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## THE SUPPORT NEEDS OF RURAL SMMEs: THE CASE OF PHUTHADITJHABA, FREE STATE PROVINCE

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*The problems and support needs for the development of small, medium and micro-enterprises (SMMEs) in the rural areas of South Africa have been little researched. In this paper, the Phuthaditjhaba area of Free State province is a case study in the developmental problems and needs of rural non-farm or SMME development in South Africa.*

### 1. INTRODUCTION

Across rural Africa, the question of creating non-farm employment opportunities is a key policy issue, particularly in the context of shifting agricultural technologies and agrarian structures. Research produced for the International Labour Organisation suggests that the expansion of non-agricultural employment opportunities is "the only hope of providing full employment" (Chuta & Sethuraman, 1984: v) for expanding rural labour forces in the developing world. One key area of non-farm employment generation relates to the promotion of rural small, medium and micro-enterprises (SMMEs).

Until recently, there was little knowledge of how much and why rural African households were involved in the rural non-farm sector. Indeed, a feature of African research was that the rural dimension of small enterprise development "received relatively less attention than urban sector initiatives" (Alila, 1996: 176). In the wake of its growing policy significance, the problems of rural small enterprise development attracted a number of researchers in many parts of Africa (see e.g. Wilcock & Chuta, 1982; Norcliffe, 1983; Freeman & Norcliffe, 1983, 1984a, 1984b; Arnold *et al*, 1994; Liedholm *et al*, 1994; Reardon, 1997 and Meyer, 1998). This body of research disclosed the existence of widespread self-employment in small enterprises in rural areas across Africa. A key theme is that of the survivalist character of much of rural small enterprise development (Liedholm *et al* 1994). Nevertheless, some newer works are pointing to the existence of rural clusters of enterprises with positive growth performances (McCormick, 1997 and Mitullah, 1997).

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With some notable exceptions (Reichenbach, 1994; Kirsten, 1995, 1996; Thomas, 1996; Rogerson & Reid, 1997 and Rogerson, 1998), the activities of the rural non-farm sector, including development of the SMME economy, are relatively under-researched in South Africa. The aim in this article is to contribute to this limited body of local knowledge concerning the support needs and development prospects of the rural small, medium and micro-enterprise (SMME) economy in South Africa. More specifically, the focus is on the problems and support needs of the SMME economy in the Phuthaditjhaba area, which is located in eastern part of Free State province.

The research builds upon two different interview approaches. First, a formally structured questionnaire was administered to 61 SMME entrepreneurs working in the Phuthaditjhaba area. These interviews were conducted at a range of sites both within the TLC area and outside of its formal boundaries. The research methodology combined a mix of standard questionnaire survey and qualitative responses by SMME entrepreneurs, allowing them to voice their views on a set of open-ended questions. It is argued that the use of this qualitative material strengthens the validity of the broader survey findings for many important issues concerning the support needs for rural SMME development remain unknown from use of the standard interview survey material alone. Second, a set of semi-structured interviews was conducted with key stakeholders, policy makers and actors in SMME development within Phuthaditjhaba and the wider eastern Free State areas.

The paper is structured in terms of four sections. First, attention turns to describe features of the selected case study area. In section two the focus is upon the policy context for rural SMME development in the Free State. In section three, the findings are presented of the questionnaire and other interviews undertaken in the Phuthaditjhaba case study. In the conclusion, policy issues concerning the support needs of rural SMMEs are raised from this investigation.

## **2. THE CASE STUDY AREA OF PHUTHADITJHABA**

The history, emergence and expansion of Phuthaditjhaba is inextricably woven into the apartheid policies of homelands creation and forced removals (Murray, 1985, 1992). The 'self-governing' Homeland of QwaQwa was established on 1 November 1974; soon after its declaration the local magistrate estimated that QwaQwa's population was some 200 000 people. By 1980 this had mushroomed to at least 300 000, a population density of 484 persons per square kilometre. The vast majority of these people were concentrated in the Phuthaditjhaba area, which constitutes the largest resettlement or 'dumping ground' in the former QwaQwa Bantustan (Murray, 1985; Pickles and Woods, 1992).

## **2.1 Bantustan capital and industrial growth point**

Phuthaditjhaba's historical growth accompanied the period of the 1970-80s apartheid 'voluntary' removals which were the product of evictions from white farms and small towns across both the Free State and (the former) southern Transvaal (Murray, 1992). Faced with mounting state pressure to relocate, few alternatives for resettlement and difficulties with migration to cities, many households moved to QwaQwa, able to take possession of a plot for a shack or believing that it would be easier to obtain labour contracts from QwaQwa than from white-owned farms. For many other relocates, the move to Phuthaditjhaba meant simply that they had "a place to die in" (Platzky & Walker, 1985). The detailed accounts of forced removals provided by the Surplus Peoples Project (Platzky & Walker, 1985:338) capture the essential origins and bases for the establishment of Phuthaditjhaba.

"There is probably not a single Bantustan community that does not have its quota of people who have been squeezed out of wherever they were before in terms of various aspects of the government's relocation programmes. QwaQwa, the smallest and most densely populated of the bantustans, illustrates this process most dramatically. The district of Witzieshoek is little more than one closer settlement - a peri-urban slum in the middle of nowhere. Most of the people who have been flooding into it in the past ten years have come off white farms and small town locations throughout the Orange Free State. They have moved there because they have nowhere else to go."

Overall, Phuthaditjhaba represents a classic example of an apartheid nurtured settlement form that is difficult to classify in terms of conventional definitions of what is 'urban' or 'rural'. Terms such as 'rural slum' or 'displaced urbanisation' apply equally well to such settlements. Phuthaditjhaba is best understood as falling into that special category of artificial rural settlements which house "apartheid's hidden urbanites" (Centre for Development and Enterprise, 1996). Officially, Phuthaditjhaba today is classed as 'urban' with those areas that fall under tribal land ownership, outside the demarcated area of the Transitional Local Council (TLC), classified as 'rural' (Smit, 1997). Accurate population estimates must await the outcome of the 1996 census; the TLC of Phuthaditjhaba, however, works on an estimated population in the functional area of roughly 400 000 persons (Kelso, 1997:11).

Although in functional terms Phuthaditjhaba was constituted as a dumping ground for surplus labour, during the early 1980s government-led efforts began to establish an economic base particularly through the attraction of manufacturing activities. Under the auspices of the 1981 Regional Industrial

Development Programme a set of lavish incentives, in the form of large capital and infrastructure incentives, including wage subsidies, were made available. The package of incentives became very attractive to investors (many of them foreign) seeking opportunities to access cheap unskilled labour. Factory employment escalated rapidly with the opening up of new industrial townships in Phuthaditjhaba; by 1982 35 factories were employing 2100 people, by 1988 there were more than 200 factories and total industrial employment had grown to 22 000 jobs. Indeed, by the late 1980s it was argued that "the limits imposed on growth under the incentive programme have actually operated as a constraint on an even greater number of possible new factories in Phuthaditjhaba" (Pickles & Woods, 1992: 644); at this time, new factories seeking to establish in QwaQwa were redirected to Industriqwa, a new industrial park that had been constructed close to Harrismith. Typically, labour at the industrial sites in Phuthaditjhaba was female, ultra-cheap and exploited in terms of poor work conditions and minimal worker protection (Pickles, 1991; Sharp & Spiegel, 1996). The majority of the factories, which were engaged in producing textiles and clothing, glass, shoes, furniture, metal goods and curios, were extremely labour-intensive. Importantly, most factories in Phuthaditjhaba exhibit few local linkages with most raw materials and inputs brought in from the major metropolitan areas (or, in the case of clothing companies, from overseas), which were also the prime markets for the finished items (Pickles, 1991; Pickles & Woods, 1992 and Sharp & Spiegel, 1996). Indeed, some clothing factories, which were locked into the system of global production, were virtually sealed off from the local environment apart from the job opportunities that they created (Sharp & Spiegel, 1996:16).

## **2.2 The economic and political demise of Phuthaditjhaba**

Whilst the raw statistics on new factory development and industrial employment growth suggest the success of Phuthaditjhaba as an industrial growth point under apartheid planning, the foundations of this achievement were extremely fragile. Even in the late 1980s it was conceded by officials of the QwaQwa Development Corporation that the majority of enterprises were not economically stable or viable enterprises and that there was a strong likelihood that without state incentives, many would choose to leave (Pickles and Woods, 1992: 646). Such predictions have been borne out by trends taking place in Phuthaditjhaba since the 1991 changes in the regional industrial incentives. Although the draft Free State provincial spatial framework for growth and development notes that industrial decline is likely to occur around former IDPs, including Phuthaditjhaba, it was optimistic that "owing to existing infrastructure and the proximity of local labour with industrial experience, tax

incentives to attract future manufacturing may sustain their growth" (Free State Province, 1996: Annexure 9).

This optimism is not confirmed by other available evidence. Although accurate data is unavailable, officials at the Free State Development Corporation (FDC) concede that the manufacturing base of Phuthaditjhaba was haemorrhaging with a loss since 1994 of almost 50 percent of factories either due to closures or relocations (May, 1997). This factor combined with the losses of civil service jobs with the demise of Phuthaditjhaba from its status as capital of QwaQwa and the rationalisation of the Free State civil service has further contributed to an employment downturn in the town. Research in Phuthaditjhaba undertaken in 1998 further confirmed a picture of employment downtown in the local manufacturing economy (Abrahams, 1998). In the opinion of Harrismith's Town Clerk, Phuthaditjhaba is presently in the throes of "dyeing a natural death" as a result of unfavourable changes in government RIDP incentives and of its new diminished political status (Botha, 1997). During the next decade it is envisioned that a further shift of businesses will occur away from Phuthaditjhaba into Harrismith (Botha, 1997). Although there is no formal lines of responsibility as Harrismith and Phuthaditjhaba are separate TLCs, the functional links between the two places were forged historically and remain still strong (Hunter, 1993 and Abrahams, 1998).

The new political geography of South Africa has resulted in a radical downgrading of the functional importance of Phuthaditjhaba. From a position of benefiting from the status of capital of an artificial state, the town is now reduced to being a minor centre at the eastern periphery of the Free State spatial system. Moreover, the new focus of provincial power is clearly anchored in Bloemfontein and Phuthaditjhaba is increasingly marginalised in terms of both political clout and development opportunities. Indeed, even within the context of the Eastern Free State, the prospects are that Phuthaditjhaba may diminish even further in significance as Bethlehem may assume the role of dominant sub-regional focus. It is against this backcloth of the changed position of Phuthaditjhaba since 1994 and particularly of the major downturn in the local economic base, that the importance of strengthening the potential for SMME development can be appreciated.

### **3. FREE STATE POLICY CONTEXT AND INSTITUTIONAL FRAMEWORK**

Until recently, it could be argued justifiably that there was "a lack of clear policy frameworks for development in the province", particularly concerning rural areas (DBSA, 1995:55). In the case of SMME development, policy development

in the Free State lagged behind certain other provinces (such as Mpumalanga) which have produced and are beginning to implement a set of programmes for SMME development (Rogerson & Reid, 1997 and Rogerson, 1998). Nevertheless, the situation as regards policy frameworks both for rural development and general SMME development in Free State is showing some signs of positive improvement. For rural development, in particular, the province is well advanced in its policy thinking.

In approaching the issue of rural SMME development, a good starting point is the work of the 'Free State Mission on Rural Investment' which was the product of a joint task team initiative conducted between the provincial Department of Agriculture, The Rural Strategy Unit and the World Bank. One of the key objectives of this study was to "help define development priorities in the rural sector" of the Free State (Task Team *et al.*, 1997:12). Although the report's core focus is upon land reform and the role and restructuring of agricultural activities, the report acknowledges the significance of the 'non-farm economy' in provincial rural development planning which would be designed "to create improved livelihoods for the majority of the population" (Task Team *et al.*, 1997). The report recognises that a substantial "share of job creation in the Free State is likely to come from agricultural processing and non-agricultural employment in small, medium and micro enterprises" (SMMEs) (Task Team *et al.*, 1997:78). Correctly, it identifies that "the development of non-agricultural enterprises and employment opportunities has important synergies with agriculture-oriented programs in creating sustainable livelihoods" (Task Team *et al.*, 1997:99). This opens the possibility for seeking to identify a set of niche focused activities or clusters in the Free State which would transcend the distinction between farm and non-farm activities (Thomas, 1996:33). Planning for the development of such clusters, which might be agro-industrial or tourism based, would involve maximising development opportunities in the production, processing and distribution of raw materials, both on and off-farm.

The overall strategy proposed for rural development in Free State is to boost the asset base of historically disadvantaged and marginalised individuals, groups and communities through a re-orientation of services and resources. More specifically, the proposed programmes for rural development contains two major components. First, is the restructuring of government departments, their services and activities, in order to address the needs of their new client base. Second, the launching of new investment programmes designed to create employment opportunities both on and off farm through assistance packages targeted at new land owners under the land reform programme and through the building of new partnerships with the private sector to finance new enterprises (Task Team *et al.*, 1997:90).

The key policy interventions surrounding the investment programmes for off-farm employment and income generation provide the link to rural SMME development. The proposed programme is geared to "direct financial resources and efforts towards improving the prospects of unemployed people, potential new entrepreneurs and existing small businesses by overcoming the main constraint to development - the lack of intermediaries that provide access to finance and to markets" (Task Team *et al*, 1997:92). There are four sets of major programmatic interventions. First, to nurture the development of retail financial intermediaries that might link to Khula financing programmes. In this respect: (1) training will be given to extension workers and to selected managers of community-based finance organisations, such as community savings and loans groups, credit unions or stokvels, (2) funding will be granted to a local parastatal support provider and to business extension workers to assist in drawing up business plans and to provide aftercare to borrowers, and seed capital grants to community-based finance organisations for a limited period of one or two years. Second, the programme will assist in establishing a Joint Micro Finance Company in partnership with commercial banks to target a group of enterprises already identified with viable business plans. Third, assistance will be provided in the marketing aspects of SMME development by provision of information and facilitating links with input suppliers. Existing incubators for SMME development will be maintained and expanded with the potential development of new market sites. Finally, the potential of developing specific eco-tourism initiatives in Free State as a further base for SMME development is to be investigated.

Overall, the Task Team report provides a solid foundation for a set of provincial policies and programmes to "create a better rural livelihood" by developing an enabling environment within which rural people can create wealth, employment and incomes. At the heart of the rural strategy, including suggestions for SMME development, is "to enhance rural development through facilitation of increased private sector involvement and mobilisation, and support of community initiatives" (Task Team *et al*, 1997:98). Against this provincial policy backdrop, it is appropriate to turn to examine the support needs of SMMEs development in the Phuthatditjhaba study area.

#### **4. PHUTHADITJHABA SMMEs: SUPPORT NEEDS AND CONSTRAINTS**

In this section, the focus turns to examine the situation of rural SMME development 'from below'. More specifically, the findings are reported from the questionnaire interviews and qualitative responses collected from emergent SMME entrepreneurs in the Phuthaditjhaba area. These findings are linked



together with the results of other recent research undertaken in the Free State concerning SMME development in rural areas (Task Team *et al.*, 1997). In presenting the results, the discussion is organised in terms of two themes, namely (1) the characteristics of the local Phuthaditjhaba SMME economy and of its entrepreneurs, and (2) the perceived needs and constraints of emergent SMME businesses.

#### **4.1 The characteristics of SMME activities**

The study area contains a diverse range of different kinds of SMME activities occurring both within the boundaries of the Phuthaditjhaba TLC and outside those borders which extend into areas of what can be styled as "deep rural settlement". Overall, the survey of 61 SMMEs was broken down in terms of 36 interviews within the TLC area and the remainder (25 interviews) outside the TLC. The gender breakdown of interviewees was 38 males (21 inside TLC, 17 outside TLC) and 23 females (15 inside TLC 8 outside TLC). In terms of broad types of SMME activity the survey captured 15 manufacturers (12 inside TLC, 3 outside TLC) , 30 retail (14 inside TLC 16 outside TLC) and 16 service enterprises (10 inside TLC, 6 outside TLC), a group that includes also three agricultural enterprises in the form of groups of poultry and egg producers. In respect of size and structure of enterprise the following breakdown was recorded in the interview sample: (1) a group of 22 enterprises (14 inside TLC, 8 outside TLC) which were owner or household (husband and wife) operated with no regular employees, (2) a group of 23 very small enterprises with less than 5 employees (12 inside TLC and 11 outside), and (3) a group of 13 small enterprises with between 5 and 20 employees (inside TLC, 4 outside TLC), and (4) three enterprises (1 inside and 2 outside TLC) with more than 20 workers; in this last group were a co-operative and two loosely structured groups of individuals.

There were some similarities in the mix of SMME enterprises that were observed and interviewed both within and outside the defined boundaries of the Phuthaditjhaba TLC. In both areas there occurred a typical mix of retail and service activities which included general dealers, spazas, cooked food sellers, restaurants, taverns, and hairdressing salons. Nevertheless, certain differences were observed in the range of SMME activities taking place within the defined TLC area as opposed to outside the TLC. Three key points of difference were noted. First, there was a stronger link back to the land and a dependence on natural resources in terms of certain SMMEs which were conducted outside of the Phuthaditjhaba TLC area. Examples included the activities of brickmakers, craft workers, the production of grass mats, brooms, sandstone producers for building and milk products. Second, there was a much higher proportion of

manufacturing activities as a whole conducted within the Phuthaditjhaba TLC area than outside the TLC. This pattern was linked both to market opportunities and also the provision inside the TLC of certain premises in the form of FDC Beehive incubator complexes which were dominated by small-scale producers. Lastly, the diversity of enterprises was considerably greater as a whole inside rather than outside the TLC area. Examples of activities occurring within the TLC that were not captured outside included the operation of book shops, radio and TV repairs, the operation of driving schools, dry cleaners, bakeries and a cluster of manufacturing activities that encompassed furniture production, clothing, upholstery and metal working.

Typically, certain gender variations were observed in terms of the kinds of enterprises that were male- as opposed to female-dominated. The group of manufacturing enterprises exhibited a marked gender divide between production SMMEs that were run by male as opposed to female entrepreneurs. Inside the TLC males dominated in furniture, upholstery and metal work; outside the TLC these activities included brickmaking and the production of building stone. By contrast, women were clustered within the TLC in a range of clothing and sewing related activities which encompassed dressmaking and the production of school uniforms; outside the TLC women producers were engaged in craft-related activities, such as the production of grass mats. In terms of retailing and service activities a similar divorce of male and female dominated businesses was in evidence with men engaged in a much broader range of activities than women. Male dominated activities included the operation of bookshops, hardware, TV and video repairs, watch repairs, the running of driving schools, panel-beaters and motorcar workshops. Women tended to cluster in the activities of provisioning cooked food, liquor vending, and hairdressing.

These findings from the Phuthaditjhaba study disclose a pattern that the quantitative development of SMMEs inside the TLC considerably exceeds that which takes place outside the defined TLC border. Within the TLC and in its immediate hinterland the nature of SMME businesses is little different from that found in urban township areas of South Africa (cf. Horn, *et al*, 1993 and Rogerson, 1996). Nevertheless, the rural character of the SMME base is more distinctive outside of the TLC and in particular in the deep rural areas where there occurs a greater linkage back to the natural resource base. This suggests that support measures for SMME development would have to include both a set of supports for the group of manufacturing, service and retail enterprises that occur both inside and outside the TLC and a more specialised set of support structures to assist those SMMEs whose needs directly relate back to the land or agricultural activities.

In terms of the size of enterprises the largest SMME that was interviewed was an Indian-owned furniture producer with over 20 regular employees. In addition, a broom-making project engaged more than 20 persons. Overall, the majority of manufacturing enterprises fell into the categories of very small or small enterprises rather than single owner-operated concerns, which suggests that such activities contained some potential for expansion. By contrast, over half of the retail businesses were simply survivalist enterprises, which were owner-operated. Illustratively, such activities included the vending of fruit and vegetables, liquor selling and the making of cooked food. A wide range of size of enterprises was evident in the service sector which reflects the sector's diversity and its mix of opportunities for expansion. In services some enterprises are confined to what appear to be survivalist niches whereas others have shown clear evidence of growth.

The age and educational profiles of entrepreneurs disclosed some interesting patterns. The age profile (36 responses) revealed that over half of our sample were entrepreneurs who were older than 50 years and almost a quarter were over 60 years. By contrast, few entrepreneurs were aged less than 30 years; indeed only 12 percent of our sample were such entrepreneurs. No distinct sectoral differences were observable apart from a trend for retail enterprises to be dominated by entrepreneurs aged 50 or more. These findings are suggestive of the role of the Phuthaditjhaba SMME economy for the absorption of retired or retrenched workers rather than a life career choice made by younger entrepreneurs. The educational profile (60 responses) disclosed a pattern that most entrepreneurs had achieved only a maximum of Standard 8 education: 42 respondents (70 percent) fell into this category and 7 respondents (12 percent) had achieved only a primary school qualification. At the higher end of the educational qualifications 18 entrepreneurs (30 percent) had achieved a matric or a post-Standard 8-diploma qualification. In the sample of interviewees the two entrepreneurs with the highest educational qualifications were both in the business of running bookshops.

The nature of premises in which SMMEs presently operate showed a variety of responses. The majority of respondents that were interviewed were occupying space in "permanent buildings other than home", including a number of beehive complexes that had been established by the Free State Development Corporation (FDC). In particular, such premises were popular amongst the group of manufacturing enterprises. Permanent buildings were also the site of operation for the largest number of interviewees in both the retail and service sector. It must be acknowledged, however, that a number of retail/service activities occupied containers rented out by FDC within industrial areas (supplying cooked food, liquor and unprepared foodstuffs) and what can be

loosely termed 'markets' which were formed around taxi ranks inside the Phuthatijhaba TLC. Other premises that were utilised were land in the case of brick makers, shacks for a number of spazas and food vendors, as well the category of fixed and temporary stalls. The survey captured only two home-based enterprises (spaza and a hairdressing salon) although it must be assumed that many of the existing SMMEs may have originated in home or backyard premises. The precise reasons for choice of existing location premises were unclear in that the majority of questionnaire responses were either that "the activity requires this type of work place" or "can make good sales in this way".

In terms of the establishment and origins of businesses a number of findings emerge. The patterns of business start-up show a range of experiences in our sample of interviewees (59 responses). More than half of the respondents (32 responses or 54 percent) have been in their existing business for less than four years and in 5 percent of cases in business for one year or less. That said, 25 percent of respondents had been operating their businesses for between five and ten years; and, 21 percent have been established for more than ten years.

The findings point to the key factors responsible for the origins of the SMMEs in Phuthatijhaba as a consequence of necessity out of desperate circumstances for survival rather than a result of a conscious choice made out of circumstances of a perceived business opportunity. From qualitative responses that were gleaned in order to supplement the questionnaire, the imperative of survival due to household circumstances was in evidence. This is illustrated in the following comments:

- "I started this business in 1985 after I got retrenched from the mines in Roodepoort - I did the same job in the mines part-time" (TV and Video repairer);
- "I was a houseworker. My husband got retrenched and I had to do this business" (Food Vendor).
- "I was retrenched. I was working at Pick and Save" (Spaza Operator).
- "The shop closed where I worked" (Cooked Food Vendor).
- "After matric I could not get jobs" (Member of Co-op Supplying Catering Services).

In some cases, it is possible to discern a pattern of building upon skills which were learned in prior formal employment for use in the start-up of an SMME in

Phuthaditjhaba. For example, a former manager of CNA now runs a local bookshop, and a former bakery employee in Johannesburg now operates a bakery business in Phuthaditjhaba. Overall, the complexities of understanding the start-up process for SMMEs in this area are illustrated by a short business history of one entrepreneur who currently operates the local hardware shop:

"I started business here in QwaQwa in 1980. Before that I was working as a salesperson for Alex Robinson factory in Johannesburg. That was in the '60s and '70s. Through their workshops I learned business skills and management - including talking to people. I was later able to buy from them and sell for myself. In the late 1970s I decided to come here to QwaQwa because the place was good for me. I then sold cosmetics, buying from Johannesburg. In 1980 I sold my car and made a fixed deposit of R15 000. Through this money I was able to negotiate a loan with Volkskas Bank of the same tune. I could then build this hardware but because I did not have money for stock I leased it to an Indian guy. This was done following several unsuccessful applications to FDC".

The sources of start-up capital for SMMEs in the Phuthaditjhaba study confirmed certain of the key findings of other research on SMME development. In total, 63 responses were obtained with many entrepreneurs citing more than one source for their start-up capital. The majority of responses related to own savings or funds from relatives as the core source for start-up capital; in total, these represented 38 (or 60 percent) of sample responses. Sometimes, the start-up capital was in terms of "own savings" related to the payment of retrenchment packages:

- "My husband got retrenched and so we had to do something to have food on the table. We used his savings to buy a gas stove and some few stock and utensils. People supported us - they bought as if they knew our situation" (Cooked Food Vendor).
- "I was working for a company in Harrismith. I then used part of my package to start a business" (Rural Settlement Poultry Business).

After own or household savings, the next set of common responses concerning source of start-up capital related to loans secured from parastatal institutions, such as FDC and Agri-Eco, or from commercial banks, possibly obtained also through the intermediary assistance of an organisation such as Agri-Eco. In total, this group of responses (14) represented another 22 percent of our sample. Finally, the remaining responses related to either "no need" for start-up capital (7 responses - 11 percent) or more worryingly "moneylenders". Significantly, only one respondent cited stokvels as the source of start-up funding.

Membership of business associations was not common in our sample of interviewees. Overall, of 51 responses, 47 were not involved in any business association, organisation, network or co-operative. Of this group, the majority (33 responses) did not know of the existence of any such organisations and 11 respondents felt strongly that they saw no benefits of joining the associations that they knew were operating. Moreover, there was little enthusiasm for helping to form or join any association in the Phuthaditjhaba area. The only survey respondents that were linked to an association were one taverner (Phuthaditjhaba Taverner Association), one bookshop owner (QwaQwa Chamber of Commerce), one hairdresser (stokvel) and most interestingly, one hardware owner who stated that he had just joined an un-named group that supposedly was committed to fighting corruption in the FDC. Overall, these findings on the low associational membership of entrepreneurs point to minimal levels of social capital in the Phuthaditjhaba area. Social capital is a critical asset of the rural poor and refers to the networks, norms and trust that facilitate mutually beneficial co-operation in a community (Moser, 1997). The weakness of community networks and social capital in Phuthaditjhaba is not surprising in view of the settlement's chequered history which was based on the forced uprooting and destruction of communities.

## **4.2 Needs and constraints**

In this section, a discussion is provided on key policy themes in SMME development. The results of the Phuthaditjhaba survey are analysed concerning SMME's assistance from support organisations, access to services, finance and markets, and training. Finally, the Phuthaditjhaba results are placed in the context of other recent research on rural SMME development in Free State Province.

### ***4.2.1 Access to institutional support***

At the time of the interview research (June-September 1997), the key support organisations in Free State Province were (1) two parastatal agencies that emerged out of the restructuring of state development corporations inherited from the apartheid period, namely the Free State Development Corporation (FDC) and Agri-Eco and (2) a group of major private sector organisations, such as the banks and the local business enterprise.

Within its defined focus on SMME development, the FDC stresses that the organisation is withdrawing from the activity of providing premises and of its predecessor's function as property developer (Nchocho, 1997). In addition, the organisation resolved to withdraw from training activities, which were seen as

financially non-viable as a whole, and instead to facilitate such training through other agencies such as the Potchefstroom-based Small Business Advisory Bureau and the local branch of University of the North (May, 1997). The FDC has made a strategic choice to stress its roles in (1) financing and (2) advisory support services which relate to improved data on SMMEs and augmenting information flows, including advice on tenders (Nchocho, 1997: 5).

Agri-Eco was constituted in 1994 out of the remnants of the agricultural and tourism sections of the former homelands development corporations (Kuun, 1997). Agri-Eco has experienced major restructuring and furnished business advice and support to new or growing businesses, primarily micro-enterprises. The organisation's mission was to establish sustainable enterprises with a special focus in rural communities (Agri-Eco, no date).

Support for rural SMME development can be provided by the private sector particularly in terms of improving access to markets and finance. Often business linkages between large enterprises and emerging SMMEs are an important element in 'growing' the local SMME economy. In addition, the role and attitude of local commercial banks often is critical in terms of access to finance. In interviews conducted with Harrismith's largest two enterprises, Nestle (Acklom, 1997) and Nouwens Carpets (Nouwens, 1997), it was revealed that neither concern had any specific initiative for assisting or interacting with local or regional SMMEs. These interviews indicated that there were few opportunities for subcontracting linkages and that the rural SMME economy was at best marginal to the operations of the large private sector manufacturing enterprises in the Eastern Free State. The most tangible potential supportive role of the private sector in SMME development in the Eastern Free State therefore relates to issues of finance.

It was clear from the survey findings that the existing network of support organisations for SMMEs is not matching the need for such assistance in the Phuthaditjhaba area. Overall, of 59 responses in total, 41 (69 percent) said that they had not received assistance from support organisations. Only 18 respondents (31 percent) indicated that assistance had been obtained. Moreover, it is evident that manufacturing and service related activities were more likely to receive assistance than survivalist retail enterprise; in proportional terms the share of enterprise that had received assistance was 43 percent of manufacturers, 40 percent of service enterprises and a mere 20 percent of retail enterprises. In total, support was most commonly obtained from Agri-Eco (11 responses including one jointly with FDC) followed by the QDC/FDC.

Few respondents stated that they had received assistance in the form of direct commercial bank loans. The most common reasons given for not applying were simply that procedures were viewed as too complex (particularly for those with poor levels of education) or respondents were unsure or "scared" of their ability to repay loans. Of our sample of 61 SMMEs, 55 responded on the issue of applying to banks. Only 11 (20 percent) had applied to commercial banks for funding, many of these being the larger enterprises in our sample or enterprises that had been facilitated by the activities of Agri-Eco. Overall, the types of assistance that were gained from Agri-Eco concerned training, help in securing a loan, and business counselling. From FDC the assistance was primarily in the form of loans or assistance with equipment.

#### *4.2.2. Access to services*

In terms of the needs of SMMEs, the issue of basic service provision can be of fundamental importance. The pattern emerged clearly that the availability or non-availability of infrastructure services was directly linked to the location of businesses. Generally speaking, those SMMEs situated inside the Phuthaditjhaba TLC area were better provided for than those situated outside the demarcated TLC area with the worst access to services occurring in the deep rural areas. Moreover, those businesses that were situated in permanent structures, whether inside or outside the TLC area, were better provided for in terms of services than those SMMEs which were conducting their businesses from shacks, containers or temporary structures on the roadside. The overall picture that was determined by survey responses (52 responses) was as follows: access to electricity (35 yes, 17 no); water (35 yes, 17 no); toilets (34 yes, 18 no); protection from weather (37 yes, 15 no); adequate drainage (36 yes, 16 no); refuse removal (23 yes; 29 no); security (23 yes, 29 no); and, adequate roads (45 yes, 7 no). The picture is clear in terms of a common package of infrastructure facilities that are available to most SMMEs which are dependent on their location. Beyond these stated services, the most commonly requested additional service that was unavailable concerned access to telephones.

#### *4.2.3 Access to finance and markets*

The material collected both from the quantitative and qualitative responses in the survey demonstrated a clear pattern in terms of the major constraints and corresponding specific needs of SMMEs for assistance in the Phuthaditjhaba area. Of a listing of 43 potential 'problems' affecting business operations only ten were even mentioned in the Phuthaditjhaba survey. All the problem responses concerned access to resources or markets. Indeed, it was significant to record that no respondents cited labour-related problems or environmental issues as



major problems or constraints upon their business operations. The caveat must be added, however, that the question of violence and crime was raised as a negative environmental factor on business development by several respondents. Of the survey respondents, 64 responses were obtained concerning the issue of problems affecting business; some respondents gave more than one factor. At the outset, it should be noted that in 12 cases (almost 20 percent of the total) the response was that they saw no problems at all in their existing business operations and were satisfied with their present circumstances. The majority of respondents did, however, identify resource or market constraints on their business. In total, 39 responses concerned resource-related issues and 13 related to market issues.

Within the category of resources, overwhelmingly the mass of respondents were concerned with finance issues, both for investment and working capital. Overall, lack of investment capital followed by lack of working capital were identified as the two most prevalent constraints on SMMEs in the Phuthaditjhaba survey. Beyond finance-related considerations, questions of access to markets loomed as the next most significant set of constraints. The lack of retail customers was the third most common individual problem that was observed. The only other factors that were cited as constraints by more than one respondent concerned lack of government customers, poor work sites (mainly among street vendors), high cost or lack of up-to-date tools and equipment (an issue raised particularly amongst the group of manufacturing enterprises) and transport (an issue of concern particularly to SMMEs situated in deep rural areas).

When entrepreneurs were requested to identify the most important problem in their business a similar set of responses was obtained. In total 40 responses were noted, 12 SMMEs cited no problems and 9 non-responses occurred. Of the 40 responses, 21 (53 percent) relate to finance considerations. Across all types of SMMEs, manufacturing, retail and services, and across all size ranges - from household or single operator run businesses, through very small to small enterprises, the issue of access to finance was identified as the most important constraint on SMME development in Phuthaditjhaba. After finance, once again access to markets was the second most significant constraint, which was cited by 11 (28 percent) respondents. Other responses relate to inadequate business premises (4 responses), poor or costly equipment (2 responses) and transport (2 responses).

The material obtained from use of qualitative interviews confirms strongly the above picture concerning access to finance and markets as the core issues that demand policy attention. The following statements and quotations amplify the importance of financing as the number one priority.

- "As I speak to you, I want money to buy stock" (Cafe Owner).
- "I desperately need money. All I need is space and finance" (Upholsterer).
- "I have not had any help. I do not want loans because I may fail to repay it back and that means a jail sentence" (Tailor)
- "There is no money to further my business...I do not have any idea of where to go" (Producer of School Uniforms).
- "We would like FDC to finance us, just giving us machines which we pay for is not enough" (Furniture Producer).
- "My major difficulty was money to buy stock and I had no one to borrow from" (Dressmaker).

Often the perceived solution to lack of finance was seen by SMME entrepreneurs as assistance from government. Typically, for example, one liquor vendor stated "I want the government to help me with money" and a spaza owner declared: "I am still crying for the government to help me with stock". Other respondents were aware of the role of the commercial banks in financing but drew attention to problems in accessing that finance. One general dealer said: "I think it is banks who can help but the banks lending system is too complicated for me". Another respondent claimed "We tried to get money from the bank but never succeeded. We finally got assisted by Agri-Eco" (tailor).

Some success stories in terms of accessing finance were, however, mentioned by interviewees. In particular, the assistance from Agri-Eco as functioning in the role of intermediary was appreciated on several occasions. In one case, a clothing retailer averred: "We did not know how to run a shop...One lady from Agri-Eco realised our failure and stepped in to help us. Agri-Eco helped us with training in business management and operational courses. We got linked with African Bank by Agri-Eco. Agri-Eco also helped us with business plans that the Bank wanted from us".

Access to markets was a problem that was aired by many respondents. Key themes of concern that were raised related to the downturn in the local economy as a result of public sector retrenchments and the closure of factories. The following three comments were typical:

- "Business was doing good up to three years ago. Some of our customers went to Bloemfontein" (Hair Dresser).

- "The problem is that there are no customers because the firms around are closing" (Seller of Cooked Foodstuffs).
- "The problem is that our customers do not have money. The general economy of QwaQwa is poor and many companies have left" (Women's Dressmaker).

Given the downturn in the private sector, it is not surprising that the issue of access to government tenders assumes considerable significance. Issues of access, information about such contracts and the transparency in the award of these contracts were raised by several interviewees:

- "The problem I have as of now is the allocation of tenders. Tenders are not given to recognised businesses but to backyard businesses and even irrelevant people. An example is a tender for the supply of HB pencils for the government. This tender was given to a guy owning a butchery. The guy does not even know where to get the lead pencils. He ended up in my shop ordering thousands at a retail price" (Bookshop Owner).
- "The problem I have is tendering. When perceived to be rich the government does not give you tenders" (Bookshop Owner).
- "Tendering is complicated. We have lost a lot of money and time filling in those big tendering documents. We are tired of it now. The problem is corruption because those who get tenders are not better than us" (Dressmaker).
- "Problem is corruption in government. If you are not known you do not get help" (Food Vendor).
- "The government must make tendering easy for us. I want the contracts for school uniforms" (Clothing Producer).
- "We do not know about tendering. We do not know who to talk to" (Tailor).

Assistance with improved access to markets came from interaction with and support gained from the SMME service providers in the Phuthaditjhaba area. For example, two groups of producers who had been assisted in such way acknowledged its significance:

- "Agri-Eco helped us to do marketing through displays and shows" (Producers of Building Stone).
- "We have not been helped by government. It is only Agri-Eco who helped us by taking us to exhibitions in various places, including Johannesburg" (Craft Producers).

#### ***4.2.4 Access to training***

The question and significance of access to training emerged at several points throughout the survey. Although training was not stated as a core need by entrepreneurs, it is evident that access to training is a significant underpinning in the success or failure of SMMEs. Indeed, it is clear that access to both finance and markets was improved through prior access to training and the assistance offered by the major support organisations in the Phuthaditjhaba area.

The issue of need for training in business skills was demonstrated in the responses related to the maintenance of business records. Of the total number of responses received (50 responses) the clear picture emerges that most businesses keep at best only rudimentary or general records (26 responses) and a substantial section of SMMEs (24 or 48 percent) keep no records at all. Very few businesses kept a ledger/general accounting book (8 responses - 16 percent) or prepared an annual set of final accounts (7 responses). It was apparent from our qualitative responses that the reasons for no record keeping were a combination of lack of business knowledge, "no one to take care of books" and the generally hand-to-mouth nature of the survivalist businesses.

- "I have not thought about it but I realise that it is important to keep records" (Taverner).
- " It is difficult for me to write down every single item as it is purchased" (General Dealer).
- " My business is too slow. I hardly get 5 cars a day. Besides my business is hand-to-mouth at this stage" (Welder).
- "I was keeping records but because of poor performance of my business I stopped. I now record in my head" (Brick maker).

Overall, it was evident that record keeping was undertaken most meticulously in the largest businesses of our sample. Typically, a driving school and an Indian owned furniture works each employed a full-time book keeper. Other

kinds of SMMEs that undertook most types of detailed record keeping included a burial society, and two bookshops. By contrast, it was not surprising that the taverners, the sellers of cooked foodstuffs and the fruit and vegetable vendors did not keep a monitoring record of their fragile businesses.

In terms of skills used in their existing businesses, the majority of skills had been secured outside of the formal training system. Indeed, of 54 responses, the most common was that the skills were self-taught (25 responses - 46 percent). The second most common response was that "no skills were needed" (12 responses). The survey did capture, however, a group of 7 respondents who had received extension training (mostly from Agri-Eco), 5 respondents who had received on-the-job training, 4 respondents who had been through an apprenticeship form of training and one individual who had learned carpentry from a relative. In terms of formal vocational training of 51 responses, 46 (90 percent) were negative and that no such training had occurred. The only exceptions were two University graduates who were both running bookshops, two hairdressers with certificates in hairdressing and one dry cleaner with a teaching diploma. Overall, these findings indicate that the potential for improving skills is considerable both in terms of basic business skills training and more specialised technical training.

## 5. CONCLUSIONS

The objective in this study was to contribute to an undeveloped literature concerning the issues of rural SMME development in South Africa. This task was pursued through the lens of the selected case study of Phuthaditjhaba in Free State Province. It is clear that the economic downturn experienced in Free State Province and the severe decline in the local Phuthaditjhaba economy does not suggest a bright short-term outlook in terms of promoting growth-oriented rural SMME development programmes and for overcoming the important constraints of narrow market potential. Indeed, it would follow that the strategic policy emphasis in rural SMME development in the Eastern Free State should be oriented towards issues of poverty reduction.

The findings from the Phuthaditjhaba SMME research confirm some of the key issues highlighted by the Task Team *et al.*, 1997 report which investigated constraints on non-agricultural employment generation. It concluded that the core problem on SMME development, whether of survivalist, very small or SME enterprises, was "the lack of intermediaries that provide access to finance and to markets" (Task Team *et al.*, 1997:92). Such intermediaries would interface with SMME entrepreneurs to allow markets and programmes to function effectively and to link entrepreneurs to potential buyers and suppliers of inputs and

finance. Overall, the absence of such intermediaries was explained as in part an apartheid legacy, in part a consequence of poverty and in part related to expectations that government would be the saviour in providing these functions (Task Team, *et al.*, 1997:79).

The lack of intermediaries was particularly crucial in respect of SMMEs access to finance, markets and training. In relation to access to finance, the situation in the Free State was seen as especially weak "because local community-based savings and loan institutions other than stokvels are virtually absent and because apartheid widened the gulf commonly found between formal financial institutions and informal producers" (Task Team, *et al.*, 1997:79). Overall, it was found that there "is a lack of rural financial/credit oriented NGOs in the Free State Province and a total absence of credit delivery mechanisms to the people and groups who do not form part of the traditionally bankable poor" (i.e. those with conventional collateral) (Task Team *et al.*, 1997:71). Moreover, the report concluded that the capabilities of the commercial banks "were ill-suited to the SMME market" and that only "a couple of cases have been identified of non-government organisations (NGOs) and credit unions involved in small loans, and they are neither oriented primarily towards non-farm SMMEs nor able to cover their costs" (Task Team *et al.*, 1997:79-80). In addition, "stokvels and burial societies primarily serve consumption and household purposes, not businesses, although they are an important means of mobilising household savings" (Task Team *et al.*, 1997:80)

Markets and marketing were a second key area of constrained access by SMMEs. It was argued that small entrepreneurs "who want to establish a full-time business outside the home often have difficulty finding affordable venues in locations that make them accessible to buyers" (Task Team, *et al.*, 1997:79). Moreover whilst there clearly are small businesses "that could supply many products and services that are demanded in the Province, they lack adequate information and the skills to tender or solicit orders" (Task Team, *et al.*, 1997:79). Furthermore, many small businesses "who do receive orders have difficulty in obtaining the necessary inputs, for lack of local suppliers who will provide materials on credit and for lack of transport or funds to travel to a distant wholesaler. The third key area of constraint was identified as relating to business and technical skills. It was revealed that in the Free State SMME economy "the prevalence of poverty combined with the legacy of apartheid mean that both existing and would-be entrepreneurs lack the basic information and experience necessary to successfully plan and manage a business, as well as to obtain inputs and market their products" (Task Team, *et al.*, 1997:79).

The general weakness of and access to 'social capital' across the Free State emerges as another major constraining factor which retards the development of the rural SMME economy. In particular, for the unemployed and those in survivalist enterprise "they often live in impoverished communities with little source of income to support business activities" (Task Team, *et al.*, 1997:79). In order to bring in external resources and to mobilise existing resources of communities, the weakness of social capital and of community groups needs to be recognised as an important constraint that demands attention.

Based upon the responses gained from the support organisations and from the SMME community in Phuthaditjhaba, several policy intervention areas can be recommended in terms of improving SMME development, albeit sometimes only at the margins in the case of survivalist enterprise. From the Phuthaditjhaba experience, it is argued that there are five issues that merit further policy attention and investigation concerning the importance of strengthening the access of rural SMMEs to existing support networks and creating mechanisms for new support structures.

1. **Improve Access to Support Organisations** - It is clear that demand for SMME support and assistance exceeds the performance of the existing network of service providers. This means that both the existing support organisations require expansion and that there is a need to nurture new organisations to further deepen the support base available to SMMEs. In terms of new organisations, consideration must be given to the role of an LBSC in the Eastern Free State. Lastly, there is a need to promote a greater degree of networking and collaboration both (1) amongst all support providers and (2) between the group of support providers, the Free State SMME desk, NEPA and Khula.
2. **Improve Capacity to Formulate and Implement Local Economic Development** - The question of building the local capacity and to develop and operationalise programmes for local economic development (LED) is critical for the future well-being and upliftment of the SMME economy. The Eastern Free State appears little different from other non-metropolitan areas of South Africa in that LED is either absent or in its infancy. It is recommended that programmes be developed at the Provincial government level to popularise the importance of LED planning and to assist local authorities to build up their capacity. This would provide the basis for improving the capacity for local identification of promising niches for LED promotion, which would integrate with rural SMME development.

3. Improve Access to Finance and Markets - The improvement of access to finance and markets is the number one priority for rural SMME development in the Free State. As has been suggested, a critical role in this respect can be played by existing support organisations that assume the role of intermediary (in terms of providing advice and information) between SMMEs and markets and financing agencies. In addition, new financing support structures need to be examined, including the potential for involving the existing commercial banks. Lastly, serious attention needs to be given to the question of who gets access to government tenders.
4. Improve Access to Training - The role of training emerges as a key 'hidden' factor in the success of SMMEs. Support needs to be given to expand access of SMMEs to the existing training programmes and to expand the range of programmes beyond simple business skills training to include specialised business training and technical skills training. Moreover, the existing training support structures should be made more gender-sensitive and seek to avoid the channelling of women only into such programmes as dressmaking, baking or sewing.
5. Improve Access to Social Capital - Lastly, there is a need for interventions that will reinforce community development through building-up relations of social trust and community networks of support. This type of intervention, albeit critical to success of upgrading SMME development, requires programmes such as the reduction of crime, improved developmental social welfare, or public works, which fall outside of the normal sphere of SMME support programmes.

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