banks and the Post Bank do not hold the primary key to improving access to financial services in rural areas.

Several studies discussed the broad range of possible institutional forms in the rural areas of South Africa. The role of decentralised financial systems has not been the focus point of any of these studies. It is argued that fertile ground exists in South Africa for these systems to address access problems at the local level. Decentralised systems also cannot be the solution to all intermediation problems. A multi-pronged approach is proposed, harnessing all institutional forms into a comprehensive strategy.

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