UNIVERSITEIT VAN PRETORIA
UNIVERSITY OF PRETORIA
YUNIBESITHI YA PRETORIA

A REVIEW OF THE SOUTH AFRICAN MICROFINANCE SECTOR, 2009

Successes, Challenges, and Policy Issues

VOLUME I – SUMMARY OF FINDINGS

FINMARK TRUST AND THE CENTRE FOR MICROFINANCE, UNIVERSITY OF PRETORIA,

March 2010

Edited by Barbara Calvin and Gerhard Coetzee

Centre for Microfinance

FINMARK TRUST
MAKING FINANCIAL MARKETS WORK FOR THE POOR

TABLE OF CONTENTS

LIST OF TABLES

LIST OF FIGURES

LIST OF ACRONYMS

ABIL	African Bank Investments Limited
ABSIP	Association of Black Securities and Investment Professionals
AEDOS	Authenticated Early Debit Order System
AMFISA	The Association of Pro-poor Micro Finance Institutions of South Africa
AMI	Applied Microfinance Institute – Africa
AMSA	Amalgamated Microlenders of South Africa
APR	Annualized Percentage Rate
ASISA	The Association for Savings and Investment in SA
ATM	Automatic Teller Machine
AULAI	Association of University Legal Aid Institutions
BankSeta	Banking Sector Education and Training Authority
BBBEE	Broad Based Black Economic Empowerment
BMR	Bureau for Market Research
BSM	Business Sophistication Measure
CBA	Cooperative Banks Act
CBDA	Cooperative Banks Development Agency
CED	Corporation for Economic Development Limited
CENFRI	Centre for Financial Regulation and Inclusion
CIPRO	Companies and Intellectual Property Registration Office
CFO	Community Finance Officer
CMF	Centre for Microfinance
CPA	Credit Providers Association
CPS	Cornerstone Performance Solutions
CSTI	Credit Skills Training Institute
CUBIS	Credit Union Banking Information System
CME	Cape Member & Employees
DAFF	Department of Agriculture, Forestry & Fisheries
DFID	U.K. Department for International Development and Cooperation
DFIs	Development Finance Institutions
DTI	Department of Trade and Industry
FAIS	Financial Advisory and Intermediary Services
FIs	Financial Intermediaries
FNB	First National Bank
FSC	Financial Sector Charter
FSC	Financial Service Cooperative
FSM	Financial Services Measures
FSS	Financial Self Sufficiency
GDP	Gross Domestic Product
GAFS	Get Ahead Financial Services
GNI	Gross National Income
HBS	Harvard Business School
HP	Hire Purchase
IDC	Industrial Development Corporation
IP	Intellectual Property
IPI	Integrated Product Intelligence
ITC	Information Trust Corporation
KDC	KwaZulu Development Corporation Limited
KYC	Know Your Customer
LOA	Life Offices Association
LSM	Living Standards Measure
MAFISA	Micro Agricultural Finance Institution of South Africa
MCP	MicroCredit Programme
MDI-NH	Microenterprise and Development Institute – New Hampshire
MFRC	Micro Finance Regulatory Council

MFSA	Micro Finance South Africa
MLAS	Microloans Administrative System
MLCB	Micro Lenders Credit Bureau
MLL	Minimum Level of Living
MSEs	Micro and Small Enterprises
NASASA	National Association of Stokvels of South Africa
NCA	National Credit Act
NCR	National Credit Regulator
NDMA	National Debt Mediation Association
NEAs	Nearest Equivalent Accounts
NEHAWU	National Employees Health and Allied Workers Union
NHFC	National Housing Finance Corporation
NLR	National Loans Register
NYDA	National Youth Development Agency
PDAs	Payment Distribution Agents
RFF	Rural Finance Facility
RFIs	Retail Financial Intermediaries
RHLF	The Rural Housing Loan Fund
RMB	Rand Merchant Bank
ROSCA	Rotating Savings and Credit Association
SACCO	Savings and Credit Co-operative
SACCOL	Savings and Credit Co-operative League of South Africa
SAM	School of Applied Microfinance
SAMAF	South African Microfinance Apex Fund
SAMWU	SA Municipal Workers Union
SAP	Systems Applications and Products
SARB	South African Reserve Bank
SEDA	Small Enterprise Development Agency
SEF	Small Enterprise Foundation
SETAs	Sector Education and Training Authorities
SIDA	Swedish International Development Agency
SME	Small and Medium sized Entrepreneurs
SMME	Small Micro and Medium sized Enterprise
SWE	Stellenbosch Wine-lands & Employees
UK	United Kingdom
USAID	United States Agency for International Development
UWC	University of the Western Cape
WDB	Women's Development Business

ACKNOWLEDGEMENTS

This study was compiled through the assistance of a large number of individuals. The wonderful team of graduate students working at the Centre for Microfinance completed the bulk of the secondary research. Damola Owolade compiled the background paper on Stokvels and the section on Market Demand, utilizing his skills with statistical packages to extract the preferred data from the FinScope studies. Sherwin Gabriel gave us the background papers on the Economic Context and the Financial Sector Charter, and got us started on all the supplier profiles. Menzie Dlamini collected information from the DFIs. Zahra Shah compiled the background papers for training institutions and information technology companies, and developed the profiles for NHFC and RHLF.

Special thanks go to the three organizations which assisted with identifying the qualifying institutions and then introduced the study to them. MFSA (Micro Finance South Africa) assisted with the salary-based microlenders; AMFISA (the Association of Pro-poor Micro Finance Institutions of South Africa) assisted with the microenterprise lenders; and the Cooperative Banks Development Agency (CBDA) assisted with the cooperative financial institutions. These organizations also contributed through the proof reading of background papers on their respective sub-sectors.

We extend our gratitude to the Centre for Financial Regulation and Inclusion (CENFRI), based at the University of Stellenbosch Business School Campus, for sharing their in-depth knowledge and compiling the background paper on microinsurance.

FinMark Trust verified all of the FinScope data included in the report and updated tables to include information from the 2009 dataset. FinMark has also been a constant and important partner, providing input and referrals and commenting on the numerous drafts.

Finally we thank all the institutions who participated in the study by completing and submitting questionnaires and sharing their corporate information with others. The success of such a review is highly dependent on the quality and accuracy of information collected; thank you for giving this study a base to stand on!

REPORT METHODOLOGY & ORGANIZATION

This Review is the latest attempt to systematically document the context, market size and characteristics, and suppliers of the microfinance sector in South Africa. For the purposes of this study, we have applied the broadest definition of microfinance: *The provision of formal financial services to low income households.* In this definition, the word "formal" refers to a formal institution as the supplier of the service.

A joint initiative between FinMark Trust and the Centre for Microfinance (CMF) at the University of Pretoria, this study encompasses multiple objectives. For researchers, government, and policymakers, it provides a useful snapshot of the microfinance landscape and highlights areas of strength and areas where further support is required. For suppliers of services to the microfinance sector, such as the credit bureau sector or banking system suppliers, it provides information on their market and their competitors which could support future strategy determination. For the microfinance institutions themselves, it provides a rich profile of the strategic context within which they operate.

It is hoped that this Review will become a biennial study, released every two years with updated data which will highlight trends and issues. In this study, we have included data up to mid 2009, with a release date of December 2009. Being the first issue, we have spent more time on compiling background information on the sector. Volume II provides a detailed background paper for each of the Review sections, for those who wish to know more about any one topic. For future Reviews, we will focus more on trends and less on descriptive narratives.

Resources available for this first issue necessitated that we focus on the primary financial services, sector players, and themes, and exclude others which we hope to cover in future issues. Over time, our objective is to make this a comprehensive compendium of all aspects of financial inclusion in South Africa.

The services which are covered in this first issue include deposit services for the low income market, microloans to salaried individuals, and microenterprise loans. A short chapter on the microinsurance sector is included in Section IV on Special Products, along with a chapter on Stokvels and Burial Societies. We have included only a passing mention of the low income housing sector and have not dealt with the growing market in remittances, both domestic and foreign.

Section I – Context, creates a profile of the external environment and factors which impact on microfinance providers in South Africa. The first five chapters focus on the broader context, such as the economic or legislative context, the role of government, and the financial sector charter. The next four chapters focus on suppliers of services to the microfinance providers, including the credit bureaux, information technology companies, training institutions, and wholesale developmental finance institutions. We hope to include additional suppliers in future, such as private sources of capital (such as equity funds and donors) as well as rating agencies and industry associations.

Information for this section was gathered initially from secondary sources, such as annual reports and websites. For the suppliers of services, we then attempted to verify information from each organization through the completion of a questionnaire. Certain organizations, therefore, are covered in more detail than others, depending on responses received.

Section II – Market Demand, creates a profile of the range of users of microfinance services. The chapter on Consumer Demographics draws on data from Statistics S.A. and the annual FinScope surveys. The chapter on Deposit Product Usage draws on the FinScope surveys to show the shift in usage of a range of deposit products over the three year period from 2006 to 2009. The chapter on Credit Product Usage equally draws on FinScope data to show a shift in usage, but also benefits from data provided by the National Credit Regulator (NCR) which reveals shifts in the overall size of the credit market. The chapter on Micro and Small Enterprises draws on the FinScope Small Business Survey 2006 to describe seven different market segments within the micro and small business market.

Section III – Market Supply, provides a profile of the six different types of organization which supply microfinance services: developmental microenterprise lenders, cooperative financial institutions, salary-based microlenders, alternative banks, primary banks, and government-owned retail Development Finance Institutions (DFIs).

In aggregate, these profiles uncover an expanding and dynamic sector with institutions catering to all levels of the micro market. The criteria for inclusion in the study are shown in the box below. For a salary-based microlender to be included, for example, they would need to meet the criterion of a minimum of 10 000 active loans outstanding. Micro loans are defined as those with initial disbursed values of less than R50 000.

Qualifying Service	**Threshold**
For banks and microlenders: unsecured salary-based loans with disbursed values less than or equal to R 50 000	Over 10 000 active loans
For banks, microlenders, or developmental lenders: micro-enterprise loans (based on self-employment income) with disbursed values less than or equal to R 50 000	Over 1 000 active loans
For banks: Mzansi or other low income savings accounts	Over 10 000 active savers
For financial cooperatives: Mzansi or other low income savings accounts	Over 500 active members

For these supplier profiles, we first sought assistance from various industry associations or regulatory authorities to identify which institutions met the criteria. We then began compiling information from secondary data, which was sent to the organization for verification and expansion. Topics covered by these surveys included: corporate history and structure; vision and mission; operating locations; products offered; banking systems utilized; and performance indicators.

For some of the sub-sectors, such as the financial cooperatives, response rates were high. For others, such as the salary-based microlenders, response rates were minimal and we were required to create a profile from a smaller sample of institutions. We believe, however, that we were able to gather enough responses to generate a meaningful profile for each type of organization. We hope that response rates will improve for future issues as organizations recognize the value of the study.

Section IV – Special Products, provides a profile of the developments with stokvels and burial societies as well as a paper on the emerging microinsurance sector.

Section V – Summary of Policy Recommendations, compiles in one place a list of all the policy issues which are raised throughout the Review.

Reminder: If you wish to know more about any particular topic, please obtain a copy of Volume II, which includes the detailed background papers for each Section, including a separate profile for each of the suppliers of microfinance services.

If you identify information in this report which requires corrections or clarifications, please send your input to the Centre for Microfinance, University of Pretoria, and attention: Katherine Blaine, at Katherine.Blaine@up.ac.za, or call 012-420-3344.

EXECUTIVE SUMMARY

INTRODUCTION

The overall profile of the microfinance sector in South Africa which emerges from these pages is one of a maturing industry, still expanding and innovating but past the early stage of rapid growth for two of the primary product categories: micro deposit services and salary-based microloans. A third primary product, loans to microenterprises, is lagging far behind, achieving less than 20% of potential market penetration. For all three primary microfinance products, this Review explores the successes and challenges and identifies possible policy initiatives which could support further progress.

This study also identifies and profiles the primary suppliers of microfinance services in six broad categories, as follows:

Not-for-profit microenterprise lenders	Cooperative financial institutions
Salary-based microlenders	Alternative banks[1]
Primary banks	Retail development finance institutions

The banks, cooperatives, and DFIs offer more than one product and are increasingly diversifying their product offerings. The salary-based microlenders and microenterprise lenders, on the other hand, have generally remained focussed on a single product offering.

Product	Micro Deposit Services	Salary-based Microloans	Microenterprise Loans
Suppliers	Primary Banks Alternative Banks Financial Cooperatives Stokvels Development Finance Institutions	Primary Banks Alternative Banks Financial Cooperatives Microlenders Development Finance Institutions	Primary Banks Financial Cooperatives Not-for-profit Microenterprise Lenders Development Finance Institutions
Stage of Development	Maturing	Maturing	Early Stage

MICRO DEPOSIT SERVICES

The proportion of the adult population which is utilizing a bank account (referred to as the *banked* population) grew rapidly from 14.3 million, or 47%, in 2005, reaching 20.0 million, or 63%, in 2008. Due to the recession and less new entrants into the 16+ age group, this figure dropped back to 19.0 million, or 60%, in 2009. Despite this drop, deposit ownership is now 84% or above for Financial Services Measure (FSM) segments 4 to 8.[2] Only FSM segments 1 to 3, with monthly incomes of below R1 000 and formal employment levels below 20%, reveal banked levels of below 50%. We can conclude from this data that deposit account ownership is now close to a saturation level.

The growth in banked individuals can be attributed to a variety of factors, but primarily to the expansion of affordable supply in areas convenient to previously unbanked populations. The range of institutions offering deposit services to the low income market has expanded in the past five years. In addition to the Mzansi initiative and other mass market offerings of the primary banks and PostBank, three smaller banks are reaching the low end market with innovative offerings.

Absa and First National Bank (FNB) lead the primary banks in number of Mzansi accounts, with 675 000 and 339 000 respectively.[3] They also actively promote their nearest equivalent low cost deposit accounts.

[1] African Bank, Capitec Bank, Teba Bank, PostBank, and WIZZIT Payments Limited

[2] According to the FinScope survey 2009

[3] According to FinScope SA 2008, total active Mzansi accounts were 3.5 million.

Capitec has the lowest fees in the banking industry and savings balances at Capitec grew R752 million, from R554 million to R1.3 billion, in the two years ending February 2009. WIZZIT has opened more than 300 000 cell phone-based accounts in the past five years. Teba Bank has expanded its defined market beyond miners and their families to also include the broader communities within which they operate.

The challenge now for the banks is to encourage higher usage of the deposit services. A fear of fees and other debits cause a large proportion of deposit holders to withdraw 90% of their funds within a few days of being paid. Deposit accounts serve one of three different needs: temporary safekeeping and transactions, short-term or emergency savings, and longer term savings or investment. Banks need to introduce operating efficiencies and new electronic access mechanisms to reduce costs and fees and thereby encourage deposit-holders to maintain and build their short-term emergency and longer-term savings balances.

With a total of 5.6 million deposit accounts, PostBank continues to play a critical role in taking savings to the rural areas. PostBank also provides critical support to group-based microenterprise lenders operating in rural areas. The potential of PostBank to improve and expand its service is substantial; further professionalisation and separation from the post office and conclusion of a full commercial banking licence would be beneficial.

Cooperative financial institutions provide an opportunity to reach deeper into rural areas with both deposit and credit services. They also appeal to a certain segment of society who prefers the developmental philosophy inherent in these institutions. In West and East Africa, savings and credit cooperatives have been highly successful and play an important role in the provision of microfinance; the story has been less encouraging in South Africa. According to the World Council of Credit Unions, the number of economically active adults who utilized a deposit account at a financial cooperative, in African countries in 2008, ranged from a high of 43% in Benin to a low of 0.1% in South Africa. Senegal and Mali both achieved 36%, while the three large East African countries ranked as follows: Kenya, 17%; Uganda, 6%, and Tanzania, 2.2%.

The cooperative sector in South Africa received a welcome boost from government with the passing of the Cooperative Banks Act, No. 40 of 2007, and establishment of the Cooperative Banks Development Agency (CBDA) in 2008, with its dual functions of supervision and development. According to the Act, cooperatives must register and be supervised as a cooperative bank once they reach 200 active members and R1 million or more in deposits. By the end of 2009, less than 20 institutions nationwide had met these criteria. The challenge for the CBDA, therefore, is to build capacity among the existing institutions and leverage from there to support the creation and development of new institutions. Hopefully the CBDA will be looking for ideas and support from our successful African colleagues.[4]

Another initiative of industry and government which was intended to support expansion of low cost and convenient savings services was that of the Dedicated Banks Bill of 2004. The intention was to reduce the amount of minimum capital required to establish a new bank, thereby creating banks which specialized in savings mobilization or savings and limited credit activities. This approach has been successful in other parts of Africa; we encourage the Registrar of Banks and National Treasury to look once again at these proposals.

[4] Supervision and development of financial cooperatives is currently split between the CBDA and samaf, as discussed in Volume II, Section I.2. This appears to be inefficient and unsustainable; we encourage government to rationalize this structure

SALARY-BASED MICROLOANS

Microloans to salaried individuals have grown dramatically since the introduction of the Usury Act Exemption in 1992, which lifted rate restrictions for loan amounts up to R6 000 and loan terms up to 36 months. In 1999, the exemption ceiling was lifted to R10 000 and the Microfinance Regulatory Council (MFRC) was created. Over the seven years of its existence, from August 2000 to May 2007, the MFRC tracked loans which qualified for the exemption. As shown in Table 1 below, these loans grew by an average annual compound rate of 15% during this period.

Table 1 - MFRC Quarterly Statistics

Loan Book (R Millions)	Aug 31, 2000	May 31, 2007	Compound Annual Growth %
Banks	5 280.5	14 628.2	15.5%
Retailers & Microlenders	5 528.9	14 194.1	14.5%
Cooperatives	130.7	388.3	16.5%
Section 21	44.2	98.0	12.0%
Total	10 984.3	29 308.6	15.0%

While the recession of 2008/09 has had some dampening effect on credit extension overall, the primary microloan categories were not affected as much as other categories. Between December 2007 and June 2009, the value of short-term credit agreements granted in the quarter grew by 5%, from R883 million to R928 million. Of these, 72% were granted to individuals with monthly incomes below R3 500 and 80% of these were 30 day loans. The number of short-term credits outstanding, however, declined over this period by 26%, from 444 000 to 352 000, and the debtors book outstanding for short-term credit dropped by 13%, from R682 million to R594 million.

The trends for unsecured credit were somewhat different. While the value of agreements granted dropped by 10% over this period, from R7.9 billion in the quarter ending December 2007 to R7.2 billion in the quarter ending June 2009, the number of unsecured credit accounts grew by 2.7% from 4.9 million in December 2007 to 5.0 million in June 2009, and the debtors book outstanding grew by 22.4%, from R40.9 billion to R50.1 billion.

Penetration levels for salary-based microloans are relatively high for the prime micro target markets of FSM 4 to 6. According to FinScope 2008, for FSM 4, 1 in 5 employed individuals have utilized a store card, a hire purchase arrangement, and credit from a big bank, and these figures rise for FSM 5 and 6.

Table 2 - Estimated Credit Usage Current and Previously, of Employed Individuals

FSM segment	Store Card	Hire Purchase	Big Bank Loan	Microlender
4	18%	19%	18%	9%
5	30%	14%	12%	10%
6	47%	20%	25%	9%
Source: FinScope 2008				

Competition for salary-based microloans is becoming intense, just at a time when profits are being squeezed by rate restrictions and new requirements stipulated by the National Credit Act (NCA), No. 34 of 2005. Once the sole domain of specialized microlenders and alternative banks such as African Bank and Capitec Bank, the larger commercial banks began entering this market space in 2007, with Absa Bank and FNB showing a particular interest. Even some microenterprise lenders are now launching salary-based loans, believing them to be a good way to cross-subsidize the more expensive microenterprise products.

Players in this market are facing serious challenges in a few areas, however, which may constrain supply or cause over-indebtedness and are worthy of continued strong attention from policy-makers. The first is the weakening status of the data held by the National Loans Register (NLR), which is now estimated to be only 70% correct (see Section I. 6). The second is the number of credit agreements in arrears for which no payments are being made due to bottlenecks either with the debt counsellors or with the Magistrate's courts. The third challenge is the lack of access to capital for the specialized microlenders, which may cause the market to be more and more concentrated among the big banks, and therefore less competitive. Lack of compliance with the NCA, particularly among selected smaller institutions, is another cause for concern. Although these lenders represent a small proportion of the total market, they can still cause hardship and distress for the most vulnerable segments of society.

MICROENTERPRISE LOANS

The microenterprise lending sector still remains woefully underdeveloped. For analysis purposes, it is useful to segment the market between the survivalist level segments (Business Sophistication Measure, BSM 1 to 3)[5], which are best served with a group-based lending methodology, and the mid and upper level segments (BSM 4 to 6) which are best served with an individual lending methodology.

The country has just three large microenterprise lending organizations[6], each with 20 000 or more active clients. Another four microenterprise lending organizations have between 1 000 and 3 000 active clients. It is instructive to explore why there are no organizations with client levels between 3 000 and 20 000.

The three big organizations all utilize a group-based methodology and active loans at their respective 2009 year ends totalled just 115 000, compared with an estimated market in the survivalist segments approximating two million microenterprises. With annual loan loss rates consistently below 5% of average portfolio, the three large organizations have proven that strong portfolio quality can be maintained utilizing a group-based methodology.

Not one organization utilizing an individual lending methodology has grown to scale, beyond a few thousand active loans, in sharp contrast with the global trend in microfinance. One reason for this is that the application of non-traditional forms of collateral and collection of these loans are particularly costly given the judicial environment in South Africa.[7]

The proven methodologies for microenterprise lending, both group and individual, tend to be labour intensive. The up-front investment required to establish an institution and reach scale, excluding on-lending capital, can be as high as R30 million or more over a five year period.[8] An inability to raise this level of *patient* capital explains why a majority of providers of microenterprise loans are sitting with small portfolios, including the smaller not-for-profit microenterprise lenders, financial cooperatives, primary banks, and development finance institutions.

For a variety of reasons, it is particularly costly to serve the microenterprise market in South Africa compared with other countries: salary levels for management and staff are higher; markets are less dense and distances are further to travel; security costs are higher; repayment discipline is harder to enforce. The Mix Market database reveals that cost levels in microfinance are higher in Southern Africa than in any other region of the world, and South Africa has the highest cost levels within the Southern African region.

Two of the commercial banks have recently entered the microenterprise lending market; Absa Bank and Standard Bank. Absa has demonstrated a substantial financial commitment, with the opening of 23 offices and the hiring and training of 64 credit officers. If Absa executives and shareholders have the patience to wait several years before realizing financial returns on their investment, this initiative could dramatically change the nature of the microenterprise finance market in South Africa.

The primary challenge for microfinance policy-makers in South Africa is to support initiatives which either reduce the cost of business for microfinance suppliers serving the informal market or provide substantial capital (equity or

[5] FinScope Small Business Survey, 2006

[6] The Small Enterprise Foundation (57 000 active loans) Women's Development Businesses (32 000 active loans) and Marang Financial Services (25 000 active loans)

[7] Investigation into Collateral Options for Lending to Micro and Small Enterprises, Vulindlela Development Finance Consultants and Kunene, Ramapala, Botha, KRB Law Firm, September 2009, FinMark Trust

[8] This period cannot be shortened easily due to the need to build internal competencies.

operational grants) to organizations in the early stages of development until they reach a sustainable level of operation. Financial support provided by wholesale development finance institutions over the years, particularly Khula and samaf, has not been sufficient or has not been delivered in a manner which builds capacity of institutions. These apex organizations have also suffered from a lack of expertise (see Volume II, Section I.9).

Samaf is the agency currently tasked with developing the microenterprise finance sector. Samaf will need to identify which microenterprise lending initiatives fulfil the key ingredients for success. Not only do they need sufficient capital, but they also need strong leadership and governance and partnerships with a variety of local and international organizations which can provide on-going access to capacity building initiatives.

A second policy priority is to review and enhance the judicial environment for alternative collateral for lending to micro and small enterprises. This will reduce losses experienced by microlenders serving the upper end of the market utilizing an individual lending methodology and will expand supply for this crucial market segment.

The lack of appropriate policy and failure of government to support the microenterprise practitioners to sustainable institutions with decent reach highlights the lack of a central or overarching policy focused on achieving financial inclusion in South Africa. This is the main requirement to bring a consistent agreed approach and link support in a coordinated way to ensure that the low-income and poor have access to quality finance, delivered in a responsible way.

STRUCTURE OF THIS REPORT

This Executive Summary has looked at the microfinance market from the point of view of the three primary products (deposit services, salary-based loans, and microenterprise loans) and certain challenges and priority policy issues have been highlighted.

The remainder of this Volume I report presents a profile of the microfinance sector and highlights policy issues according to four Sections. Section I looks at the context within which microfinance operates in South Africa, including macro level elements, such as the economic and legislative environments, and meso level elements, such as the availability of banking systems or the role of the credit bureau sector. Section II explores the client market characteristics and the demand for and usage of different products. Section III provides a profile of each of the six categories of organization which provide microfinance services. Finally, Section IV touches on the role of stokvels in micro deposit services and provides an introductory profile of microinsurance activities in South Africa. Section V provides a summary of policy recommendations.

Volume II provides a full background paper on each Section and can be used as a reference document for those who wish to explore a topic in more depth.

SUMMARY OF FINDINGS

SECTION I - CONTEXT

This Section looks at the environment within which microfinance operates in South Africa. This includes four macro level components: the economic and legislative context; the financial sector charter, and the role of government; and five meso level components: non-financial service providers, the credit bureau sector, availability of banking systems, availability of training, and the role of wholesale development finance institutions.

I.1- Economic Context

Despite accelerated economic growth in the country, which averaged 3.4% between 2000 and 2004, growing to 5% between 2005 and 2007, South Africa continues to have escalated poverty levels, with close to 40% of its population living below a poverty line of R283 per month, according to van den Berg (2009), dropping from a peak of 53 % in 1996. The Gini coefficient[9] estimated by Bhorat (2009) has increased marginally from 0.64 in 2002 to 0.68 in 2008, suggesting that the benefits of economic growth have not benefited the poorest households.

In the second quarter of 2009, there were an estimated 31 million adults of working age, of which just 13.4 million were employed, or 43%. Of this group, 60% were employed in the formal sector, 30% were employed in the informal sector, and 10% were employed as domestic workers in private households. This means that just 26% of adults of working age are employed in the formal sector in South Africa. It is this group which has fuelled the growth of the salary-based microlending over the past five years.

The nature of the microfinance sector in South Africa has been largely defined by the dual economy and the presence of structural unemployment. Despite South Africa's high Gross National Income (GNI) per capita (US$ 7 995 in 2007) and accelerated growth rates, the country is characterised by an unresponsive labour market. Structural unemployment refers to unemployment caused by the mismatch of skills offered by the workforce and skills required of available vacancies. Of all upper middle income countries reporting their unemployment statistics in 2008[10], South Africa had the second highest unemployment rate at 22.9%. Those who are better educated are able to participate in the *first* economy, while those who did not have access to education are forced to earn a livelihood in the *second,* informal economy. The history of residential segregation in South Africa also results in forgone work opportunities due to the restrictive costs of travelling to work or to look for a job opportunity.

Economic growth slowed to 3.1% in 2008 and turned negative in the last quarter of 2008 and the first quarter of 2009. Together with high inflation, particularly food and energy inflation, the economic environment has been a difficult one for microfinance institutions over the past two years, battling to contain their own costs while client arrears were rising.

Unlike mortgage bond or vehicle leasing markets, microloans are less sensitive to interest rates, so the 5.0 basis points rise in rates from June 2006 to June 2008 did not dampen credit demand significantly for the microloan categories of credit. Between June 2008 and June 2009, the repurchase rate dropped back 5.0 basis points to its 2006 level of 7.0%. This drop will also not directly affect the microfinance sector, but should enhance the environment through increased liquidity and restoration of economic growth.

I.2 - Legislative Context

Two significant pieces of legislation have been introduced in recent years which are expected to create a stronger enabling environment for the provision of microfinance services in South Africa: the National Credit Act (NCA), No. 34 of 2005, and the Cooperative Banks Act (CBA), No. 40 of 2007.

---

[9] The Gini coefficient is a measure of income inequality. A value closer to zero suggests low income inequality (which is favoured); while a value closer to one is indicative of high income inequality and a skewed income distribution.

[10] Defined by the World Bank as countries with a GNI per capita of between US$ 3 856 and US$ 11 905 in 2008

The National Credit Act: In effect since the 1st of June, 2006, the NCA was introduced particularly to improve opportunities for asset accumulation for previously disadvantaged South Africans, by 1) improving access to finance, 2) reducing the cost of finance and 3) increasing the levels of protection available to consumers. The National Credit Regulator (NCR) was established to ensure compliance.

The Act was also a reaction to certain undesirable practices which had developed in the consumer credit market. These included: negative option selling; misleading disclosure; extreme interest rates; inflated prices for goods sold on credit; extreme over-indebtedness; no effective debt rehabilitation; burdensome payroll deductions and garnishees, inflated debt collection charges; hidden profits in credit life insurance; preferential treatment for certain consumers; and unjustified blacklisting of clients.

The NCA governs all credit agreements extended to all consumers, regardless of loan size. For registered businesses, the Act applies only if the assets or turnover of the business are less than R1 million and the loan is less than R250 000. Once a lending institution reaches a portfolio of 100 or more disbursed loans or R500 000 or more outstanding, they must register with the NCR and comply with the Act.

The NCA has impacted on microlenders primarily in the following five areas: 1) lowering rates of return on loans below R10 000; 2) raising rates of return on loans above R10 000; 3) new reporting and record-keeping requirements; 4) new consumer protection mechanisms; and 5) new requirements regarding debt collection and counselling.

Overall, the Act has reduced the level of profitability of microlending and has forced credit providers to become more efficient and professional. On the positive side, however, the Act has created a level playing field and credit providers recognize that it provides necessary protection to consumers and should, over time, reduce the proportion of consumers with impaired credit records.

The Act limits the rates and fees which can be charged on loans, as set out in Chapter Five of the Regulations. Eight loan categories are defined: incidental credit agreements; mortgage agreements; credit facilities; other credit agreements; unsecured credit agreements; short-term credit agreements (loans up to R 8 000 and terms up to 6 months); developmental credit for small business; and developmental credit for unsecured low income housing. The microfinance sector is primarily comprised of the last four categories.

The allowable interest rates are linked to the Repurchase Rate set by the Reserve Bank and must be fixed throughout the life of the loan for all loan categories except for credit facilities and mortgage bonds, which have variable rates. The allowable Annualized Percentage Rate (APR), which reflects all rates and fees bundled together, drops as the loan gets larger and the term is extended. For a one month loan of R500, the APR is close to the yields previously realized by the industry of 30% per month. For a loan of R20 000 for twelve months, however, the APR drops to approximately 5% per month.

The new rate limits will have a lower impact on revenues of the microenterprise lenders as most of them charged rates which were below the new maximum levels. Most developmental microenterprise lenders were charging APRs of between 80% and 120%. It is only for loans of over R5 000 and over six months in term that the new rates may have an effect.

Prior to enactment of the National Credit Act, rates earned on loans over R10 000 were governed by the Usury Act, providing a disincentive for microlenders to exceed this loan size. Under the NCA, there is no longer a sudden drop in returns for loans over R10 000, but a gradual flow of dropping returns according to the size and term of the loan. This has resulted in an overall increase in average loan sizes and a lengthening of loan terms. This may have a negative effect on portfolio quality as longer term loans are generally more risky than shorter term loans.

The new reporting requirements include quarterly statistical returns, annual compliance and assurance reports, and annual financial and operational returns. There is also an expectation that lenders will submit daily records to the National Loans Register in order to have access to this database to comply with affordability assessment standards. New record-keeping requirements include, for example, loan applications, declined applications, pre-agreements and quotes, payments made, and collection steps taken. These new reporting and record-keeping requirements have increased costs and require a higher degree of professionalism than was the case in the past; one reason for the microlending industry rationalization observed over the past three years.

Provisions in the Act which protect the consumer are far ranging and include items such as: a requirement to provide a refund on interest owed if a loan is settled early; a requirement to provide statements at least every three months; a prohibition against false and misleading advertising; and a requirement for simple language in contracts (see Volume II, Section I.2, Annex A). Reckless lending is defined in detail, together with standards for assessment of credit capacity and consequences for the lender if they do not meet these standards. Once again, compliance in these areas requires more costly procedures and a high degree of professionalism.

The final area of significant impact on lenders is in the area of debt collection and enforcement. Prior to proceeding to legal collections a lender must provide certain notices according to specified dates and formats and must refer the client to debt counselling. The debt counselling industry is young and still struggling with a range of challenges, causing delays in the resolution of cases and frustration on the part of credit providers.

Under the Act, there is a provision to apply for a supplementary registration as a developmental lender. This registration allows an institution to apply the pricing guidelines for the two categories of loans reserved for developmental purposes; one for small business and one for low income housing. It also provides certain other compliance exemptions and provides for approval of unique affordability assessment methodologies.

Up to March 31, 2009, a total of 3 690 credit providers had registered with the NCR, of which 3 202 or 87% are microlenders and 152 credit providers have been granted a supplementary registration as developmental lenders.

The debt counselling provisions introduced by the NCA became effective from 1 June 2007. Debt counselling seeks to create a mechanism for the rehabilitation of over-indebted consumers through mediation between the consumers and credit providers. By the end of 2009, over 1 500 debt counsellors had been trained and registered throughout the country while more than 150 000 consumers had applied for debt counselling. Eight training institutions are now accredited to train debt counsellors. *The cases are not getting resolved quickly, however, and this is one area of the Act which has experienced significant implementation challenges. The NCR and others are currently spending significant time trying to resolve these challenges; we hope to see good progress before the end of 2010.*

Another partner in the process of debt counselling in South Africa is the National Debt Mediation Association (NDMA), an initiative by credit providers to combat over-indebtedness and assist consumers before they reach formal debt counselling. According to the NDMA March 2009 newsletter, out of 50 000 reported debt counselling cases up to the end of February 2009, only between 1% and 3% were brought to conclusion and sanctioned by a court order. There are obviously gaps in the system and it is these gaps that the NDMA aims to fill by partnering with credit providers, debt counsellors, and payment distribution agents.

A Consumer Tribunal was established on 1 September 2006 as an independent adjudicative body. Section 27 of the Act provides that the Tribunal may rule on matters arising from any application made to it in terms of the Act, or as a result of allegations of prohibited conduct. The Tribunal hears and decides on applications and referrals involving consumers, credit providers, debt counsellors and credit bureaux.

Despite the wide application and ramifications of the National Credit Act, implementation thus far has been smooth with the exception of the debt counselling structures. The Act has introduced considerable consumer protection and has created a level playing field and higher professionalism among credit providers, thereby contributing to a stronger enabling environment for microfinance.

Cooperative Banks Act: Cooperative Financial Institutions are regulated by one of four different bodies, depending on the size of the cooperative. The South African Microfinance Apex Fund (SAMAF) and the Savings and Credit Co-operative League of South Africa (SACCOL) are mandated to register and regulate all the smallest financial cooperatives in South Africa. Once the cooperative reaches 200 or more members and R1 million or more in deposits, the cooperative must apply for registration as a Cooperative Bank to the supervisor within the Cooperative Banks Development Agency (CBDA). Once a cooperative bank reaches deposits exceeding R20 million, they are required to apply for registration with the South African Reserve Bank (SARB).

The Cooperative Banks Act, No. 40 of 2007, is intended to improve access to financial services by providing a legislative framework allowing cooperative banks to develop and provide financial services to their members. The Act specifies prudential requirements and the Cooperative Banks Development Agency (CBDA) is establishing a supervisory capacity to monitor those who register under the Act. Prudential standards include capital adequacy, reserve requirements, loan loss provision requirements, liquidity requirements, and deposit limits per entity.

Less than twenty cooperatives nation-wide have been identified which meet the requirements for registration and are currently in the application process. This is a shockingly low figure for a country of 30 million adults, especially given the success and strength of the financial cooperative movements in West and East Africa. The table below reveals that South Africa had the lowest penetration level of credit union membership of 22 Africa countries tracked by the World Council of Credit Unions in 2008.

Table 3 - Credit Union[11] Penetration of Economically Active Populations in African Countries

Country	Credit Unions	Members	Penetration
Benin	52	1993198	43.5%
Togo	85	1250217	37.3%
Senegal	330	2744117	36.5%
Mali	132	2240963	36.3%
Ivory Coast	81	3025411	25.9%
Burkina Faso	103	1912432	23.7%
Seychelles	1	10933	17.8%
Kenya	3990	3682272	17.1%
Mauritius	105	90000	10.0%
Niger	54	533327	7.3%
Uganda	2401	880000	5.7%
Gambia	86	32022	3.4%
Lesotho	141	33339	2.6%
Cameroon	203	252629	2.4%
Tanzania	3896	480000	2.2%
Guinea-Bissau	13	17075	2.0%
Ghana	326	253863	1.8%
Malawi	60	93850	1.3%
Ethiopia	5975	477817	1.1%
Zimbabwe	53	80000	1.1%
Liberia	105	18715	1.0%
South Africa	28	14471	0.1%
Total Member Countries	**4608**	**4308288**	**5.0%**
Total Other Countries	**13612**	**15808633**	**11.0%**
TOTAL FOR AFRICA	**18220**	**20116921**	**8.8%**
Source: WOCCU 2008 Statistical Report			

It is hoped that the CBDA, working together with other government departments, will explore lessons from our African neighbours to finally give the sector the support it needs to grow and thrive.

Other Legislative Issues: Only two other legislative issues currently require attention which could have a significant impact on the microfinance sector.

The first is the legislative and judicial frameworks governing collateral options for lending to small and micro enterprises. A report on this issue was released by FinMark Trust[12] during 2009 and FinMark is now organizing a series of meetings to debate the options. *An improved collateral environment could provide a significant boost to the market for enterprise loans of between R10 000 and R100 000, which accounts for the least well served microfinance market.*

[11] Including all forms of saving and credit cooperatives.

[12] Investigation into Collateral Options for Lending to Micro and Small Enterprises, Vulindlela Development Finance Consultants and Kunene, Ramapala, Botha, KRB Law Firm, September 2009, FinMark Trust

The second area is the Dedicated Banks Bill of 2004, developed through discussions between the Policy Board for Financial Services and Regulation and the Standing Committee for the Revision of the Banks Act. The purpose of this Bill was to create space or opportunity for smaller banks to be established in South Africa as the current situation is concentrated with five banks controlling nearly 90% of all banking assets in the country. At the moment, the minimum capitalisation of banks requires an upfront investment of R250 million. The intention with the Dedicated Banks Act was to create two types of bank, Core and Narrow, which would create structures to specialise in savings mobilisation, or savings and limited credit and other products. If product range and size are contained, these entities would not pose a high systemic risk and their capitalisation requirements could be lower. *Unfortunately the Dedicated Banks Bill is still a concept. We encourage the Registrar of Banks and National Treasury to take the discussions forward*.

While several microenterprise lenders have expressed interest in obtaining deposit-taking privileges, the challenges and costs of doing this in South Africa given the current level of crime are daunting compared with other African countries which have established categories for non-bank financial intermediaries. *One alternative to explore is an expansion and enhancement of the role of the PostBank, together with agreements between the PostBank and microenterprise lenders in which deposits gathered on behalf of their clients would be loaned back to these institutions at discounted lending rates.*

I.3 - Financial Sector Charter

At the 2002 NEDLAC Financial Sector Summit, the financial sector committed itself to the objectives of broad based black economic empowerment. This commitment was encompassed in the Financial Sector Charter (FSC), which was negotiated between the sector and the Association of Black Securities and Investment Professionals (ABSIP), as representatives of black interests in the sector. This was the first voluntary charter by an economic sector to advance transformation and equitable growth. The Charter came into effect in January 2004 and was expected to run until 31 December 2014.

Institutions' compliance with the Charter is assessed by an annual rating based upon a balanced scorecard, overseen by the Financial Sector Charter Council, an independent body representing the Charter participants, government and other stakeholders. The scorecard comprises of a total of 100 points pertaining to targets in six areas, as shown in the table below. By the end of 2008, the larger commercial banks were all approaching full marks on the scorecard. Some banks, such as African Bank, do not incorporate all elements of the scorecard in their business model, such as infrastructure development. In such cases, these banks are scored only on that portion of the scorecard congruent with their business model.

Table 4 - Scores for Financial Sector Charter, 2008

	Total	**ABSA**	**FNB**	**Nedbank**	**Standard**	**African**
H.R. Development	**20**	17.7	19.9	18.3	19.2	17.9
Procurement & Enterprise Development	**15**	15.0	15.0	15.0	15	15.0
Access to Financial Services	**18**	16.4	14.5	17.3	18	4.0
Empowerment Financing	**22**	22.0	22.0	22.0	22.0	22.0
Ownership & Control	**22**	20.0	20.0	22.0	19.8	14.0
Corporate Social Investment	**3**	3.0	3.0	3.0	3.0	2.7
	100	**94.50**	**94.40**	**97.60**	**97.0**	**75.6**
Source: Commercial Bank Annual Reports						

The charter has clearly provided an impetus for the recent entry by primary banks into microfinance, and particularly the Mzansi deposit initiative. Only 8 points in the scorecard, however, are allocated to lending to the previously disadvantaged: 4 for housing; 2 for agriculture, and 2 for Small and Medium sized Entrepreneurs (SME) lending.

Microenterprise loans are excluded from the scorecard altogether. At the time of negotiation, the sector agreed with the Department of Trade and Industry that the apex fund, Samaf, would be the vehicle through which microenterprise loans would be expanded.

The Charter was signed in 2003, shortly before the Department of Trade and Industry began formalising the Codes of Conduct to ensure Broad Based Black Economic Empowerment (BBBEE) in South Africa. These codes then served as a guideline for other sector charters, but those charters signed before the Codes were not fully aligned with the rules and intention and guidelines of the Codes of Conduct. There is now agreement between all stakeholders to align all elements of the FSC to the Codes, where relevant. There is also agreement to include in the Sector Codes all elements which are specific to the Charter, such as Access to Financial Services. The topic on which agreement has not yet been reached is that of ownership. The differences between the sector and other stakeholders on this topic delayed the process to gazette the FSC as a Sector Charter. *Perhaps in any newly formulated Charter, microenterprise loans should be recognized and given some weighting*.

I.4 - Key Government Departments

All three layers of government within South Africa recognize the importance of supporting self-employment and entrepreneurship. Within the National Government, five departments in particular play a role in supporting microfinance, as shown in the box below.

National Government Department	Primary Role regarding the Microfinance Sector
National Treasury	Establishes financial sector policies Houses the Cooperative Banks Development Agency Allocates budgets to all microfinance related state entities
Dept. of Labour	Supports BankSeta which, in turn, supports microfinance through learnerships, vouchers, and a Centre of Excellence at the University of Pretoria Created the National Youth Development Agency which operates a retail microenterprise lending operation (formerly Umsobomvu Youth Fund).
Dept. of Trade & Industry	Establishes policies for the support and development of enterprises of all sizes Established two wholesale financing agencies which provide support to microfinance institutions: Khula Enterprise Finance and the South African Microfinance Apex Fund. Created the Small Enterprise Development Agency which provides non-financial support to microenterprises. Established the National Credit Act and National Credit Regulator.
Dept. of Economic Development	Samaf, Khula, and other DFIs will shift to this new ministry beginning April 2010.
Dept of Agriculture, Forestry, & Fisheries	Established the Micro Agricultural Finance Institution of South Africa to provide on-lending finance to retail agricultural schemes.

The wholesale Development Finance Institutions (DFIs) mentioned in the table are discussed later in this section. The retail DFIs are discussed under Section III on Suppliers.

In addition to these national initiatives, various provincial development corporations have become involved in microfinance, including Ithala Development Finance Corporation Limited in Kwa-Zulu Natal, the Eastern Cape Development Corporation, and more recently the Gauteng Economic Propeller. These are also discussed under retail DFIs in Section III.

I.5 – Non-financial Service Providers

A large variety of organizations provide non-financial service support to micro and small enterprises in South Africa: government agencies, non profit organizations, and the private sector.

The Small Enterprise Development Agency (SEDA) established by the Department of Trade and Industry (dti) in 2004 in terms of the National Small Business Amendment Act, is the biggest of these service providers, with 530 employees based in one or two offices per province, as well as partner organization offices and Enterprise Information Centres. SEDA was an amalgamation of the Ntsika Enterprise Promotion Agency and NAMAC Trust. For several years following the amalgamation, SEDA struggled with harmonizing products and policies as well as forming a cohesive management team. Board and management were renewed during 2008 and services appear to be improving, in both impact and efficiency.

SEDA support services are designed for businesses in the conceptualization phase, start-up phase, and expansion phase, and include such areas as: business registrations, training, mentoring, and business planning. SEDA also supports a number of business incubators in specialized fields such as information technology.

While non-financial support does not have a direct impact on microfinance services, it can contribute to a more vibrant entrepreneurial culture and does provide practical support, particularly for those businesses at the upper end of the micro market.

I.6 - Credit Bureau Sector

South Africa has a well developed credit bureau sector which has contributed to the rapid growth of the salary-based lending market over the past five years. Consumer credit information which is gathered and stored by credit bureaux includes a person's credit history with payments and defaults, a person's financial history, including past and current income and assets and financial obligations, a person's education, employment, career, professional or business history, and a person's identity, including the person's name, date of birth, identity number, marital status and family relationships, and past and current addresses.

Since past behaviour is an excellent predictor of future behaviour, access to this data allows a lender to judge both the character and capacity of the consumer without expensive assessments. Individuals are increasingly learning that a negative listing on a credit bureau reduces or eliminates their chances of accessing credit in future, providing a strong incentive to repay loans in a timely fashion.

Up to just five years ago, the microenterprise lenders did not bother with credit bureau references as their clients generally did not have access to any other credit. Recently it has come to light that self-employed microenterprise owners have obtained store cards and other microloans, as well as borrowing from more than one microenterprise lending organization at the same time. The issue of credit references, therefore, is becoming more relevant for this group.

The National Credit Act introduced the registration and supervision of credit bureaux. Up to March 31, 2009, 23 applications had been received from which 12 were approved and 9 were refused or withdrawn. The remaining 2 are still being reviewed.

The consumer credit bureau sector is separated into primary and secondary credit bureaux. The four primary credit bureaux [13] have the right to receive and host the credit payments data from the two primary sources: the Credit Providers Association (CPA) and the National Loans Register (NLR). The secondary bureaux enter into agreements with the primary bureaux to access this data. All members of the CPA and NLR are required to submit data to all four primary credit bureaux.

The CPA is a non profit user group consisting of 80 credit provider members. This membership includes South Africa's four major banks and most of the major retailers, telecommunications companies, and smaller banks. The CPA allows for consumer credit data to be shared between all members of the association, who submit 208 data files

[13] TransUnion, Experian, CompuScan, and XDS

containing 31.5 million records on a monthly basis. Once combined with NLR data, this covers almost the entire credit granting industry.

The NLR was launched by the Micro Finance Regulatory Council (MFRC) in 2000. The register contains details of loans extended to consumers under the Usury Act Exemption (loans up to R10 000 and with terms of up to 36 months). Upon establishment, the MFRC reached a reciprocal data sharing agreement with the CPA, which allowed the NLR members access to CPA information if they are in good standing with the regulator and submit loan data on a regular basis as per the requirements.
The principle of reciprocity is applied by the CPA and NLR. If a member refuses to supply data, they are then prohibited from accessing the data to assist with credit decisions. If they do not access this data, however, they could be deemed to be issuing reckless loans as they cannot confirm the current level of indebtedness of an individual.

An important step to improve effectiveness of the credit bureau sector is the integration of the CPA and NLR databases and establishment of a new entity and governance structure to host this data. Once the NCA came into effect, it was no longer necessary to distinguish between loans below R10 000 and those above, as was required under the Usury Act Exemption.

An initiative to achieve this integration was launched by the NCR, CPA, and MFSA in late 2007. Objectives and benefits included one repository for reporting and storing data and equal access by all primary credit bureaux which meet certain technical and security standards. This initiative was challenged, however, by differing objectives between the CPA and NLR members. For loans at the micro level, it is important to get daily updates of information; this is less important for higher balance and longer term credit agreements.

With replacement of the MFRC with the NCA and NCR, microlenders no longer have a legal obligation to submit data to the NLR. While some lenders continue to submit data on a voluntary basis, the quality of the data is worsening with each month and this is beginning to undermine the credit assessments performed by microcredit providers. *It has now become urgent for this issue to be resolved in a manner satisfactory to all stakeholders.*

Another limitation of the credit bureau sector is that certain categories of loans are missing from the CPA and NLR data, such as loans fully secured by pensions or private banking loans. Within 12 months, the National Credit Regulator hopes to fill this gap by launching a National Credit Register of all outstanding credit commitments per consumer and legal entity. The register will not have dynamic reporting on payments, but will simply reflect the total credit commitments per entity.

I.7 - Banking Systems and IT Company Developments

According to supplier profiles included in this report, there are now five established IT companies in South Africa which cater for the smaller microfinance institutions, as follows: Integrated Product Intelligence, the Xpertek Group, Compuscan ProLoan Group, SAP, and Fern Software. A sixth company, the Neptune Group, has operations throughout Africa and has recently opened an office in Johannesburg. With a range of savings and debtor management and related systems, costing from less than R100 000 to over R 8 million, an MFI can generally find a system which suits its needs and budget (Volume II, Section I.7 provides details on the services provided by these six companies. Banking systems utilized by the larger financial institutions were not included in this review.)

I.8 - MFI Training Institutions (MFIs)

Three training institutions in South Africa are particularly active in the microfinance sector. Cornerstone Performance Solutions and Compuscan Academy each provide a variety of courses relevant to low income salary-based lending. The Centre for Microfinance at the University of Pretoria specializes in courses relevant to lending to microenterprises as well as general management in microfinance.

Six training institutions outside of South Africa provide quality microfinance training which is relevant for African based microfinance providers and policy-makers: the Applied Microfinance Institute in Ghana; the Boulder Institute of Microfinance in Turin, Italy; the School of Applied Microfinance in Kenya; the Microenterprise and Development

Institute (MDI) of New Hampshire; the Frankfurt School of Applied Microfinance; and the Harvard Business School – ACCION leadership programme in microfinance.

Between the local and international options, MFIs can find courses which range from strategic to technical and from broad to narrow (Volume II, Section I.8 provides details on the courses provided by these organizations.)

Finding funds to cover training fees and expenses, however, is often a challenge for the smaller microfinance institutions; support and provision of bursaries is one area in which donors and governments could play a facilitating role. BankSeta has a variety of bursary options which were recently expanded to cover courses at the Centre for Microfinance; we encourage continued support in this direction.

I.9 - Wholesale Development Finance Institutions & Access to Capital

Access to on-lending capital is crucial for a financial intermediary. Institutions working in developmental microfinance which are not yet realizing a profit do not generally have access to commercial funding, such as loans from commercial banks, unless these loans are guaranteed by a donor or government entity.

The foreign donor agencies which have been most active in the microfinance field over the past ten years[14] are no longer providing the large multi-year capacity building grants which helped to build the Small Enterprise Foundation (SEF) and Marang Financial Services during the 1990s into the organizations they are today.

Government has recognized, therefore, that there is a valid role for it to play in filling the gap in the provision of on-lending funds and associated capacity building grants. Five agencies, in particular, have been established to carry out this function for the microfinance sector. The National Housing Finance Corporation and the Rural Housing Loan Fund were both established by the Department of National Housing (now Human Settlements) to facilitate housing finance for low income and rural communities. Khula Enterprise Finance was initially established to support finance to Small Micro and Medium sized Enterprise (SMMEs), particularly for those with owners from previously disadvantaged groups. In 2005, when the fourth entity was established, the South African Microfinance Apex Fund (samaf), the focus for Khula shifted to small and medium enterprises while samaf focussed on the microenterprise sector. The final agency, the Micro Agricultural Finance Institute of South Africa (MAFISA), provides funding to support small scale agriculture.

The success of these wholesale DFIs has been mixed. The mere creation of new agencies in the SMME and agricultural areas serve as an indication that Khula and the Land Bank largely failed to facilitate finance towards small enterprises and small farmers. The current decision by government to extend the Khula mandate to a retailer rather than just a wholesaler or apex institution also reflects this failure. On the housing side, the National Housing Finance Corporation (NHFC) has struggled to expand its outreach. One persistent challenge has been the building of their own internal capacity and know-how regarding how to build and support healthy retail financial intermediaries.

While Khula provided important access to on-lending capital for the three large micro-enterprise lenders (SEF, Marang, and Women's Development Business (WDB)), their product offerings for the smaller institutions ended in failure. Those institutions which did not have strong external support from a foreign donor, and relied on Khula for operational grant funding as well as on-lending capital, were perpetually undercapitalized by Khula's small short-term grants and slow approval and disbursement cycles. The Khula Start programme also did not conform to international best practices and failed to establish any large scale sustainable institutions.

Samaf has also struggled to have a positive impact on the microfinance sector. Of the 49 institutions which have received support from samaf, close to half are in the process of liquidation. The initial strategy developed for samaf was to support up to 200 village based cooperative organizations and funds were disbursed without a thorough assessment of their capacity. Over the past two years, this strategy was adjusted to focus on the stronger microfinance institutions and valuable support is now being extended by samaf to SEF, WDB and others.

[14] Such as the United States Agency for International Development (USAID), the U.K. Department for International Development and Cooperation (DFID), and the Swedish International Development Agency (SIDA)

The samaf strategy still needs to be reviewed, however, to better suit the microenterprise finance market. For the small and mid-sized microenterprise lenders, samaf policies do not allow for sufficient capital to be granted facilitating a move to self-sufficiency; the organizations are still under funded. Working as a trading entity within a Department has also been a constraining factor and less than ideal in terms of both operations and governance.

But capital alone will not create a leading institution. If the market can only accommodate eight to ten large micro-enterprise lenders, the challenge for samaf is to determine which small initiatives to support – which fulfil the ingredients for success. In addition to sufficient capital, a micro-enterprise lender needs experienced management and leadership, strong governance, and ideally a variety of relationships with international networks which can provide on-going capacity building support.

For the financial service cooperatives, the trick will be to balance financial support without the organization losing its cooperative nature. Samaf will need to work closely with the Cooperative Banks Development Agency to develop a joint strategy of support for this sector. Alternatively, it may be preferable to consolidate all support for financial cooperatives under the Cooperatives Bank Development Agency and allow samaf to specialize in supporting the microenterprise lenders.

Conclusions from Section I

As revealed by this contextual review, many supportive elements exist in the environment for microfinance in South Africa, including: a relatively stable economic environment; the introduction of the NCA and CBA; commitments embedded in the Financial Sector Charter; the mature credit bureau sector; the available choices of information technology companies and training institutions; and a commitment from government to provide support through wholesale development finance institutions.

The review also revealed a number of areas where further policy development or government support would be beneficial. These are listed in Section V of this report, together with issues raised in other Sections.

SECTION II – MARKET DEMAND

This section attempts to document the size and nature of the markets for each of the primary microfinance services, as well as estimate the degree of saturation of each market. It begins, however, with an overview of South African demographics.

II.1 - Consumer Demographics

This chapter reveals a young population with a highly skewed income distribution. Only 8.16 million or 26 % of adults of working age are employed formally, while 43% of households depend on some kind of social grant. While the level of formal employment was rising up to 2007, this trend has reversed over the past two years.

The population of South Africa is dominated by the "youth", with 42% age 19 or younger and another 27% age 20 to 34; resulting in 69% of the population under 35 years of age. Only 3.8 million, or 7.9%, of the population are pension earners at 60 years of age and older.

As mentioned in the Economic Context, the distribution of South Africa's income is highly uneven and has been getting worse over time, with a Gini Coefficient of 0.68 in 2008. According to the Income and Expenditure Survey of 2005/6, the top 20% of households in terms of income earned 72% of total household income, while the remaining 80% of households earned just 28% of total income. The top 40% of households earned 87% of total household income, while the remaining 60% of households earned just 13% of household income.

This uneven income distribution reflects employment patterns. The formal economy employs approximately two-thirds of the economically active population, from 68% in 2006, increasing to 71% in 2007, but dropping to 62% again in 2008. The informal economy and private households together employ a third of the economically active population; this ratio grows during times of economic stress.

Table 5 - Employment Patterns

Type of Employment	March 2006		March 2007		March 2008	
	0		0		0	
Formal	9042	68%	9418	71%	8157	62%
Informal	2901	22%	2646	20%	3739	29%
Private HH	1288	10%	1251	9%	1176	9%
	13231	**100%**	**13315**	**100%**	**13072**	**100%**
Source: Annual Labour Force Survey, Statistics South Africa						

With an estimated adult population of working age standing at 31 million, the table above accounts for just 42% of these individuals; the balance are either discouraged or unable to work for other reasons. This means that just 26% of adults of working age were employed in the formal sector in 2008.

As shown in Table 6 below, a total of 12.3 million social grants are paid out by the state each month, for a total of R 5.5 billion. According to Statistics South Africa, 42.5% of households receive at least one grant. Of those households, the mean number of grant recipients is 2.1 and the mean number of grant types per household is 1.3.

Table 6 - Social Grants Disbursed Monthly, 2008

Grant Type & Section of the Social Assistance Act of 2004	No. of Recipients	Amount per Month	Total Monthly (R Millions)
Child Support Grant * (S. 6)	8115074	R210 / month	R1 704.2
Care Dependency Grant **(S. 7)	107991	R940 / month	R101.5
Foster Care Grant (S. 8)	435317	R650 / month	R283.0
Disability Grant (S. 9)	1409012	R940 / month	R1 324.5
Old Age Grant (S. 10)	2216763	R940 / month	R2 083.8
War Veteran Grant (S. 11)	2019	R960 / month	R1.9
Grant in Aid (Section 12)	35896	R210 / month	R7.5
TOTAL	12322072		R 5 506.4

'* paid to a primary caregiver of a child
'** paid to a parent or a foster parent in respect of a care dependent child.

The next two topics on Demand look at the usage of savings and credit products for each of the eight market segments defined by FinScope in terms of Financial Services Measures (FSM). FSM is partially correlated with income but also reflects an individual's financial sophistication and attitudes. For a description of each segment, see Volume II, Section II.1.

Table 7 - Average Monthly Income & Distribution of Adult Population (18 and over) by FSM

FSM	2006%	2008%	Personal Income (R)	Household Income (R)
1	16.9	12.8	371	2 211
2	21.5	16.1	439	2 747
Sub-total	**38.4**	**28.9**		
3	14.4	15.9	928	2 935
4	14.5	15.9	1 361	4 123
5	14.7	15.7	2 258	6 040
6	9.3	11.7	4 334	9 518
Sub-total	**52.9**	**59.2**		
7	6.2	7.9	7 134	14 391
8	2.6	3.9	11 240	23 221
Sub-total	**8.8**	**11.8**		
Total	**100.0**	**100.0**	**2 096**	**5 725**
Source: FinScope Data 2008				

This table demonstrates that the adult population is becoming more financially active, with a 10% drop in FSM levels 1 and 2 from 2006 to 2008. The salary-based microlenders target segments FSM 3 to 6, with personal incomes from R1 000 to R5 000.

II.2 - Deposit Product Usage

The term "banked" is used to describe an individual who is actively using at least one institutional deposit service; a transaction account or a savings account.

Table 8 - Banking Status 2005 to 2008

	2005	**2006**	**2007**	**2008**	**2009**
Banked (millions)	14.3	15.9	19.0	20.0	19.6
Banked %	46.6%	51.0%	60.3%	62.7%	59.8%
Previously banked	12.3%	11.5%	9.6%	7.5%	8.9%
Never banked	41.1%	37.5%	30.1%	29.8%	31.2%
Source: FinScope data					

According to FinScope data, the banked status of individuals grew rapidly from 47% in 2005 to 63% in 2008, dropping slightly in 2009 to 59.8% This growth can be partially attributed to introduction of the Mzansi account and other low cost offerings by Capitec and WIZZIT bank, most of which do not have a monthly service fee and therefore suit individuals who work as seasonal or casual labourers. The growth in usage of bank accounts can also be attributed to rising levels of crime against businesses and the desire by employers to reduce the amount of cash held on business premises. A final explanation may be the rise in credit accounts over this same period and the requirement by many lenders, such as Capitec and the primary banks, for a borrower to hold a deposit account at the same institution.

Although the banking status is encouraging, a large number of these account holders tend to withdraw all of their funds one or two days following a pay day. Once initial Mzansi features were embellished to allow debit orders, this behaviour may have been partially offset. An individual can now, for example, initiate a debit order on an Mzansi account for a funeral insurance plan or a loan instalment, saving both time and expense.

The *Mzansi* account is an entry-level bank account, based on a magnetic stripe debit card platform, launched collaboratively by the four largest commercial banks together with the state-owned PostBank in October 2004. By

December 2008, more than six million *Mzansi* accounts had been opened[15], a significant number in a country with an adult population of 32 million. Despite 40% of these becoming inactive, today at least one in ten South African adults currently has an *Mzansi* account; and one in six banked people are active *Mzansi* customers. According to FinScope data, the Mzansi account is most popular within FSM segments 3 to 6.

Mzansi accounts are different in profile from that of the banks' respective Nearest Equivalent Accounts (NEAs) in terms of the average balances (R208 vs. R1910 per active account), average transaction activity (3.3 vs. 7.3 transactions per month per account) and monthly flows in/out of the account (R680 vs. R3000).

The table below demonstrates that the proportion of banked population far exceeds the proportion of population which is formally employed. In fact, segments FSM 4 and up, with personal monthly incomes of R1300 and higher, have been substantially saturated, with penetration levels of 87% and higher. It is only those segments with incomes of R900 and lower and formal employment levels of below 20%, which are not yet well banked.

Table 9 - Banking Status by FSM Segment

FSM categories	2008		
	Total Population 16+ (millions)	**Proportion Formally Employed**	**Proportion Banked**
1	4.1	3.7%	1.2%
2	5.1	6.0%	10.3%
3	5.1	17.3%	50.3%
4	5.1	26.6%	87.4%
5	5.0	47.4%	98.0%
6	3.7	57.4%	100.0%
7	2.5	73.3%	100.0%
8	1.2	79.9%	100.0%
	32.0		
Source: FinScope data			

II.3 - Credit Product Usage

Considering all credit categories defined by the NCR, there was an overall reduction in credit granted of 53% between the last quarter of 2007 and the second quarter 2009, a reflection of the global recession. The largest drop, however, was recorded by the mortgage market, which is not a significant component of the microlending market. The two categories comprising the bulk of the microlending market did not contract significantly during this period; unsecured credit dropped by just 10% and short-term credit grew by 5%.

Table 10 - Credit Granted by Credit Type

Agreements (R Millions)	Q4 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008	Q1 2009	Q2 2009	% change from Q4 '07
Mortgage	53139	44619	42693	33766	27188	18932	17660	-67%
Other credit agreements	32014	28143	25 783	22 ,283	22652	19008	18780	-41%
Unsecured credit	7938	7 1,58	7 ,595	7 ,656	7971	6792	7171	-10%
Short-term credit	883	792	912	1 ,013	1031	887	928	+5%
Total	**93975**	**80712**	**76984**	**64 ,719**	**58842**	**45619**	**44539**	**-53%**
Source: National Credit Regulator Consumer Credit Report								

[15] 3.8 million at the four large banks and 2.2 million at Post-bank

Looking at credit accounts and debtors books outstanding, only the short-term credit agreements showed a drop over this 18 month period, with the value of unsecured credit showing strong growth of 22%.

Table 11 - No. of Accounts and Gross Value of Debtor's Book by Credit Type

	No. of Accounts (000)			Value Debtors Book (R m)		
Agreements	**Dec 2007**	**June 2009**	**% change**	**Dec 2007**	**June 2009**	**% change**
Credit Facilities	22 137	22 089	-0.2	125 959	140 184	11.3%
Unsecured credit	4 904	5 035	2.7	40947	50 132	22.4%
Short-term credit	444	352	-26.1	682	594	-12.9%
Source: National Credit Regulator Consumer Credit Report						

Of the short-term credit agreements granted during the second quarter of 2009, 72% went to the lowest income group of R 1 to 3500 monthly income. Furthermore, 80% of short term credit granted was in 30 day loans, revealing the strength of this product.

For the unsecured credit agreements, the longer repayment terms are now dominant, perhaps reflecting an increase in consolidation loans during 2008 and a new willingness to disburse loans over R10 000. Loans with terms up to 12 months accounted for just 25% of the number of loans and just 10% of the value of loans granted during the second quarter of 2009. A majority of unsecured credits have terms of between 19 months and 36 months. This bracket represented 49% of the number of loans and 48% of the value of loans granted during this period.

Despite the drop in credit agreements granted during 2008-09, the overall book value still rose by 8.9% compared with December 2007. The 35% drop in vehicle financing (included in other credit agreements) was partially offset by a rise in the book value for mortgages and unsecured credit.

Table 12 - Credit Usage Current and Previously, 2008

FSM	% Formal Employment	Family and Friends	Store Card	Big Bank	Hire Purchase	Informal Lender	Microlender
1	3.7%	30.4%	1.9%	1.6%	0.2%	3.0%	0.7%
2	6.0%	27.9%	1.2%	1.4%	1.1%	4.1%	0.1%
3	17.3%	41.9%	4.3%	0.7%	3.0%	7.8%	0.7%
4	26.6%	45.1%	4.9%	4.8%	5.0%	9.2%	2.4%
5	47.4%	41.1%	14.0%	5.8%	6.4%	7.2%	4.6%
6	57.4%	39.9%	26.8%	14.5%	11.5%	5.5%	5.3%
7	73.3%	37.0%	30.7%	27.7%	18.7%	6.0%	7.7%
8	79.9%	27.0%	52.0%	42.1%	31.1%	2.4%	11.0%
Total %		**37.4%**	**11.7%**	**7.8%**	**6.6%**	**6.1%**	**3.0%**
Source: FinScope 2008							

The most common source of credit for all segments, with the exception of FSM 8, is family and friends, followed by store cards and a loan from a large bank. Since the market for salary-based lenders is comprised primarily of those who are formally employed, this table reveals penetration levels for the different suppliers:

- For employed individuals in FSM 4, 1 in 5 have utilized a store card, credit from a big bank, and a hire purchase arrangement (26.6/4.9) and 1 in 10 have received credit from a microlender (26.6/2.4). One in 3 borrowed from an informal lender at some point.
- For employed individuals in FSM 5, 1 in 3 has a store card, 1 in 8 has borrowed from a big bank, and 1 in 10 has received credit from a microlender.
- For employed individuals in FSM 6, 1 in 2 has a store card, 1 in 4 has borrowed from a big bank, and 1 in 5 has utilized a hire purchase arrangement.

These penetration levels are quite high, indicating that the market is approaching a mature phase and growth is likely to slow in future years.

II.4 - Micro & Small Enterprises

To assess the nature of microenterprises and their demand for financial services, this Microfinance Review draws on the Business Sophistication Measure segments introduced by the FinScope Small Business Survey in 2006. The objective of the survey was to size, benchmark and segment the market for the first time. The survey was only conducted in Gauteng, however, so interpretation of the data needs to take this into account. The study was conducted on a national basis during 2009, with results to be released in 2010.

The study developed a new methodology for segmenting this market called a Business Sophistication Measure (BSM). Seven separate segments were identified, from BSM 1 to BSM 7. Businesses were placed in a segment according to their formality, financial record keeping and compliance, use of business management tools, use of technology, and use of banking services. As one would expect, there is a significant correlation between the level of sophistication of a business and its demographic characteristics, such as type of business, location, turnover levels, and education of the owner.

Table 13 - Market Segments by Business Sophistication Measure (BSM)[16]

	BSM 1 to 3 Survivalist	BSM 4 to 6 Microenterprise	BSM 7 Small Enterprise
Total No. estimated for Gauteng	499 000 (47%)	458 000 (43%)	97 000 (9%)
Most Common Business Category	Stall traders	Unregistered indiv./ Sole Prop	CC / Partnerships
Operate Primarily From	Footpath	Home	Home/ Shop/ Office
Average Education Level	Some H/S	Some H/S/ Matric	Post Matric
Avg. No. of Employees	0.1 to 0.2	0.47 to 1.78	8.88
Avg. Annual Turnover	R9 000 to R 17 000	R 25 000 to R 120 000	R 460 000

Small businesses in segment BSM 7 are still predominantly owned by whites, although the number of previously disadvantaged owners has reached 37% and this ratio is believed to be improving each year. Businesses in segment BSM 7 are mostly registered, whereas 84% in segments BSM 4 to 6 are still informal, and 95% of the survivalist market is informal. A large majority (90%) of owners of businesses in segment BSM 7 have completed Matric or a higher qualification, whereas only 42% of owners in segments BSM 4 to 6 and 23% of owners is segments BSM 1 to 3 can claim the same level of education. While cell phone usage is high with all segments, computers and internet usage is negligible except for level 7. Clearly education and prior work experience equips a small business owner with the skills required to build a more substantial enterprise.

In the section on Consumer Demographics we saw that 3.7 million individuals are employed in the informal economy. Given that employment levels within the informal sector are very low (an average of less than one employee per enterprise), a figure of 3.7 million employed informally could indicate as many as 3.0 million individual business owners who could benefit from microenterprise finance. In Gauteng, the number in Segments 1 to 3 is just slightly higher than the number in Segments 4 to 6. In other provinces, the distribution is likely to be more strongly weighted towards the survivalist segments. As a rough estimate, therefore, we could estimate the number of microenterprises nationwide to approximate 2 million in the survivalist segments of BSM 1 to 3 and 1 million in the mid-level microenterprise segments of BSM 4 to 6.

Group-based microenterprise lending methodologies best suit the lower BSM levels, 1 to 4, whereas individual lending methodologies best suit the higher BSM levels 4 to 6[17].

[16] FinScope Small Business Survey, Gauteng 2006, Summary chart provided by Khula Enterprise Finance

[17] The overlap here is intentional

Table 14 - Banking Status and BSM

	Total	BSM1	BSM2	BSM3	BSM4	BSM5	BSM6	BSM7
Personally Banked	59%	21%	36%	38%	70%	82%	92%	100%
Business Banked	42%	0%	14%	24%	48%	65%	81%	97%
Source: FinScope Small Business Survey, Gauteng 2006								

Banked status correlates directly with BSM level, but with a significant jump from Level 3 (38%) to level 4 (70%). Of those who are banked, the majority utilize a savings or transaction account (82%), many have an ATM or Debit Card (37%), while a smaller number have a current account (21%). Only BSM 6 and BSM 7 utilize credit cards or fixed term deposits. Only BSM 7[18] has access to formal credit: vehicle finance (19%), an overdraft (22%), or a mortgage bond (7%).

Conclusions from this Section

This section highlights that the microfinance sector has done a good job of reaching the low income markets with deposit products. The salary-based lending sector has also come close to saturation with the exception of the low income housing market. It is the microenterprise sector which is lagging behind, with an estimated 150 000, or 7.5%, of two million survivalist microenterprises being served and perhaps only 10 000, or 1%, of the one million higher level microenterprises being reached.

Some salary-based loans are going to support microenterprises in households with both sources of income. In 2002, this was estimated by ECIAfrica to be as high as 27%[19]. In the FinScope Small Business survey, 70% of microenterprises reported that the business income was their sole source of income and a low proportion access loans, indicating that cross financing is not likely reaching these households.

A massive effort to support private sector microenterprise lending initiatives is clearly warranted, whether among the NGO, banking, or other sectors.

SECTION III – MARKET SUPPLY

This section provides a profile of the six different types of organization which supply microfinance services, and highlights the issues and challenges facing each: Microenterprise Lenders, Financial Cooperatives, Salary-based Microlenders, Alternative Banks, Primary Banks, and Retail Development Finance Institutions.

III.1 - Microenterprise Lenders

The criterion for inclusion in this document as a lender to microenterprises was a minimum of 1 000 active loans outstanding. With assistance from samaf and AMFISA, seven institutions were identified, six of which are group-based lenders serving the survivalist microenterprise market and one, Vengro Capital, provides seven day individual loans to micro-enterprises which buy from wholesalers[20].

---

[18] It is important to note that there is quite a jump and many major differences between BSM 6 and 7. This makes it difficult to get a clear understanding of the actors in this range from R120k to R463k turnover. Clearly more detailed work is needed here in the current detailed national BSM survey that is taking place and will report in June 2010.

[19] ECIAfrica (Pty) Ltd, Unpublished report on the application of borrowed funds, prepared for the Micro Finance Regulatory Council, Johannesburg.

[20] We are aware that other wholesaler models of lending exist which have not been included in this study due to limited resources. A separate study is currently being conducted by FinMark Trust and Rudo Consulting on Small Business Finance models in the Supply Chain with a report expected in 2010.

From the seven identified microenterprise finance institutions, three have more than 20 000 active loans each (The Small Enterprise Foundation (SEF), Marang Financial Services, and Women's Development Businesses (WDB)),and the remaining institutions have less than 3 000 active loans each (Akanani Financial Services, Tetla Financial Services, Tiisha Financial Services, and Vengro Capital).

Table 15 - Key Indicators per NGO Microfinance Institution, by order of Asset Size

	SEF	Marang	WDB	Tiisha	Akanani
Date	**Jun 09**	**Mar 09**	**Feb 09**	**Mar 09**	**Mar 09**
Total Assets (R 000)	104 126	65 718	30 177	3 123	1 822
Lending Methodology	Centre Based Group	Solidarity Group	Centre Based Group	Centre Based Group	Centre Based Group
Gross Portfolio (R 000)	91 193	28 529	23 159	2 130	1 447
Active Loans	57 425	24 522	32 078	2 136	1 782
% female	99%	95%	100%	96%	98%
Average Loan Size	1588	1163	722	997	812
Provision Ratio	1.34%	4.23%	2.0%	2.0%	n/a
PAR>30 days	0.3%	n/a	1.7%	16.8%	15.0%
Approx. F.S.S.	86%	78%	47%	110%	100%+
No. Offices	38	23	27	1	2
No. Staff	373	178	244	12	11
Clients/staff	154	138	131	178	162

Five of the seven organizations submitted company profiles (see Volume II, Section III.1, Annex A). Below is a summary of findings and a discussion of characteristics and issues facing the microenterprise lenders of South Africa.

Origins: The three large microenterprise lenders have their origins in the late 1980s and early 1990s. Get Ahead Financial Services, one of the predecessor companies of Marang Financial Services (Marang), was the first to introduce group lending into South Africa in 1987. Women's Development Business (WDB) followed in 1991 and the Small Enterprise Foundation (SEF) was established one year later, in 1992. All three organizations began as Grameen replicators, utilizing the centre based group lending methodology.

In 1993, in an attempt to address a significant increase in arrears rates at Get Ahead Financial Services, technical assistance was sought and the lending model was redesigned based on the solidarity group lending methodology developed initially in Latin America. In this model, groups of four to eight members take one loan and each member carries joint and several liability for the loan. The group operates independently; it does not combine with other groups to form a centre and does not attend monthly meetings with the credit officer. This methodology is better suited to more dense urban and peri-urban areas than it is to rural areas. It is also well suited to the mid-level micro market whose members are sometimes resistant to attending regular meetings.

Two of the smaller microenterprise lenders, Tiisha and Akanani, were launched in 1998 and received support from the Khula Start funding programme. They also adopted the Grameen model of centre based group lending, inspired by the success of SEF and WDB.

Both SEF and WDB operate two levels of credit programme: a "poverty" level programme and a "mainstream" level programme. For the poverty programmes, these institutions target women who live below half the poverty line and do not currently operate a business, but are encouraged to begin an income generating activity. In addition to credit, they are given basic business training and conduct empowerment activities during centre meetings. The mainstream programmes target women who have at least six months business experience and loan sizes are somewhat higher. At SEF, the poverty programme accounts for 73% of clients. At WDB, the emphasis is reversed, with 70% of recent disbursements accounted for by the mainstream programme.

Marang does not offer a poverty programme but, instead, has recently introduced an individual lending programme to serve clients who are graduating from group lending. Marang has also restructured through the creation of a for-profit entity which will be able to attract investors. It has recently committed significant resources to upgrade its information technology infrastructure, positioning for more rapid growth in future.

Every one of the group lenders focuses primarily on women, with females accounting for between 95% and 100% of clients. All are primarily located in rural or peri-urban centres, with Marang having a stronger urban presence than the others.

Loan Products: Each one of the group lenders provides loans of between 4 months and 12 months duration; not one has extended yet into fixed asset loans beyond 12 months. A majority offer loans of between R500 and R10 000 per group member, with a few going as high as R15 000. A large majority of disbursements, however, are below R5 000 per group member, as follows: Marang, 99%; Tiisha, 87%; Akanani, 100%, and WDB, 90%. [21]

All the group lenders utilize graduated steps for the loan sizes, which replaces the need for detailed affordability assessments. All also utilize monthly repayment schedules, but SEF requires first and second loans to be repaid in fortnightly amounts. This could be one reason for the superior portfolio quality at SEF, although fortnightly meetings may increase operational expenses.

Savings requirements play an important role in most of these programmes. At Marang and WDB, clients are required to save at least R20 per month per member in their club accounts; at SEF the required savings are R5 per fortnight. These policies encourage a savings habit, reinforce the group cohesion, and provide the group with a fund which can be drawn upon in times of hardship and in the event of a shortfall in a loan instalment.

Debtor management systems: All the group lenders have until now opted for low cost systems solutions. Marang is the first to have invested in a more powerful banking system, shifting during 2009 from MLAS to SAP All-in-one Banking Solution software. SEF is still operating primarily with a home-grown excel based database management system, but has started to investigate banking systems. WDB is operating with MLAS.

The two smaller group lenders are utilizing Pastel Partner for both debtor management and accounting functions. Akanani is planning to upgrade to MLAS upon receipt of funds anticipated this year from samaf.

Performance: All five group lending respondents have managed to survive for more than ten years, indicating that their methodologies, management, and governance have resulted in levels of portfolio quality which are sustainable. SEF, Marang, and WDB are reporting impressive portfolio quality measures with annual loss rates of below 5% of average outstanding portfolio. Tiisha and Akanani are reflecting slightly weaker portfolio at risk figures this year, no doubt related to the tough economic environment, but both are experienced in collections and are operating at self sufficient levels.

Over the two years reported on by respondents, the big three microenterprise lenders recorded total growth of 48 800 active loans, of which 29 800, or 60% was contributed by Women's Development Businesses. In early 2006, WDB held a strategic planning workshop during which they set an ambitious target to reach 60 000 clients by 2010, and subsequently hired a new Managing Director[22] to address this challenge. While WDB absorbed the client base of a few MFIs which were closing, most of the growth was realized through the opening of 22 new branches over the two year period. WDB is now consolidating and concentrating on the growth of its portfolio and improved self sufficiency levels.

Four of the five group lending respondents are close to self sufficiency. WDB is the exception, at 46%, reflecting their dramatic growth as discussed above. The self sufficiency levels for SEF and Marang have slipped somewhat in the past two years as a result of both the economic climate and expansion initiatives.

Issues and Challenges: The three large group lenders appear to be attracting sufficient donor and government support to continue growing and investing in capacity upgrades such as new management information systems. We need to ask, however, why the second tier institutions appear to be "stuck" at a client level below 3 000; what is

---

[21] Figures not obtained for the Small Enterprise Foundation

[22] Mr. Ben Nkuna, who previously held the post of Operations Director at the Small Enterprise Foundation

required to quadruple the number of clients they are serving. There are also another ten or so microenterprise lenders nationwide who are operating at levels below 1 000 active loans. What strategies will best support their growth and development and is this desirable?

Not all of the small microenterprise lenders currently in operation will necessarily fulfil the criteria or ingredients for success. In addition to sufficient capital, the winners will need an experienced managing director and a skilled financial manager and operational manager. A strong and committed board of directors is also required, along with a variety of international partnerships which will provide on-going access to capacity building initiatives. Samaf or other donors and investors will need to assess which initiatives meet these criteria and which present the highest probabilities of success. Perhaps some of the smaller players should be merged to consolidate resources and create more substantial organizations.

Another challenge reflected in our sample of institutions is the difficulty faced by individual microenterprise lenders in South Africa. Not a single organization has managed to reach scale and international levels of performance with an individual lending methodology in this country. There are a variety of reasons for this. One is the size of the upper end of the microenterprise market, which is considerably smaller and more dispersed than the survivalist level of the market. Another is a lack of funding available to those institutions who have tried to serve this market. Another is the challenging legislative and judicial environment in the country.[23] Nicro Enterprise Finance and The Nations Trust are two organizations which attempted to serve this market; both were absorbed by the newly established retail lending arm of the National Youth Development Agency (NYDA) (previously the Umsobomvu Youth Fund) in 2004. Khetani Finance and Nkwe Enterprise Finance both closed due to lack of operational grants.

The Centre for Microfinance has estimated that the South African market could support perhaps eight to ten microenterprise lenders who reach scale and self sufficiency and represent a variety of visions and approaches. Some will focus on the poverty market, as does SEF and WDB. Others will strive for larger loan sizes and commercial viability, as reflected in the strategies being adopted by Marang. Some will combine social intermediation services with credit, such as HIV-AIDS programmes or business training. Others will want to add other financial services, such as microinsurance and remittances and savings.

The three large group lenders have all received significant investments from donors and government over the years, as well as benefiting from strong leadership and governance and strategic partnerships with international microfinance networks. How can these lessons be replicated to support the smaller institutions? What is the role of samaf in this challenge? What is the role of international players? And which other types of models are emerging? How can these organizations raise the R30 million and more in grant funding (excluding on-lending capital) required to reach 20 000 or more active loans?

During this review, two commercial banks were identified as making serious investments in microenterprise finance. They are spending shareholders funds to build capacity in this market. Will the shareholders be patient enough to wait three to five years for a return on their investment? Should these commercial players be supported with incentives from government or donors? All of these issues need to be explored to develop a broad policy to support the sector.

III.2 - Cooperative Financial Institutions

The criterion for inclusion in this document as a financial cooperative was a minimum of 500 active members. The Cooperative Banks Development Agency was consulted to identify institutions which meet this threshold.

A total of twelve institutions were identified; ten of which participated in this survey, as shown in Table 15 below. The two SACCOs with R20 million or more in deposits, which are required to register for regulation by the Reserve Bank, do not appear here as they have less than 500 members and operate at levels above the micro market. Of the cooperatives listed below, those who are members of SACCOL, the South African Savings and Credit Cooperatives League, use the name SACCO. Those who are not SACCOs are called Financial Service Cooperatives (FSCs) and tend to be village/rural based organizations. Most SACCOs which started as organizations serving workers of one or

[23] Investigation into Collateral Options for Lending to Micro and Small Enterprises, Vulindlela Development Finance Consultants and Kunene, Ramapala, Botha, KRB Law Firm, September 2009, FinMark Trust

two industries, have broadened their “common bond” to include individuals residing, working, or worshipping in a certain geographic area.

Table 16 - Key Indicators per Cooperative Banking Institution (as at most recent financial year end)

	Location	No. Staff	No. Deposit Acts % female	Deposit Balances (R)	No. Loans % female	Gross Loan Book (R)
Alrode SACCO	Alrode, Gauteng	3	3 328 n/a%	10 321 013	909 n/a%	9 719 353
Beehive SACCO	Lydenburg, Mpumalanga	4	1724 45%	547 337	4 75%	11 618
Disaneng FSC	Disaneng, North West	4	649 70%	831 600	87 59%	n/a
Ditsobotla SACCO	Ditsobotla, North West	4	1420 35%	5 393 413	769 22%	4 840 367
Mathabatha FSC	gaMathabatha, Limpopo	4	1927 49%	556 684 (Total Assets)	646 94%	396 032
Motswedi FSC	Motswedi, North West	6	2 632 72%	5 278 000	n/a	n/a
NEHAWU SACCO	National, Nine Provinces	3	n/a	1 011 759 (Total Assets)	n/a	n/a
SAMWU SACCO	National Nine Provinces	2	5 290 n/a%	3 440 882	2 391 n/a%	2 160 400
Sibanye SACCO	Cape Metropole District, WC	7	3 842 40%	4 429	n/a 38%	4 505 007
SWE SACCO	Stellenbosch Western Cape	3	806 70%	301 899	181 55%	159 357

Origins and Profiles: While Alrode, Motswedi, Sibanye, and Ditsobotla go back as far as the mid 1990s, a majority were registered in 2000 and 2001, partly due to support received from donors through two support organizations, Finasol and the FSA. Motswedi is the only cooperative which does not, as yet, provide credit to members; member savings are rather placed in interest bearing investments. Two of the cooperatives operate on a national basis through union memberships: the National Employees Health and Allied Workers Union (Nehawu) and the SA Municipal Workers Union (SAMWU). Only one of the Cooperatives has more than one office, Sibanye, which was formed through the merger of three cooperatives and currently works from four different locations. Ditsobotla was also born out of a merger of three separate SACCOs.

Deposit Products: One of the primary objectives of SACCOs is to encourage a savings culture among members and assist members to break free from borrowing from money-lenders. Most of the cooperatives provide a basic savings account as well as special purpose and contractual savings accounts, particularly for Christmas or educational savings. They generally offer nominal interest rates which are higher than those offered by commercial banks, but they may only credit the interest on an annual basis and based on minimum monthly balances. A few also offer fixed time deposits for 3, 6, and 12 month terms.

Lending Products: Some SACCOs, such as Alrode and the union-based SACCOs will only lend to salaried individuals. The FSCs lend also to micro-enterprises, partially due to encouragement and on-lending funds provided by samaf over the past three years. Most cooperatives offer a short-term loan with terms up to 12 months. A few offer longer terms of 18 or 24 months. Only Alrode mentioned loans up to 60 months. Most cooperatives also offer emergency loans of less than R1 000, which are repaid over one to three monthly instalments.

Cooperatives generally reflect a commitment to equity in their lending policies, as reflected in Sibanye’s policy shown below:

The maximum loan amount that can be borrowed by members is R25 000. However any amounts above this cap can be considered by the board of directors depending on availability of funds and members ability to repay the loan. Loan applications shall be considered in the order in which they are received provided that whenever there are more *applications for loans than there are funds available; preferences will be given, in all cases, to smaller loans, members who have never borrowed before, new members who have qualified for a loan, and members who have cleared their first loans. Sibanye SACCO*

Most cooperatives require members to save prior to receiving a loan and maintain a minimum amount of 33% of the disbursed loan amount in their account during the life of the loan.

Information Technology: Of our sample, five cooperatives utilize the CUBIS System (Credit Union Banking Information System) provided by Fern from Ireland. Four cooperatives utilize a manual record-keeping system.

Performance: It is not possible to draw general conclusions on performance from our sample of ten institutions. Several of them did not provide complete financial information; others provided figures which were not consistent or reliable and had to be omitted. It appears that a majority of institutions did grow slowly but steadily over the past three years, but profitability declined, particularly in the last reported year. Data is not sufficient to comment on loan portfolio quality.

Issues and Challenges: Given that cooperatives are member driven, their product range and design is a good indicator of what the microfinance market desires: regular liquid savings; contractual savings; loans up to 12 months; and emergency loans. These institutions also approach their business with a commitment to equity and upliftment of the previously disadvantaged; these are the strengths of the financial cooperative movement.

A few of the cooperatives have reached a level of scale to support a more professional institution: the hiring of professional staff and bookkeepers, the implementation of a banking system, and the diversification of products. Others, however, have struggled to reach this level of operation. Those who are members of SACCOL have benefited from support in these areas; the Financial Service Cooperatives are operating in isolation of strong institutional development support.

A number of cooperatives have maintained pricing policies on their loans which do not conform to the new NCA guidelines. It appears from our survey that others do not maintain monthly financial statements and debtor management reports. Clearly the development of skills in these areas will be critical for the industry as it matures. The new Cooperative Banks Development Agency was established to address these issues; we look forward to documenting their progress in the next biennial Microfinance Review in 2011.

III.3 - Salary-based Microlenders

The criteria for inclusion in this document as a dedicated salary-based lender was a minimum of 1 000 active borrowers in South Africa. With assistance from Micro Finance South Africa (MFSA), we identified fifteen organizations which meet this threshold:

AMSA	Elite Group (Subsidiary of African Dawn)	Onecor / SA Micro Loans *
Atlas Finance *	Mafori Finance *	People Society
Bayport Financial	Maravedi	Real People
Blue Financial Services *	Metrofin	Surecard
Credicor	Net-1	Thuthukani *

Due to the highly competitive nature of this sector, together with the private ownership structure which dominates, just five of these organizations participated in the survey, as indicated by the asterisks. Despite the small sample size, however, these five organizations represent a broad range of approaches and present a useful profile of the sector, as discussed below.

Table 17 - Key Indicators per Microlending Institution

	Date Established	Head Office	Branches in SA
Blue	2001	Pretoria	178
Onecor	N/A	Pretoria	** 100
Atlas	1994	Johannesburg	87
Mafori	2005	Gauteng	** 11
Thuthukani	1998	Pretoria	62

** Primarily agent offices

The primary target market for microlenders is the low-income wage earner represented by LSM segments 3 to 6, earning between R1 500 and R10 000 per month.

The sector began its rapid growth during the mid 1990s, with introduction in 1992 of the first exemption to the Usury Act for loans under R6 000 and fuelled by consumer optimism following the end of apartheid. It received a significant boost in 1999 with the lifting of the exemption ceiling to R10 000 and the creation of the MFRC. The Usury Act Exemption Notice of 1999 provided for a complete removal of rate restrictions for those lenders who registered with the MFRC, thus allowing much stronger returns to be made by microlenders.[24]

Profiles: From our sample, Blue Financial Services represents the aggressively managed organizations with assets approaching R1 billion or more, which have listed on the Alt^{X} board of the Johannesburg Securities Exchange over the past five years. Other organizations in this group include African Dawn and their subsidiary the Elite Group and Finbond. Real People (assets of R2.3 billion) is in this same size category but is still privately owned.

These organizations primarily operate through their own branches (rather than agents) and have diversified into a broad range of products. In addition to the standard personal loans of 1 to 36 months, they have launched longer term personal loans, home improvement loans, education loans, and cellular loans. Blue and Real People have also launched a range of insurance services for the low income market, including life and funeral cover, building insurance, house content insurance, medical insurance, accidental death, and vehicle insurance.

Onecor represents the larger privately owned organizations which distribute their services primarily through a network of agents. This group offers a more narrow range of personal loan products, primarily unsecured and short term loans from 1 to 12 months.

Atlas and Thuthukani represent the mid-sized privately owned organizations which distribute their services primarily through a network of branches. In some cases, such as with the Amalgamated Microlenders of South Africa (AMSA), each branch is owned by a franchisee which benefits from brand awareness and other support services provided by the franchisor. In other cases, such as with Atlas, the branches are wholly owned by the parent company family and management. Thuthukani employs an interesting combination of wholly owned branches plus branches which 50% are co-owned by a franchisee. This group of organizations also offers a more narrow range of products than the publicly owned giants, primarily consisting of personal loans from 30 days to 36 months.

Mafori represents a group of black–owned and development oriented salary-based lenders which have emerged more recently, over the past five years. These organizations have grown with the support of grants and investments from donors and government, as well as tender preference for employer based payroll loan services, although most are not yet close to the threshold for inclusion in this report. Some of these organizations are launching pilots in microenterprise lending in addition to their salary-based loans. It will be interesting to see how this group evolves and impacts on the industry overall.

Distribution Channels: There are five unique distribution channels employed by the salary-based lenders and many organizations utilize more than one of these models: own branches/offices/stores; third party branches/stores (such

[24] The Usury Act was replaced by the National Credit Act of 2005; rate limits are now governed by those included in the Regulations to the National Credit Act, see Section I.2

as in retail outlets); call centres with direct marketing outreach; agent/broker model; and employer or union based payroll lending.

The advantages of working through agents include rapid growth and low capital costs. The disadvantages include low client loyalty, the risk of losing business more easily, and higher operating costs due to agent commissions. Payroll lending tends to be the least risky.

Lending Products: Most salary-based lenders offer three basic types of personal loans:

- 30 day loans of from R50 to R3 500 to cover for food and medical and other emergencies. The average loan size for 30 day loans is approximately R600.
- 2 to 12 month loans of from R500 to R10 000 to cover for emergencies, rental deposits, funeral expenses, and school fees. The average for these loans is estimated to be R3 500.
- 12 to 60 month loans of from R3 000 to R60 000 to cover housing improvements, purchase of fixed assets, or for consolidation of existing loans. The average for these loans is estimated to be R8 000.

Blue Financial has been a leader in product innovation, perhaps hinting at the likely direction for the industry as a whole. In addition to the standard products listed above, Blue has developed a cellular loan for the purchase of mobile handsets, a home improvement loan from R1 000 to R15 000 over up to 36 months for the purchase of supplies to expand a building structure, and a pension or provident fund linked home loan.

Performance: While Blue and Mafori grew rapidly from fiscal year end 2008 to 2009, fuelled by new investor funds, the three other sample organizations remained flat or realized a modest growth, likely reflecting the global economic downturn.

Provisions for losses ranged from 3% of gross loan portfolio to 40% of gross loan portfolio, reflecting a wide range of risk appetites and portfolio quality performance. Those organizations at the lower end of this spectrum are proving that portfolio quality can be maintained in lending to low income wage earners despite the economic environment.

Profitability of our sample organizations also reflected a wide range, from a low of -50% return on equity to a high of 35% return on equity in the most recent fiscal year.

A recent announcement from Blue Financial may be a reflection of performance for the higher risk organizations: Blue Financial posted a loss of R162.3 million for the six months to August 2009, down from R51.5 million profit in 2008. The group's loan book was R1.2 billion at the end of August, compared with R1.37 billion in February. Non-performing loans increased from 6%, or R54 million, at the end of February, to 23%, or R365 million, in August 2009.

Profitability has come under pressure over the past three years with introduction of the National Credit Act (see Volume II, Section I.2). Compliance with the Act has resulted in higher operating costs and lower rates and fees being realized on loans below R10 000, and these pressures have been exacerbated by the recession.

While the Act may reduce the attractive profits earned by the sector in past years, some of our sample organizations are still earning solid commercial rates of return, demonstrating that the Act should not threaten the viability of the industry, particularly those more efficiently run and managed on a more conservative basis.

Issues and Challenges: The sector has faced significant challenges over the past three years as a result of increasing competition, the global economic recession, and introduction of the NCA. Commercial banks are placing more branches in township areas and are increasingly moving into the personal microlending market. The alternative banks, such as Capitec or Teba Bank, are providing particularly strong competition with their strategic advantage of low cost deposit service offerings.

In response, the industry has been consolidating through mergers and acquisitions and the resultant mid-sized companies are looking to diversify their product range. The industry association, Micro Finance South Africa, has been working hard to support professionalisation of the industry and compliance of members with the NCA.

Other challenges currently faced by the industry have already been mentioned, including the weakening quality of NLR data and dealing with teething problems of the debt counselling sector. The slower than average Magistrate's

Court proceedings is another serious threat to the cash flow of microlenders and banks alike. A final serious challenge for salary-based lenders is a lack of access to capital for on-lending. The commercial banks are hesitant to lend significant funds to companies in a competing business and most are too small to go to the capital markets directly. The creation of an investment funding vehicle is currently being considered by the MFSA.

III.4 - Alternative Banks[25]

This section provides a profile of five banks which are dedicated to serving the low income markets, including African Bank, Capitec Bank, PostBank, Teba Bank, and WIZZIT Bank. All but the PostBank provided company profiles for inclusion in this report, as found in Volume III.4 - Annex A. For the PostBank we have included only information derived from secondary sources.

Table 18 - Key Indicators per Alternative Banking Institution, by order of Asset Size

	African Bank	Capitec Bank	Teba Bank	WIZZIT Bank	PostBank
Date	Sep 08	Feb 09	Feb 09		
Total Assets (R millions)	17 339	4 969	3 089		
No. Offices	478	363	96		2 500+
No. Staff	3426	3414	930		
No. Depositors	n/a	n/a	484 594	300 000+	
Total Deposits (R millions)	n/a	1 571	2 300		3 296
No. of Active Loans	2 196 000	3 500 000	99 828		
Gross Portfolio (R millions)	15 818	3 195	669		
% female	n/a	54%	n/a		
Average Loan Size	7 203	913	6700		
Provision Ratio	16.3%	7.5%	19.9%		
Return on Equity %	60%	27%	8%		
Source: Annual Reports and Survey Returns					

Origins and Profiles: Of the five banks profiled in this section, African Bank most closely resembles a microlender, as described in the previous section. African Bank was established in 1998 through the merger of the original African Bank, a small developmental bank, with three microlending organizations: King Finance, Unity Financial, and Alternative Finance. African Bank has chosen not to provide savings services but to fund its lending activities through wholesale markets. With over 2 million loans, a portfolio of R15.8 billion, and consistently high returns, African Bank is the recognized leader in salary-based lending.

Capitec Bank was established in 2001, also through a merger of several microlending organizations. Unlike African Bank, however, Capitec has chosen to provide a full range of banking services and has been aggressive in the development of low cost and technology driven savings and transaction services. Through the Global One Facility, Capitec offers the most competitive banking rates and fees of any institution in South Africa, including free point of sale transactions. While still just one third the size of African Bank by assets, Capitec saw the highest growth rate of our sample in the year ending February 2009, with 69% growth in total assets, while remaining profitable.

Teba Bank was operating under an exemption to the Banks Act since 1976 through an entity called Teba Cash, until it acquired a full banking license in 2000. The bank is wholly owned by a trust managed by the National Union of Mineworkers and the Chamber of Mines. Teba initially provided basic financial services, such as facilitating

[25] For analysis purposes, this study groups the big four commercial banks under the name “Primary Banks” and the smaller banks which target the low income market under the name “Alternative Banks”. While WIZZIT is not itself a bank, it is allowed to use the bank name as an agent of the South African Bank of Athens.

remittances from miners and their families. Today, the bank offers payroll solutions for gold and platinum mines, savings accounts, fixed deposits, microloans, home loans, ATM cards and funeral insurance. Their target market has expanded beyond mineworkers to also include their families and communities. The low profits earned by Teba reflect its ownership structure and the similarity between Teba's objectives and those of the financial cooperatives described previously.

WIZZIT Payments Limited was established in March 2005 and has an alliance banking relationship with The South African Bank of Athens Limited, utilizing their banking license to support cell phone-based transaction accounts extended to the unbanked. A sister company, RQubed Consultants, developed the EVEREST Mobile Commerce Solution ("EVEREST") which is a fully functional mobile commerce and cell phone banking platform. EVEREST gives a bank the ability to offer its customers a world-class cell phone banking service. In addition to applying this technology at WIZZIT in South Africa, RQubed has sold the technology to clients worldwide.

WIZZIT account holders receive a debit card which can be used at any ATM or point of sale device which uses a Maestro card. Through their cell phones, clients can obtain a balance, make a payment to another account holder, make pre-payments and pay bills. A call centre is available to provide assistance and answer queries. It is WIZZIT's vision to evolve into a full service bank for the low end market. To this end, WIZZIT has been investigating the launch of both consumer and microenterprise credit products. WIZZIT has not yet generated a positive return for its shareholders, but is supported by investors with a development agenda, including the International Finance Corporation, OIKO Credit, and the AfriCap Fund.

The Post Office Savings Bank (PostBank) is a deposit taking institution which offers savings and transactions services through the more than 2500 post office branches and outlets in the country. It has been operating as a division of the South African Post Office since 1991 but is in the process of registering a commercial banking license. The PostBank does not offer credit services directly, but allows Bayport Financial to sell microloans through selected outlets. The PostBank plays a critical role in extending banking services to the people of South Africa, particularly in rural areas. It also plays an essential support role to the microenterprise lenders who require group members to make repayments at a local bank.

Savings Products: Teba Bank and PostBank both offer a traditional array of deposit services, including a transaction account with a debit card, a savings account which offers higher interest rates, and fixed term deposits for balances of R1 000+ or more. Teba fixed deposits begin with terms of one month whereas those for PostBank begin at 6 months.

As mentioned above, the deposit services for Capitec and WIZZIT are not conventional. With the Capitec Global One account, up to four separate savings "pockets" can be opened, either fully liquid or with fixed terms, and can be labelled to indicate different objectives (school fees or wedding for example). WIZZIT has focused on ease of access through cell phone technology.[26]

Loan Products: Each of the three alternative banks which offer credit services, African Bank, Capitec Bank, and Teba Bank, offer the standard range of unsecured personal term loans which are also offered by dedicated microlenders, but with slightly different amounts and terms as reflected below:

	African Bank	**Capitec Bank**	**Teba Bank**
Maximum Loan Size	R 30 000	R 50 000	R 12 000
Maximum Term	60 months	36 months	24 months

African Bank also offers two credit cards; a blue card with credit limits up to R8 000 and a gold card with credit limits up to R20 000. The balances on these cards are still small, however, representing just 6.5% of the total portfolio outstanding.

Teba Bank also offers a "Create a Dream" home loan of up to R350 000 over a maximum period of 10 years. This loan can be used to purchase or expand a house and is secured by a pension or provident fund.

[26] The primary banks are also now offering cell phone facilities on their savings accounts and PostBank is in the process of implementing this.

Performance: The three sample organizations which provided detailed financial data have all performed well over the past few years. All recorded positive income figures in the last financial year included in our schedules, with African Bank maintaining its high level return on equity at 60% and Capitec recording a respectable 27%. Teba's profits are more modest at 8% ROE.

All the sample organizations also recorded strong loan portfolio growth, with 45% for African Bank, 47% for Capitec, and 32% for Teba Bank. Although African Bank's portfolio at R15.8 billion is almost five times greater than that of Capitec, at R3.2 billion, Capitec has 60% more loan accounts (3.5 million compared with 2.2 million). With an average loan balance of just R900 for Capitec, compared with R7200 for African Bank, it appears that Capitec is reaching further down-market.[27]

Despite the tougher economic environment, the financial statements do not reflect any perceivable weakening of portfolio quality over the past few years. Capitec's provision ratios per loan portfolio are the strongest, at between 6% and 12%, followed by African Bank at between 14% and 22%. Teba has the highest provision ratio at 19%.[28]

Issues & Challenges: The alternative banks are well positioned to take advantage of the growing acceptance of institutional financial services among the previously unbanked segments of the population. Capitec recorded an 86% growth in deposit balances in the year ending February 2009, while the number of branches grew by only 10% in the same period. Given that a primary reason for the reluctance to use institutional deposit services is the fear of high bank fees, Capitec's strategy of low fees may explain this success.

With the commercial banks moving into low income salary-based lending, and the microlenders growing and becoming more professional, African Bank will be facing tougher competition over the next five years. They will also need to maintain competitive pricing and service to hold on to their customers.

Not one of the alternative banks has moved into microenterprise lending beyond the pilot stage, despite the fact that two primary banks have done so. It will be interesting to see if this changes over the next few years.

III.5 - Primary Banks[29]

This section provides a profile of the mass market initiatives of the four large banks: Standard Bank, Absa Bank, First National Bank, and Nedbank. Products covered include low income deposit accounts, personal microloans, and microenterprise loans.

Entry into Mass Market products: From our survey, Absa Bank and FNB appear to be the two banks most committed to the mass market. At Absa, low income groups are a segment of the Retail Banking and Unsecured Lending Divisions. Absa has actively promoted its Mzansi and Flexi accounts and has been developing electronic banking solutions to reduce costs for the low income markets. In 2006, ABSA moved aggressively into microlending to salaried individuals and in 2008 into microenterprise lending for self-employed individuals.

At FNB, products aimed at the mass market, defined as the segment of individuals earning less than R100 000 annually or R8 333 monthly, are grouped under the FNB Smart brand. Microloans were introduced as early as 1999. The Smart Account is a savings and transaction account for the mass market, offered together with the Mzansi account.

[27] Although a majority of these loans are for 30 days.

[28] Provision ratio = total provision balance on the balance sheet / total gross portfolio

[29] For analysis purposes, this study groups the big four commercial banks under the name "Primary Bank" and the smaller banks which target the low income market under the name "Alternative Bank".

Table 19 - Key Indicators per Primary Banking Institution[30]

	Standard Bank	ABSA Bank	First National Bank	Nedbank
Date	Dec 2008	Dec 2008	June 2009	Dec 2008
Total Assets (R millions)	1 509 459	773 758	809 851	567 023
Total Equity (R millions)	105 143	52 966	52 097	40 073
Return on Equity %	18.2%	23.4%	13.0%	17.7%
Total Branches	n/a	975	712	444
Total ATMS (own)	n/a	5044	4800	1 747
Total Other Outlets	n/a			781
No. Mzansi Accounts	8 074	673 112	339 043	n/a
Mzansi Deposits (R m)	R2	R168	R110	n/a
Average Balance	R248	R250	R324	n/a
No. Other Mass Market Accounts	n/a	4 260 523	118 416	n/a
Other Deposits (R millions)	n/a	R 9 731	R887	n/a
Average Balance	n/a	R 2 284	R 7 490	n/a
No. Personal Microloans	n/a	n/a	n/a	n/a
No. Microenterprise Loans	n/a	2 844	nil	nil
Gross Portfolio (R 000)	n/a	2 900	nil	nil
Average Loan Size	n/a	1 020	-	

Standard Bank has launched initiatives to reach the low income market going back as far as 1994, such as the E-Banking programme and a microenterprise lending pilot in Soweto. Due to budgetary and operational challenges, the microenterprise initiative was not sustained while E-Banking was rebranded and combined with other divisions. Following industry commitments to the Financial Sector Charter in 2005, the Community Banking Division was established to renew and coordinate efforts to reach the under-banked population, including anyone earning up to R8000 per month.

Nedbank is not targeting the microlending market for either salary based individuals or microenterprises; very few loans have been disbursed below R50 000. Nedbank is committed, however, to serve the middle and higher income consumer markets with convenient savings and transactional services.

Deposit Products: All four primary banks are participating in the Mzansi deposit account initiative, together with the PostBank. Common features were developed by this group to make these accounts accessible, including: low balances to open the account; no monthly fees; no requirement for proof of residence; and a certain number of free or low fee transactions per month. In order to prevent these accounts from being used for money laundering purposes, account balances may not exceed R15 000 and daily transactions may not exceed R 5 000.

The banks view these accounts, however, as highly costly and unattractive and generally attempt to sell their Nearest Equivalent Accounts (NEAs) in their place (see Volume II, II.2 Deposit Product Usage). They impose stiff penalty fees if a customer exceeds the number of low cost transactions in a month, reducing the appeal of the product for the low income groups.

---

[30] Comparative data was not provided by the banks for the personal microloan portfolios

Standard Bank's primary mass market deposit product is the *Community Banking Transactional Product:* This is a card- and mobile-based transactional account with no monthly charges. A mobile phone application provides a platform for payments, prepaid purchases and account information. A debit card is also issued which can be used at all existing bank infrastructure. An additional distribution channel has been implemented in the form of in-community retailers that allow customers to do transactions within walking distance from their homes. The transactions are priced at a 1% *ad valorem* with a minimum of 10c and a maximum of R10. A dedicated savings pocket has now been designed. Standard Bank also offers an Mzansi deposit account and money transfer product, as well as the MTN mobile money account and money transfer products.

The Absa Flexi account is a card-based low-cost transaction and savings account. A R50 minimum opening balance is required. Free funeral cover is provided to clients ages 18 to 65, and other free services, including legal assistance, emergency medical evacuation and funeral support, are provided, subject to the minimum balance requirement being fulfilled. Absa also offers the Sekulula card, aimed at social grant beneficiaries, which credits accounts with their grant receipts on the first working day of each month, eliminating the need to wait in queues to receive their grants.

The FNB Smart Account also offers free cell phone banking and use of the free InContact service, and has a wider range of features than the Mzansi product, such as free cash deposits and balance enquiries at FNB ATMs, as well as free prepaid airtime purchases through the bank's telephone, cell phone, online and ATM channels. Free funeral cover to the value of R1 000 or R10 000 (depending on the account pricing option) is offered to accountholders with a positive balance.

Loan Products: Absa and FNB are the most aggressive in pursuing microloans to salaried individuals; Absa is the undisputed leader so far in microenterprise lending.

Absa's Personal Loan Business Unit was established in February 2007. It offers Micro Loans ranging from R3 000 to R15 000 with terms from 12 months to 60 months, and Personal Loans from R15 000 to R150 000, with terms from 12 months to 84 months. Sophisticated risk- based pricing models are applied to both products to price the product according to the specific credit risk of each customer.

The ABSA Microenterprise Finance Division was launched in November 2007. By December 2009 it had opened 7 branches dedicated to group lending and 16 branches dedicated to individual lending, with a total of 64 loan officers and 124 staff.

The group loan product utilizes the centre group methodology. Clients form groups of five which are then combined into centres and meet on a monthly basis. Loans range from R1 000 to R5 000 per group member and are repaid over a period of between 4 and 12 months. Clients open a club account into which the group loan is disbursed. Repayments are made by the group at the bank branch, with deposit slips being submitted at Centre Meetings.

The individual loan product provides loans from R1 000 to R15 000 over a period of between 6 and 12 months. Microenterprise owners must have a permanent place of business and a minimum of 12 months' business experience. A Community Finance Officer (CFO) visits the home and place of business to conduct an assessment and compile financial statements. Approval is done at head office following a recommendation from the local credit committee.

The FNB Smart Spend Loan is a credit facility offered to employed individuals who have had an active bank account for at least three months, earning a take-home pay of at least R750 per month. Loan amounts start from R2 000 to a maximum of R15 000 over a period of between six and 60 months, and may be used for any purpose. A one-month payment holiday is allowed every January, and the loan is offered with insurance. Borrowers with an FNB account enjoy lower interest rates.

Standard Bank is the second bank to show a commitment to microenterprise loans, with its Community Banking Unit launching a pilot in Tembisa in 2009. There are four loan products, the Micro Working Capital Loan, the Small Working Capital Loan, the Micro Equipment Loan, and the Small Equipment Loan. All loans are to individual business owners and are non-salary-based. A decentralized approach is being used with respect to Origination, Assessment and Evaluation, Loan Approval and collections and recoveries.

Performance: The deposit initiatives of the primary banks are now close to saturating the low income markets. Microloan programmes for salaried individuals are also growing well for Absa and FNB. It is still too soon to comment on the microenterprise lending initiatives.

Issues and Challenges: In the case of deposits, the primary banks are ahead with numbers and it is largely a saturated market. The challenge here is to improve on service offerings and reduce costs and fees to protect their leadership in this area. Capitec offers lower fees and higher returns on daily deposits than the primary banks and thus one would expect more innovative approaches from the banks in retaining their leadership.

For salary-based lending, the banks offer a similar product range as the more agile and purpose built large microlenders, such as Capitec Bank and African Bank. The challenge in this area also, therefore, is to surpass what the competition offer in terms of client experience and efficiency of services.

The inclusion of a micro enterprise service by two of the banks indicates a serious approach to more inclusive banking. There are three particular challenges, however, to operating microenterprise credit services within a commercial banking entity. First, commercial banks largely run centralised lending models in terms of credit decisions and support services. Internationally, however, the best practise model is a decentralised one. Second, it is a challenge to apply the transfer pricing models of banks to a business with lower profit margins[31], especially in the establishment period. And, finally, it is not yet clear if commercial banks will have the patience to wait while building portfolio and capacity and, at the same time, supply the "patient capital" required to build a microenterprise finance business at scale over the four to five years it will take.

III.6 - Retail Development Finance Institutions[32]

Over the past ten years, multiple government entities have launched retail microenterprise lending initiatives. The common objective for all these programmes has been to support the livelihood and empowerment of those who were previously disadvantaged and assist them to build a sustainable enterprise. Programmes of the provincial development corporations have been both general, targeting any previously disadvantaged microenterprise, and specialized, such as Uvimba which targets small scale farmers in the Eastern Cape. Programmes at the national level tend to be specialized. The National Youth Development Agency, for example, is targeting youth up to the age of 35. The Land Bank operated a large microenterprise lending operation called "Step Up" which targeted rural areas[33].

The weak state of the microenterprise lending sector, as described previously, is one reason cited by government to justify its direct lending operations. Unfortunately, however, government performance in the sector has not been any better in terms of outreach, portfolio quality, or efficiency, and significant tax funds have been wasted. Despite four years of operation, significant funding, and an office in most provinces, for example, the NYDA was serving just 2,500 active microenterprise clients at March 2009 with a large portfolio at risk and a low repayment record.

The general failure of government run microfinance is a global phenomenon; it is not unique to South Africa. Even if the most knowledgeable and experienced individuals are hired to run a government microfinance institution[34], they have many inherent challenges to overcome which result in high arrears and inefficiency.

Below is a sample of some of these challenges:

- Clients have the impression that the loan is "easy money" and arrears rates tend to be significantly higher than for privately run microfinance,

---

[31] The preferred global model for bank downscaling generally includes a separate "service company" which applies the decentralized model and develops independent and lower cost standards and policies and manages the microfinance portfolio of the commercial bank.

[32] Also referred to as State Owned Retail Banks.

[33] This unit was inexplicably closed in 2006 after it build a cumulative reach of over 200 000 clients and disbursed more than R1 billion of loans over a nearly 10 year period, arguably the most successful microfinance endeavour of the government to date.

[34] NYDA has an experienced team of both local and international microfinance experts

- Given the above, the government institution needs to be even more disciplined about collections; this is difficult when local politicians are trying to gain votes,
- The politicians or ultimate “masters” of the programme can change. New politicians may begin to put pressure on the organization to lend to un-creditworthy individuals or individuals who fall outside the target market,
- Personnel policies for government organizations are dramatically different from the policies and performance management culture required to be successful in microfinance.
- For political reasons, government offices may be required to serve individuals who reside outside an economic service area. This is inefficient and generally goes against best practices.

There is just one well known example of a successful government run microfinance institution worldwide; Bank Rakyat Indonesia. The cultural, economic, legislative and political environment for this institution allowed it to thrive where others have failed.

Rather than fill the microenterprise finance gap with government programmes, however, an alternative strategy would be to evaluate more thoroughly what is required to support the three large microenterprise lenders in reaching 100 000+ clients each, what is required to foster the development of five or six more large privately owned microenterprise lenders, as discussed in Section III.1 or what partnerships can be formed with the commercial banks interested in this area. Consideration should also be given to at least partially privatize the largest national microenterprise finance DFI, the National Youth Development Agency.

Private microfinance is thriving all over Africa, with a wide range of organizations: commercial banks, not-for-profits, financial cooperatives, and non-bank financial intermediaries. Let’s learn from these initiatives.

SECTION IV – SPECIAL PRODUCTS

IV.1 – Stokvels and Burial Societies

Stokvels are informal savings groups which operate under an exemption to the Banks Act. Defining stokvels has been contentious as a wide variety of stokvels exist. In its purest form it is known as a Rotating Savings and Credit Association (ROSCA) where members contribute to a common pot and at each contribution the pot is allocated to a specific member. Some stokvels retain part of the savings to extend as credit to members at a given interest rate. There are also stokvels which keep the savings to be used in an investment fund or to purchase an asset which is meant to generate income for the members. Some stokvels are used to save funds towards a particular holiday or year end event such as Christmas. Stokvels also have a social component in that meetings are always social gatherings where the host member can also generate income in providing refreshments and food to the other stokvel members.

The National Stokvels Association of South Africa (NASASA) was registered as a Section 21 company in 1988 and is a national, self-regulating umbrella body for all stokvels, including burial societies. NASASA currently represents 150 000 individual members from 11 000 groups nationwide.

NASASA defines stokvels to have the following characteristics: voluntary membership; groups are informal and rely on trust to ensure the safety of funds; functioning of these groups is solely the responsibility of members.

In 2006, an amendment was made to the Banks Act of 1990 to cater for stokvels whereby they are viewed as legal, self-governing entities, operating outside the regulations covering banks. They are allowed to take deposits from members only, but are not allowed to hold in excess of R9.99 million at any one time. Any stokvel exceeding this amount is required to register as a mutual bank and would then legally fall under the Mutual Banks Amendment Act, 1994 (Act 25 of 1994).

The Permanent Building Society (now part of Nedbank) was the first financial institution to create a special savings vehicle for stokvels in 1988 called a Club Account; today all big four commercial banks offer a similar account. These accounts are generally fully liquid passbook savings accounts which allow for multiple signatories.

According to FinScope 2009, 8.3% of adults hold savings in a Stokvel and 1.1% currently have a loan from a Stokvel. Stokvel usage is most popular among those in FSM 4 (10.6%), FSM 5 (11.7%), FSM 6 (19.0%) and FSM 7 (13.3%). It is also most popular among females, with 10.5% usage compared with 5.8% for males. Usage among blacks is strongest, at 10.7%, compared with 1.1% for Asians, 0.7% for coloureds, and 0.2% for whites.

Burial Societies are informal funeral insurance schemes where members make a monthly contribution that covers the funeral of the member and close family members. It is operated within the confines of the Friendly Societies Act of 1956 and it is estimated that 6 m South Africans are members of burial societies. Many formal institutions emulate the burial societies but provide formal funeral insurance. These entities do not have the social component where members of the society support families during their bereavement and assist with the provision of food and other services during the funeral.

IV.2 – Microinsurance

All members of society face risks that threaten their lives and possessions. For low-income people, the impact of such risks is particularly severe. It can force them to draw on their savings, to sell hard-won assets or to become indebted, thereby plunging them into or keeping them in poverty. International experience has shown that insurance can play an important role in risk mitigation for those with low incomes. Whereas the individual may not be in a position to accumulate sufficient savings to cover losses when they occur, he or she may be able to pay premiums relating to the risk, provided that the product is appropriately designed to his/her needs and affordably distributed (National Treasury, 2008; IAIS/MIN Joint Working Group on Microinsurance, 2008).

Microinsurance is any insurance product that is targeted at the low-income market. Though very small as a percentage of overall premium flows[35], South Africa has a well-developed microinsurance industry relative to its peers, particularly in the two areas of credit life insurance and funeral cover.

Credit life insurance insures the value of outstanding debt in the case of a policyholder's death. It may also include riders such as funeral insurance for the purchaser or insurance on the value of a financed asset (such as furniture) if lost or damaged. Most often, credit life insurance is made a compulsory precondition to a loan, as it provides the credit provider with protection against payment default in the case of a debtor's death or (in some cases) disability. At the same time, it protects the deceased borrower's family from having to repay the debt (Smith, 2008).

Credit life insurance dominates microinsurance worldwide. A 2007 global scan of insurance in the 100 poorest countries by the Microinsurance Centre, found that 36% of all those covered by insurance and 60% of life products were directly linked to credit schemes (Roth, McCord & Liber, 2007). These figures closely resemble those for South Africa, where it is estimated that credit life constitutes 40% or more of total formal microinsurance in the country.

The insurance market in South Africa is divided into long-term insurance, governed by the Long-term Insurance Act, 52 of 1998, and short-term insurance, governed by the Short-term Insurance Act, 53 of 1998. A single company is not allowed to have licences under both acts. Most policies relating to life events are captured under long-term insurance[36], while short-term insurance covers the loss of an asset as well as a number of other categories[37]. Both acts include personal accident death and disability events as well as capital/sum assured insurance for health events. That is, insurance policies that have a health event such as hospitalisation as trigger for payout may be provided under both acts. However, both strictly exclude indemnity health insurance, which is any health insurance that covers actual health expenses (reimburses the client or doctor/hospital for the cost of treatment). The latter may only be provided by registered medical schemes as regulated under the Medical Schemes Act, 131 of 1998.

---

[35] In 2008, funeral insurance (the only distinct "low-income" type of insurance for which data is recorded in South Africa) accounted for 1.4% of total net insurance premiums in the long-term insurance market in South Africa (FSB Annual report, 2009).

[36] The definition of a long-term insurance policy under the Long-term Insurance Act, 52 of 1998 is: an assistance policy (the term used for funeral insurance), a disability policy, fund policy, health policy, life policy or sinking fund policy, or a contract comprising a combination of any of those policies; and includes a contract whereby any such contract is varied.

[37] The definition of a short-term insurance policy under the Short-term Insurance Act, 53 of 1998 is: an engineering policy, guarantee policy, liability policy, miscellaneous policy, motor policy, accident and health policy, property policy or transportation policy or a contract comprising a combination of any of those policies. The miscellaneous category includes for example legal insurance.

Under the insurance acts, only public companies and friendly societies, in terms of the Friendly Societies Act of 1956, are permitted to provide insurance. Friendly societies are exempted from registration under the Long-term Insurance Act if they provide policies for which the benefit amounts do not exceed R7,500[38]. For any larger benefits, a friendly society would have to convert into a full insurer. The Cooperatives Act, 14 of 2005, provides for the formation of financial services cooperatives, including cooperative burial societies, as legal persons. Such cooperatives may also provide insurance but are obliged by the Cooperatives Act to then register for insurance purposes under the Long-term or Short-term Act.

There are 79 registered long-term (life) and 99 short-term (non-life) insurers in South Africa[39]. No composite insurers are allowed. In 2008, un-audited figures indicate that long-term insurers collected R253.7 billion in premiums (net of reinsurance), compared to the R61.8 billion in the short-term industry (FSB Annual Report, 2009). Not all players provide or specialise in microinsurance. The only type of microinsurance for which data is reported to the regulator is funeral insurance. It is a dedicated class of policies under the Long-term Insurance Act, where it is officially referred to as “assistance business”. There are 47 registered providers of funeral insurance in South Africa.

Though traditionally characterised by smaller, specialised funeral insurance providers, interest in the funeral coverage market has increased significantly in recent years, with a number of the large insurers now actively pursuing funeral insurance. This is part of a broader trend in the insurance industry. Traditionally serving the high-end of the market, commercial insurers are now increasingly targeting the low-income market, and considerable product and distribution innovation have made insurance offerings more appropriate and attractive to the low-income market (Bester et al., 2008). As a result, various products are now available that provide cover at as little as R20 per month and that are characterised by simple and flexible terms.

Products aimed at the low-income market (funeral, as well as personal accident, disability and other types of policies) are often sold on a group-underwriting basis with contract periods of no more than one year (with the norm being one-month contracts renewable with the payment of each premium). All of this has assisted in bringing down the risk; both from an underwriting and a market conduct point of view, of insurance products sold to the low-income market, and have resulted in the implicit emergence of a “microinsurance” category of products (Bester et al., 2008).

One of the drivers of this process has been industry’s efforts to comply with the Financial Sector Charter. In South Africa, the extension of access to financial services to the low-income market is an explicit policy goal, and the financial sector has been committed to certain access targets under the Financial Sector Charter (FSC) of 2003[40]. The long-term industry, through its industry body, has developed product standards that are applied in the Zimele accreditation programme launched in 2007 (ASISA, 2010; Bester et al., 2008). Similarly, the short-term industry has launched an initiative called “Mzansi”-type products to make insurance more accessible (SAIA, 2010)[41]. These products are all aimed at the low-income market and rely on simplicity and flexibility. For example: for a product to gain Zimele accreditation, customers have to be able to buy the policy, pay a premium or amend a policy at least once a month within 40km of their residence or place of work. The intention is to send a signal to consumers that products are trustworthy and reasonable in terms of pricing and terms (Bester et al., 2008).

In addition to the commercial insurers, there are a number of burial societies providing funeral insurance formally as registered friendly societies. Yet the bulk of burial society funeral cover is informal. It has been estimated that there are between 80,000 and 100,000 mutual burial societies serving between 4 and 8 million individuals, as well as between 3,000 and 5,000 funeral parlours providing funeral cover. Of these funeral parlours, only an estimated 50% have underwriting by registered insurers. The rest provide informal, in-house insurance (Bester et al., 2008, quoting 2005 FinMark research). All in all, almost two thirds of the demand for funeral insurance is met informally.

---

[38] This was increased from its previous R5,000 ceiling by Note 457 under the Long-term Insurance Act as contained in the Government Gazette of 25 April 2008.

[39] Not counting the 3 dedicated long-term insurers, 6 dedicated short-term insurers, and the 6 composite reinsurers.

[40] Note that the future of the FSC is uncertain. That, however, does not negate the impact it has had on financial inclusion.

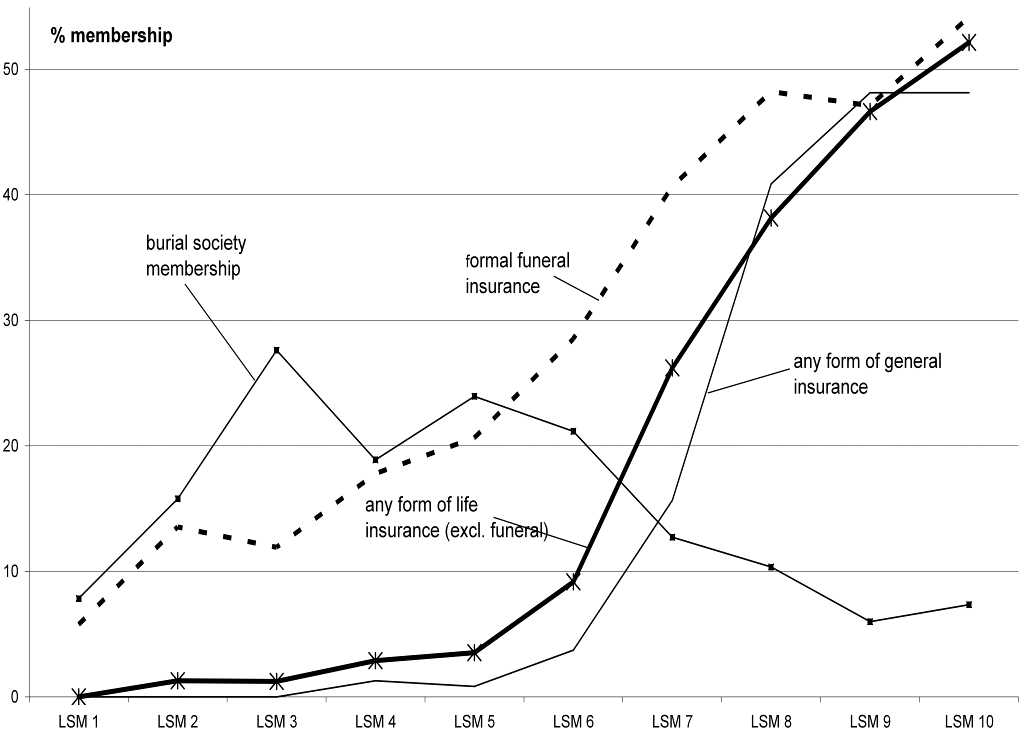
[41] Zimele is a Zulu word meaning to stand on your own two feet, whereas Mzansi is a colloquial Nguni expression meaning “south”.

In the quest to develop products for the low-income market, insurers increasingly focus on cost-effective distribution. Intermediation innovations have played an important role in microinsurance models[42]. These include the use of the cell phone as communication and sales tool, as well as partnerships with retailer chains (Bester et al., 2008). Virtually all of these products are sold in a passive, "off the shelf" way, with no or limited advice and verbal disclosure of product terms. Rather, insurance policy contracts are filled out using a "tick-of-the-box" approach that requires minimal insurer or sales person engagement. This is a feature that characterises only those models aimed at the lower-income market. High-income individuals tend to be served via the traditional broker/agent model (Bester et al., 2006).

In addition, groups play an important role in distribution to the low-income market in South Africa. Burial societies, stokvels, microfinance institutions, church groups or even sports clubs are among the groups that can act as group policy holders or intermediaries for insurance provision by commercial insurers to their members. The intermediation of insurance is most often initiated as a client collective process rather than by an existing intermediary or insurance product provider. The trust placed in the group by the members play an important role in facilitating insurance uptake among members. Although these groups normally have a relationship with only one insurer as underwriter, the group is independent in the sense that if the products of a specific insurer no longer meet the needs of its clients, it can move to another insurer. The group often drives the product innovation process with the help of the insurer, and products are tailored to meet the needs of members (Bester et al., 2008).

In 2009, around 45% of South African adults had some form of insurance or financial product covering a defined risk, the bulk of which was comprised of funeral insurance.

Figure 1 - Insurance Uptake across LSM Groups



Beyond funeral insurance, penetration in the low end of the market remains low. The *cultural imperative* to provide a dignified funeral drives the high take-up of funeral insurance relative to all other types of insurance. For this reason, funeral insurance seems to be the one insurance product that is "bought, not sold" in South Africa. Most consumers appear to utilize more than one policy from more than one provider of funeral cover, often to provide for different aspects of the funeral and there is a relatively high insensitivity towards the price of funeral cover.

---

[42] See Bester *et al* (2008) for an overview of innovative microinsurance models in South Africa.

Overall short-term insurance uptake remains low. Focus group research conducted for Bester et al. 2005; 2008, revealed this to be the result of a combination of factors:

- *Knowledge*. Though people generally have a grasp of the concept of short-term insurance as covering assets, their understanding largely relates to credit insurance.
- *Claims hassle*. Despite revealing trust in short-term insurers in general, respondents felt that claims were not automatically paid out and that the claims procedure is difficult.
- *Affordability of a regular premium*. The general feeling was that, though insurance offers value, one sometimes simply cannot afford it given other spending priorities. This is especially relevant for those participants with irregular incomes or persons who cannot commit to a certain amount every month, as other contingencies may arise that demand all their resources in certain months.

South Africa is currently in the process of reviewing the insurance regulatory framework in order to facilitate the development of microinsurance. Proposals were contained in a Discussion Paper released by National Treasury for public comment in 2008. While this process is not yet complete, it signals government's commitment to microinsurance.

SECTION V – SUMMARY OF POLICY RECOMMENDATIONS

A number of areas requiring further government support have been identified throughout this document, as summarized below:

To support greater usage of deposit services and a stronger savings culture:

1. Support to initiatives which reduce the cost of banking, such as point of sale and biometric applications, assisting in ensuring enabling legislation in this regard.
2. A rationalization of mandates for supervision and development of financial cooperatives under the Cooperative Banks Development Agency.
3. A strong emphasis on capacity building support for financial cooperatives, including the creation of new Second Tier Cooperatives and a seeking of lessons from our African counterparts on how they built their thriving credit union sectors.
4. A revisiting of the Dedicated Banks Bill proposals.
5. Further professionalisation of the PostBank and finalization of a full banking licence for this institution.

To support lower cost salary-based lending for the low income markets, with a lower number of impaired credit records and stronger consumer protection:

6. A concerted effort to resolve issues with the debt counselling programme.
7. A concerted effort to resolve the backlog of cases of impaired credit in the Magistrate's courts.
8. Rationalization of the CPA and NLR payments data; and urgent steps to rebuild the quality of the NLR database.

To support a massive expansion of supply of microenterprise credit by a variety of private sector organizations:

9. Inclusion of microenterprise lending in the weighting for any new Financial Sector Charter.
10. Stronger operational funding and capacity building support for carefully selected microenterprise lenders.
11. A review of the legislative and judicial environment for collateral options for lending to micro and small enterprises.
12. An independent review of the samaf mandate, legal structure, policies, and funding vehicles.
13. A cessation of expansion of government-run retail DFIs offering microenterprise credit.
14. Consideration of the partial privatization of existing retail DFIs.

Other

15. Continued support and encouragement to the microinsurance sector.

16. Consideration of stronger support for bursaries for both local and international training programmes.

One of the major shortcomings in South Africa is a lack of coherent government policy in the development finance arena in general and, more specifically, on financial inclusion or access to finance. Most of the inclusion programmes were driven by donor entities and, in the absence of a coherent government policy which coordinates all ministries, most public projects and initiatives have been uncoordinated and of a stop-start fashion. Development of a broad Policy on Inclusive Banking / Access / Financial Inclusion would be an important contribution to the sector without which the uncoordinated current approach will continue to generate little traction in including more South Africans in the formal financial sector.

REFERENCES

Association for Savings and Investment SA (ASISA). (2010). Zimele. Secure your future. Available at: http://www.asisa.co.za/index.php/financial-sector-charter/zimele.html

Bankable Frontiers Association. (2009). The *Mzanzi* bank Account initiative in South Africa. FinMark Trust, Midrand.

Bester, H, Chamberlain, D and Hougaard, C. (2008). Making insurance markets work for the poor: micro-insurance policy, regulation and supervision. South African pilot study. IAIS/Microinsurance Network Joint Working Group on Microinsurance Report. Available at: www.cenfri.org

Bester, H, Chamberlain, D. and Short, R. (2006). Brokering change in the low-income market. The threats and opportunities to the intermediation of microinsurance in South Africa. Genesis Analytics report. Prepared for FinMark Trust and the Ford Foundation. Available at: www.finmark.org.za

Bester, H., Chamberlain, D. and Walker, R. (2005). A regulatory review into formal and informal insurance markets in South Africa. Genesis Analytics report prepared for the FinMark Trust. Available at: www.finmark.org.za

Bhorat, H. (2009). Quoted in Business Report September (On line edition).

Financial Services Board. (2009). Annual Report, Financial Services Board, Pretoria

FinMark Trust. (2006). FinScope Small Business Survey Report 2006 Gauteng. FinMark Trust, Midrand.

National Consumer Tribunal. (2008). National Consumer Tribunal. 2008 Annual Report.

NCR. (2007). National Credit Regulator Annual Report 2007. NCR, Midrand.

NCR . (2008a). National Credit Regulator Annual Report 2008. NCR, Midrand.

NCR. (2008b). National Credit Regulator Consumer Credit Report 2008 December. NCR, Midrand.

NCR. (2008c). National Credit Regulator Consumer Credit Report 2008 June. NCR, Midrand.

NCR. (2009). National Credit Regulator Credit Bureaux Monitor 2009 March. NCR, Midrand.

NDMA. (2009). National Debt Mediation Association Newsletter 2009 March.

Roth, McCord & Liber. (2007). The Landscape of Microinsurance in the World's 100 Poorest Countries

SASSA. (2007). Statistical Report Number 1 - 2007. South African Social Security Agency, Pretoria.

SASSA. (2008). Statistical Report Number 11 - 2008. South African Social Security Agency, Pretoria.

SSA. (2006). Income and Expenditure of Households. 2005/2006. Statistics South Africa, Pretoria.

SSA. (2008). General Household Survey 2008. Statistics South Africa, Pretoria.

SSA. (2009). Quarterly Labour Force Survey. Quarter 2, 2009. Statistics South Africa, Pretoria.

Van den Berg, S. et. al. (2009). Development Indicators in South Africa, The Presidency, 2009. *Development Indicators, 2009 (online)* - Available from www.italcoop.co.za/Public Documents/SA Development Indicators_2009.pdf