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The Provident Financial Model: Innovation in South Africa's Microfinance Industry

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Executive Summary

Background

Provident South Africa (PSA) closed its operations entirely in December 2001 due to a number of factors which are expanded on in this report. The key reasons were:

- Lack of UK investor support
- Lack of available suitably qualified staff
- Higher than anticipated levels of fraud from staff and agents

The Study

This report sets out to study the organisations operating model in greater depth. The report details who Provident Financial Plc are and why they decided to set up operations in South Africa and the challenges it faced. The study then goes on to look in depth at the operating model used internationally by Provident, before identifying the strengths and weaknesses of the operation in South Africa.

The Provident Financial Model

Provident Financial (PF) has been in the credit business for 120 years. Their head office sits in the Northern city of Bradford, United Kingdom. The South African operation was a sub-division of the Provident Financial International Division. The international division had five branches including South Africa. The others are Poland, Czech Republic, Slovakia and Hungary

Provident South Africa was established in April 1998 as a pilot project. This came after the author was seconded from the UK operating company Provident Personal Credit Ltd. (PPC), to conduct that investigation. Following a successful report on the viability of market entry to SA.

Nearly seven years after the election of the first democratic government, the duality of the South African landscape is still evident in all sectors of the economy. It is embodied in a concentration of big institutions, a missing middle and a plethora of small informal institutions. This is especially evident in the financial sector. About five commercial banks control nearly 80 percent of the sector's assets. Access to financial services is particularly skewed, with most of the population having access to banking services in the form of savings accounts, while only a small proportion has access to other services such as credit. This small proportion is mostly the urban employed. The self-employed and especially the rural self-employed have very little access to banking services. The Strauss Commission conclusively confirmed this in 1996 (a commission appointed by the President to investigate access to rural financial services).

Home Credit (HC) is a well-established, financial service, which has its origins back in the 19th Century. This service is provided to customers in their home (hence the term, Home Credit) and mainly serves people, who wish to borrow relatively small sums on a fixed-term basis. This friendly service has remained unchanged over the years, with an agent of the company calling at customers' homes each week, to collect repayments. Customers tend to find that this style of credit is much more suited to their needs and circumstances than that offered by, say, the Banks and Building Societies.

Relationships developed between customers and agents are the critical success factor in the business, after all the agents are the faces of the company to the customers. Over 80% of agents were female, working part-time and normally providing a service to around 130 customers. The weekly agent/customer contact establishes a regular repayment pattern. The agents were genuinely interested in the well being of their customers and see at first hand any changes in their circumstances, which allowed a much more flexible approach.

Performance of the Model

At the beginning of 2000 Provident SA had 11,000 active customers supported by 250 self-employed agents and 36 full-time staff. Twelve months later, in January 2001, PSA had over 34,000 active customers, 620 self-employed agents and 113 employed staff, of which only 2 are UK ex-pats. And PSA kept on growing. The RSA Company moved from a small Pietersburg-based operation, to be in a position to serve over 60% of the Northern Province and be rated as a leading micro-finance organisation in the Province.

Explaining Performance

At end of the year 2001 PSA could not achieve the year's operational and financial targets. PSA therefore conducted a critical review of its situation and identified that poor collection performance, unacceptable levels of bad debt, and fraud had been the principal problems and these had threatened the business' viability.

The analysis further revealed that the current market situation could not be improved to the extent where the business in its current form or structure would become viable, and given this the business had to close down. Provident therefore decided to dispose of its interest in the South African micro-finance business.

Conclusions

The decision to close the business was a very difficult one, as Provident had invested significant resources into meeting the credit needs of tens of thousands of customers and provided hundreds of employment opportunities across many communities. However, the combination of the above factors had created an unfavourable trading environment, and the situation would always threaten the continued viability of the business. The Management of PSA used their best endeavors to mitigate the impact of these factors but all attempts to rescue the business proved futile. The last resort was a closure.

PSA had the ability and the systems to expand access to its potential target market. The uptake of its existing financial products by the clients was a powerful indication of the need and was reflected in the growth of PSA during the period of its operation. Nonetheless, this opportunity could not be exploited due to continued threat to the viability of the business as specified in the problem statement. In the light of this study, it can be concluded that the most critical success factors that determine the operational and financial sustainability still remains controversial and debatable. This implies that each MFI had its own unique critical success factors that may need continuous monitoring and refinement.

Acknowledgements

The author is especially grateful to Kwakye Donkor for his cooperation in preparing this report.

List of Acronyms

BIS	**Branch Information System**
CIS	**Customer Information Sheet**
CLA	**Cash Loan Agreement**
DM	**Development Manager**
GPC	**Greenwood Personal Credit Ltd.**
HC	**Home Credit**
HCD	**Home Credit Division**
ICD	**International Credit Division**
MFRC	**Micro Finance Regulatory Council**
PF	**Provident Financial Plc**
PPC	**Provident Personal Credit Ltd**
PSA	**Provident South Africa**

The Provident Financial Model: Innovation in South Africa's Microfinance Industry

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1. Introduction

Provident Financial (PF) had for the past eight years been developing its international strategy to reflect the customers' recognition of the valuable services that it provided in the UK and help to maintain its long-term profit forecasts. The decision to go international was taken following a strategic review undertaken by the Board of PF in 1994. Subsequently pilot operations were set up in Eastern Europe, specifically in Poland and the Czech Republic. Following a successful review of the pilots, at the beginning of 1997 by the Board the International Credit Division (ICD) was formally established and a mission statement was adopted:

To research the opportunities to establish Home Credit (HC) and its derivatives in new overseas markets, to establish a number of pilot operations so that PF can establish the viability of business in particular markets and so that PF will have a number of operating units that it can compared, to proceed to expand these businesses in particular markets if viability is established and PF approves such expansion.

The criteria which distinguishes the business are:

- Small personal loans
- Short term
- Unsecured
- To lower income groups
- Home collection is desirable but not essential and will depend on local conditions.

In line with the mission statement another country was identified for further investigation, specifically diametrically opposing in its culture, to further compare the viability of establishing differing operating Home Credit units. The country, which was selected for further investigation, was Republic of South Africa (RSA)

1.1. Market Entry into South Africa

Provident South Africa was established in April 1998 as a pilot project. Targets were set to measure performance on a weekly basis. These targets were set to achieve annual objectives. The basis of these targets was to achieve break even in 3 years. A series of key business drivers were used to measure the performance of the South African Model. Performance to targets was measured on a weekly basis down to development manager level.

REVENUE
Issue value per customer
Collections per customer
Average rate (what the customer should pay back) per customer

QUALITY
Collections % maturities
Bad debt % sales
Number of missed payment
Quality % (Internal measure of the number of missed payment out of a 12 week window. If 8 payments or more are made out of a 12 week window then the customer is classified as quality)

PRODUCTIVITY
Agent/customer ratio
Development manager/agent ratio
Development manager/all staff ratio
Clerk/customer ratio
Security manager/customer ratio

This came after the author was seconded from UK operating company Provident Personal Credit Ltd. (PPC), to conduct that investigation. Following a successful report on the viability of market entry to SA. The author was offered a permanent move to the International Credit Division as Country Manager, which was accepted.

The key issues arising from the research are briefly summarized below.

- SA posed problems, which appeared fairly unique in the world of market research, you have a First World mixed with a Third World, but you have a Euro centric attitude and mentality when it comes to consumer behaviour.
- Both PF and its people were on a new learning curve having to requisite knowledge and skill competencies. PF had to understand how firms respond to environmental threats and opportunities in markets that appear totally different to their domestic ones.
- To be effective in international marketing the most important requirement is to undertake thorough market analysis before and after entering the market.
- It is widely written that the environmental analysis and forecasting play a major role in the formulation of strategy. A full knowledge and appreciation of the environmental forces and changes that are possible to have an impact upon the organisation are the true starting point of a planning system.
- One key lesson learned from the research was not to fall into the trap, which is the tendency of so many people of differing cultures, of people from one culture-judging people from other cultures according to the formers set of values. Some examples of this were found in the attitude of the UK staff that came out to South Africa for short periods to train staff. They assumed they were dealing with staff that had the same values and beliefs of Europeans. This meant that training was not as effective and the UK staff would go back to Europe with the belief that the SA staff were of inferior intelligence.
- If PF entered the market it could well cause some rivalry so it was important to fully understand competitors positioning and likely retaliatory moves. PF clearly had advantages with its funding abilities, history of expertise, systems and technology and its unique modes operandi for RSA, which gave the Company a good competitive advantage.
- PF's proposed market entry needed to take into account what the Company could offer such as funding, expertise, systems and technology but what was lacking was the local knowledge and local credibility, something which a local alliance could have contributed.

Having completed this investigation into the development of the home credit in the South African market the conclusions were overwhelmingly in favour of entering that market. The foundations of the business, in the United Kingdom, had been built upon the key issues of relationships between the agent and the customer and the strength and depth of community spirit had reinforced this. Both these key issues had been proven to be very strong, particularly in the rural areas of South Africa. Added to this was the desperate need of so many previously disadvantaged people to have access to small loans to enable them to make a living (there is no social benefit scheme), this being supported by the Government of the day. These issues were supported by factual data and extensive fieldwork based around academic models.

1.2. Who is Provident Financial?

Provident Financial (PF) has been in the credit business for 120 years. Their head office sits in the Northern city of Bradford, United Kingdom. The South African operation was a sub-division of the Provident

Financial International Credit Division. The international division had five branches including South Africa. The others are Poland, Czech Republic, Slovakia and Hungary (see Figure 1).

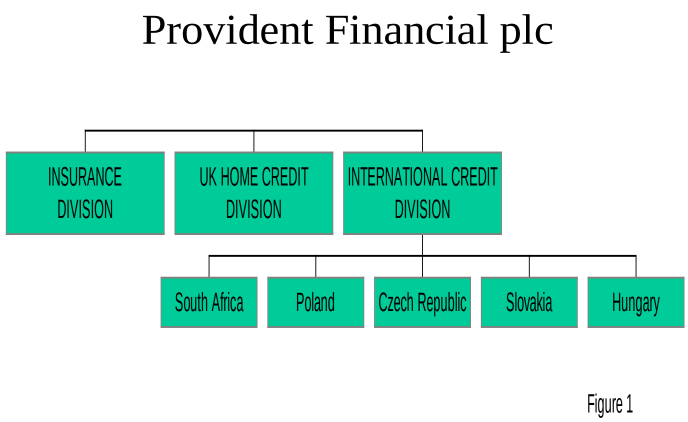


Figure 1. Organisational Chart For Provident Financial-UK
The above organisational chart (Figure1.) illustrates the various division of the Provident Financial Group.

The objective of this report is to describe the Provident Financial operating model and to examine its relative performance in South Africa. The last section examines its strengths and weaknesses and suggests lessons that other MFI's and donors can learn from this experience.

1.3. Why South Africa?

The matrix on the table below **(*Table 1.*)** offers a look at South Africa in context to countries where PF have established operations, new operations and other potential countries. The matrix is based on world development indicators used by the World Bank and tries to recognise the interplay of a range of issues. The factors covered focus mainly on low and middle-income countries and these economies, but also information is provided on high-income economies to provide a comparison.

Table 1. South Africa in context:

Country	Pop Million	Adults 15-64 Million	Per-Capita GNP $ 1995	Compet-itiveness Ranking	Crime Rating	Capital time difference from UK (Hrs)	Business Language
UK	59	38	18,700	8	A	-	English
Ireland	4	2	14,710	33	A	0	English
Poland	39	26	2,790	36	C	1	Polish
Czech Republic	10	7	3,870	31	C	1	Czech
South Africa	42	24	3,160	38	C	2	English
Hungary	10.2	7	4,120	41	C	2	Hungarian
Australia	18.1	12	18,720	20	A	10	English
India	929	562	340	24	B	5.3	Hindi/English
Bangladesh	120	64	240	Not ranked	B	6	Bengali/English
Pakistan	130	70	460	Not ranked	D	5	Urdu/English
Russian Fed.	148	99	3,870	37	D	2	Russian
USA	263	172	26,980	1	B	-6	English
	Potential size of market			Ease of doing business for a UK company			

Note: Crime ratings (A: relatively low crime to D: high rates) reflect the comparative rates of violent and organised crime. International comparisons of crime rates are often misleading due to different reporting categories and standards.
Source: World Bank – World Development Report 1997, World Economic Forum – Executive Opinion Survey Competitiveness ranking, SA Institute for security studies.

Further desk research on RSA identified that the regulatory environment, market size and payment culture suggested that closer investigation was required. To be effective in international marketing the most important requirement is to undertake thorough market analysis before and after entering the market. This then allows for a continuous awareness of opportunities, threats and trends. This led to a series of visits to SA by senior people from PF culminating in detailed research being undertaken by the author.

2. Microfinance in South Africa

2.1. The context

Nearly seven years after the election of the first democratic government, the duality of the South African landscape is still evident in all sectors of the economy. It is embodied in a concentration of big institutions, a missing middle and a plethora of small informal institutions. This is especially evident in the financial sector. About five commercial banks control nearly 80 percent of the sector's assets. Access to financial services is particularly skewed, with most of the population having access to banking services in the form of savings accounts, while only a small proportion has access to other services such as credit. This small proportion is mostly the urban employed. The self-employed and especially the rural self-employed have very little access to banking services. The Strauss Commission conclusively confirmed this in 1996 (a commission appointed by the President to investigate access to rural financial services).

The Government's approach to alleviating this access problem has encountered difficulties. Its efforts are mostly channelled through the Land Bank, Khula Enterprise Finance and its retail partners and, some provincial parastatal banks. This government system has proven to have a limited outreach as well as penetration into the enterprise finance market. Access problems cannot be properly addressed without private sector presence in this market. Surprisingly, South Africa has a major private sector presence in microfinance, but as stated, mostly for the urban employed and concentrating on consumer finance.

It is estimated that 17 million South Africans earn less than R1 600 per month. Of these, 8 million have access to credit services, but according to MFRC research 98% of this access it through cash or term lenders and retail stores for consumption finance. This implies that less than 2% have direct access to enterprise finance and it is also estimated that the penetration of the total enterprise finance market by state supported institutions is less than 1%.

2.2. The Local Financial Landscape

Microfinance in its current form started in the mid 1980s. The industry size is currently estimated at R15billion, according to Micro Finance Regulatory Council (MFRC) special report (2001:2). The industry members were, however, primarily more concerned with the number of beneficiaries than the viability of the institutions they were helping. This perspective implicitly assumed that donor support was limitless but this was not the fact hence that attitude could not last. The realities of finite donor support and escalating global poverty have now forced the micro-finance industry to undergo a shift toward the financial systems approach to micro-finance development.

According to the literature, the micro-finance industry has now mushroomed to such an extent that it has become a significant player in the local financial services sector. The MFRC report further indicated that micro lenders disbursed R12, 9 billion as at August 2000 whilst outstanding loans amounted to almost R11 billion. Other important statistics are shown below in table 2.

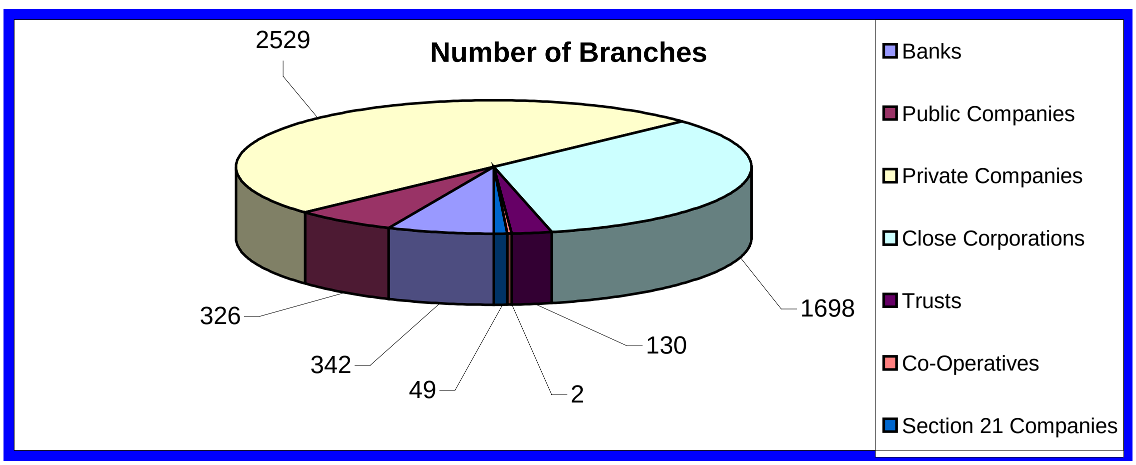
Table 2. Industry statistics for 1st September 1999 – 31 August 2000

Entities	Number registered	Number of branches	Number of Loans disbursed	Gross Loans outstanding	Average loan size
Industry	1,309	5,051	8, 997, 254	R11.0 billion	
Banks	9	342	699,287	R5.3 billion	R7,118.00
Public Companies	9	326	1,413,492	R2.5 billion	R 696.00
Private Companies	182	2,535	2,981,248	R2.1 billion	R1385.00
Close Corporations	1,015	1,669	3,439, 960	R 508.3 million	R 694.00
Trusts	76	129	366, 482	R301.0 million	R 657.00
Co-operatives	2	2	90,390	R130.7 million	R 2,201.00
NGOs	16	48	6,395	R 44.0 million	R 5,126.00

Source: MFRC Statistics, 2001

The micro-finance industry really took off about eight years ago when the South African Government lifted the cap on interest rates for loans under R6000-00. Presently, the micro lending industry bridges the gap between the sophisticated financial institutions and small-scale borrowers. The annual turnover as at September 2000 was estimated at about R25billion. The Figure 2.5 below shows that over 8 millions total number of loans disbursed since the industry mushroomed. Figure 3 below shows the broader industry competitors and the various legal entities in the industry.

Figure 2. Registered Organisations In South Africa Micro-Finance Industry



Source: MFRC special report, 2001.

Figure 3 above illustrates that there over 5000 legally registered branches in South Africa. Out of these, only 8 per cent operate in the Northern Province (see table 3)

Table 3. National Loan Dispersion By Lenders Countrywide

	Province	Percentage
1	Western Cape	13%
2	Northern Cape Province	4%
3	Northern Province	8%
4	Mphumalanga	8%
5	Kwa Zulu-Natal	12%
6	Eastern Cape	12%
7	Free State	10%
8	Western Cape	10%
9	Gauteng	25%

Source: MFRC News Brief (April 2001)

The number of registered companies also gives an indication of the industry contribution to socio-economic development. In the Northern Province where unemployment is high, PSA had created over 150 full-time and 700 self-employed sales jobs respectively. This made a great difference to the improvements in standard of living of many disadvantaged individuals and communities, as well as the mainstream South African grass roots economy.

3. The Provident Financial Model

3.1. What is Home Credit?

3.1.1.Industry Profile

Home Credit (HC) is a well-established, financial service, which has its origins back in the 19th Century. This service is provided to customers in their home (hence the term, Home Credit) and mainly serves people, who wish to borrow relatively small sums on a fixed-term basis. This friendly service has remained unchanged over the years, with an agent of the company calling at customers' homes each week, to collect repayments. Customers tend to find that this style of credit is much more suited to their needs and circumstances than that offered by, say, the Banks and Building Societies.

3.1.2.Provident Personal Credit Ltd. UK (PPC)

PPC and Greenwood Personal Credit Ltd. (GPC) comprise the Home Credit Division (HCD) of Provident Financial Plc. As market leader they have been meeting the changing needs of customers for well over 100 years. They currently operate within the UK and the Republic of Ireland, providing a high quality service to well over one million customers. This service is delivered through the agency force, which currently stands at over 11,000 self-employed agents. Support to agents is provided at a local level through a network of nation-wide offices backed up by a Head Office, which is located in Bradford, West Yorkshire. Bradford was the birthplace of the company founded in 1880 by Sir Joshua Waddilove.

Customer requirements have changed over the years and now some 80% of Provident's business is short term Personal Loans. There has also been an increasing demand for Shopping Vouchers, which are redeemable at many well-known high street retailers. Typically, the average loan is £300 - £400, with a repayment period of 6 months or a year.

3.1.3.Agents' Role

Relationships developed between customers and agents are the critical success factor in the business, after all the agents are the faces of the company to the customers. Over 80% of PF's agents are female, working part-time and normally providing a service to around 130 customers. The weekly agent/customer contact establishes a regular repayment pattern. The agents are genuinely interested in the well being of their customers and see at first hand any changes in their circumstances, which allows a much more flexible approach.

The Company develops agent loyalty and commitment to customer service, through investment in improved communication channels, people support and continued investment in technology. Local management provides advice and support to all agents and weekly contact enables them to be flexible and offer guidance where any changes in circumstances arise.

Agents are self-motivated, and are always keen to develop and manage their agencies well. They also need to be good administrators to account for weekly collections from their customers. Agents say that they greatly enjoy the opportunities for contact with their customers, as well as the flexibility of being able to manage their own time.

3.1.4.Market Research

Home Credit allows the customers to enjoy the freedom of discussing their personal finances in the privacy and comfort of their own homes. Lifestyles are constantly changing and the Company is seeing a steady increase in demand for its services. Many of the new and younger customers are being introduced through personal recommendation or through connections within their family.

3.2. Products and services

3.2.1. Products

In the South African operation the customers would start with a small first loan that if repaid satisfactorily qualified them for access to larger loans. They would therefore graduate to larger loan sizes based on their performance with each loan. Initial loans started at a maximum of R700 (at inception loans started at R300 over 14 weeks. Market forces and profitability dictated the increases) repayable over 14 or 23 weeks (See Table 4 for product characteristics).

Table 4. Product Characteristics

Designation	**Product 1**	**Product 2**	**Product 3**
Lending Methodology	Individual lending	Individual Lending	Individual Lending
Loan Size	R700-1, 500	R1600 – R3, 000	R3000 – R7, 500
Interest	14.5% per month	9.5% per month	7.5 % per month
Repayment Frequency	Weekly	Weekly	Weekly
Collateral	None	None	None
Repayment Period	14 weeks	23 weeks	33 weeks
Savings	None	None	None

PSA's largest loan was R7 500 repayable over 33 weeks. Experience of the first loan gave PSA the opportunity to build information on the customer and their creditworthiness. All charges were transparent and no additional charges were levied in situations where the customer misses a payment. However this caused a problem by increasing the number of defaulters. Provident believed, wrongly, that peer pressure and the need for additional access to credit would be a sufficient motivator for satisfactory repayment patterns. The charge included all costs, including those of the agent and the cost of visiting clients. All this made for a highly transparent and straightforward product. Disbursement and collection took place in borrowers' homes (home-credit).

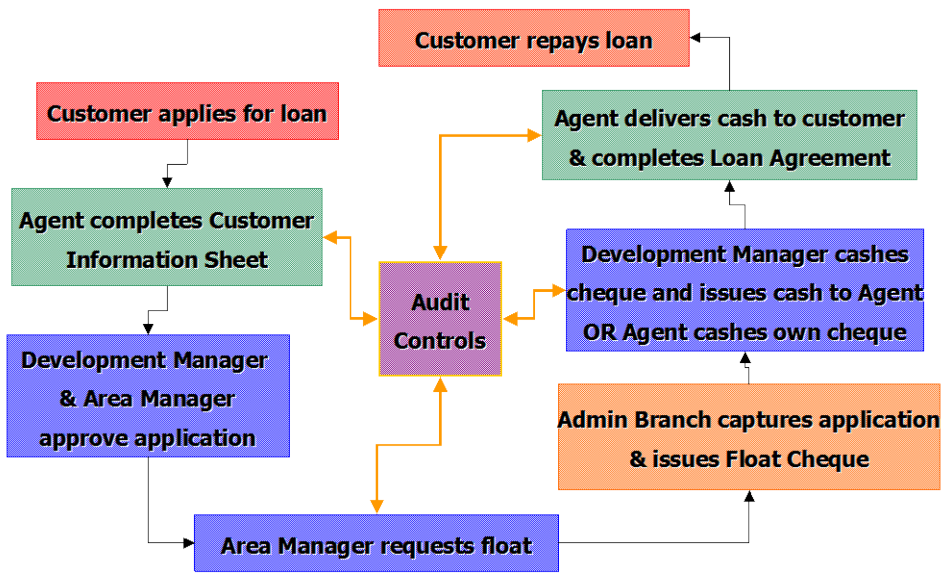
Responses provided on loan application forms approximately 95 per cent of the loans were used to finance micro-enterprises. The success achieved over the three years was indicative of the huge demand amongst micro-entrepreneurs in the Northern Province and the extent of the available market.

The product and strategy entailed continuance of PF's model but adjusted and, updated, for South African circumstances. The approach started with the employment of local managers in areas in which micro-finance services would be offered. The local manager typically recruited 12 agents from the local villages, which they targeted for implementing home credit. After initial training, an agent recruited customers within a five-kilometer radius from where the agent lived. The agents' success was based on their inherent local knowledge that informed their assessments. The system further depended on home visits and close working relationships and high levels of personal contact between all parts of the business. PSA also had an in-depth training and coaching system. Training and coaching of staff and agents was seen as an integral part of PSA business development process. Progress and approach were evaluated annually and this information was used to keep to or adjust the implementation plan.

3.2.2.Loan application, disbursal and repayment procedure

PSA staff and agents received classroom training and field support on the loan processes and on credit control techniques. An agent recruited customers only within a 5km radius of where he / she lives. This training and local knowledge of people and businesses was crucial to PSA's responsible lending culture.

Diagram 1 below details the loan application and disbursal process.



(Diagram 1)

When a person approached one of PSA's local agents requiring a loan, the agent first collated the information pertaining to the customer, including personal details, employment / business details, income and expenditure, on the standard Customer Information Sheet (CIS). After checking the applicable stock and the business and using his / her local knowledge of the applicant and their business, the agent made the initial judgment on whether the customer could be offered a PSA loan. Typically the customer would keep a simple sales ledger, which the agent would use to help assess the weekly turnover. The agent's local knowledge of seeing how busy the customer was also a good indicator of how well the business was doing and the customer's business acumen. The manager would also visit the customer separately and check the level and quality of stock.

The local Development Manager (DM) discussed the loan application with the agent during their regular contact, asking further questions about the customer information and checking the affordability of the loan. Renewal loans required the completed Customer Payment Card and a computer-generated payment history of the previous loan for further credit control. The DM then approved the application and obtained further authorisation from the Area Manager, Regional Manager or Field Development Manager, in accordance with credit control policies, should the loan exceed certain limits.

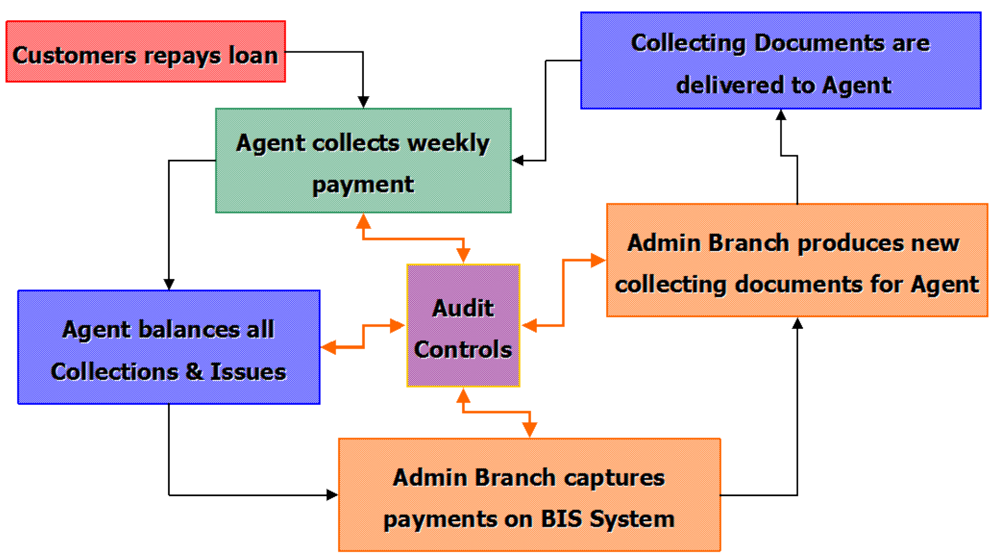
The Area Manager, having seen and authorised the CIS, faxed a float request to the local Admin Office, where float cheques were prepared, then delivered to the Area Management Centre. Float cheques were made out to either the agent or the DM, who cashed the cheques locally. The Security Department made regular checks in the field of the cheques / cash floats carried by agents or DMs.

The agent then delivered the loan in cash to the customer in the privacy of his / her own home. The agent completed a standard Cash Loan Agreement (CLA), which clearly stated the value of the loan, the loan term, the weekly instalments and the total amount payable. The terms of the CLA were fully explained to the customer, who then signed the agreement and kept a copy. The process, from the first contact with the agent to the home delivery of the cash, took less than 7 days.

The CIS and CLA were returned to the Admin Office at the end of each working week, where the allocation of float and issue of loans were reconciled. The CIS forms were checked to ensure that proper authorisation limits had been adhered to. Details and signatures on the CIS and CLA were compared. A check was made on the Branch Information System (BIS) that the customer had not already got an active PSA loan. A security letter, with details of the loan values, was sent to customers by post from the Admin Office for every loan that had been issued.

Security systems were based in South Africa and relied heavily on the security staff doing spot checks and analysing the Management Information, with some support from the UK. Customers from that week's issues were allocated for the Development Manager to visit and complete a Loan Verification Visit Form. Customers for visitation were selected by the system using set criteria, based on Provident's risk management experience. The objectives of these visits were to ensure that the customer exists and that the customer had received the stated loan value. The DM would also take the opportunity to re-emphasise the loan terms, check satisfaction of the agent's service, offer informal business development advice and increase borrower education. The completion of these visits was controlled on a weekly basis and outstanding visits were escalated. Visits completed by DMs were spot-checked by Area Managers and the Security Department, which also conducted selected loan confirmation visits to customers.

Diagram 2 below details the loan repayment process.



(Diagram 2)

The agent visited his / her customers each week in the customer's home to collect the weekly loan repayments. In this way the agent became a trusted friend, listening to the customer's circumstances during the weekly visit and giving support where necessary, often including business advice. The payments were made in the privacy of the home and customers did not have to travel the usual long distances into towns to make bank deposits or pay at an office. The great strength of the operation was this close relationship that was built between the agent and the customer.

Before the first repayment was made, the customer received a payment card, produced by the Admin Office, which detailed the loan terms and the opening balance. The agent recorded all payments on this payment card. The agent and customer signed on the payment card as proof of receipt of each payment. The payment card remained in the possession of the customer until the loan was fully paid-up, at which time the card was used as a record of credit history for further credit applications.

Payments were also recorded by the agent in his / her Collecting List, which was printed every week by the Admin Office and contained up-to-date loan details of every customer. During the course of the week the agent deposited collections in a local Post Office. At the end of the collecting week the agent balanced all collections and issued a simple Weekly Return, and all the relevant documents were delivered to the Admin Office.

The Admin Office captured every customer payment on the BIS computer system and reconciled the declared collections against the deposits. Any shorts or overs were closely monitored. Financial transactions were matched locally and by the UK-based Cash and Bank Department, whose Query Management System controlled the identification and resolution of any discrepancies.

The customer payment card and the computer-generated payment history was compared in the field at any time to ensure the agent's correct recording of repayments. That comparison was especially used by the Security Department during spot-checks or investigations, instigated locally or as a result of UK advice and experience. When "risk" agents were identified a process of dual visitation took place with Security Managers.

No security was required from the customer. Instead, local knowledge of the individuals and micro enterprises involved and regular personal contact ensured that the agents kept control of repayments.

After a small starter loan of R700 had been successfully repaid, a customer would then be eligible for a higher amount, as their businesses grew and the relationship between the agent and the customer became one based on increasing confidence and trust.

3.2.3.Audit controls

Any breach of Standard Operating Procedures was monitored. Regular internal reviews were undertaken by the Administration and Security Departments to ensure correct compliance to these processes and the implementation of agreed actions, in preparation for external audit.

Diagram 3 below illustrates the internal audit control procedures involved throughout the process.

(Diagram 3)

Within the above audit control procedures, there was some interaction with the UK in terms of advice and experience provided to PSA.

3.2.4.Customers

PSA had 60 per cent coverage of the target population in the Northern Province with over 30,000 active customers and approximately 10,000 paid-up customers, with good credit histories. All customers came from previously disadvantaged communities. Over 80 per cent are women, 95 per cent are informal workers and, only 5 per cent earn formal income and had bank accounts. This meant that a vast majority of customers were cut off from the traditional sources of credit, which demand such formalities and securities.

Loans were used for the following purposes:

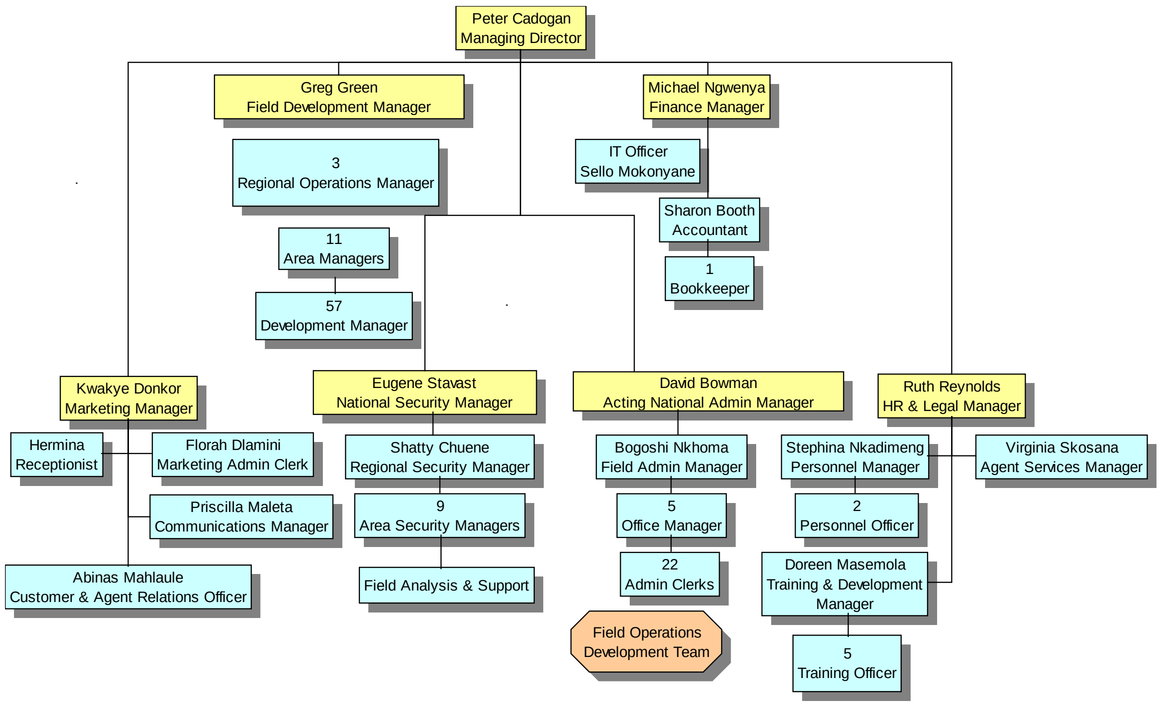
Table 5. Loan Use

Micro enterprise	95%
School fees	2%
Housing materials	1%
Consumption	2%

4. Organisational Structure

4.1. Operational structure

The organization chart below (Diagram 4) details the organizational structure at the close of the operation.



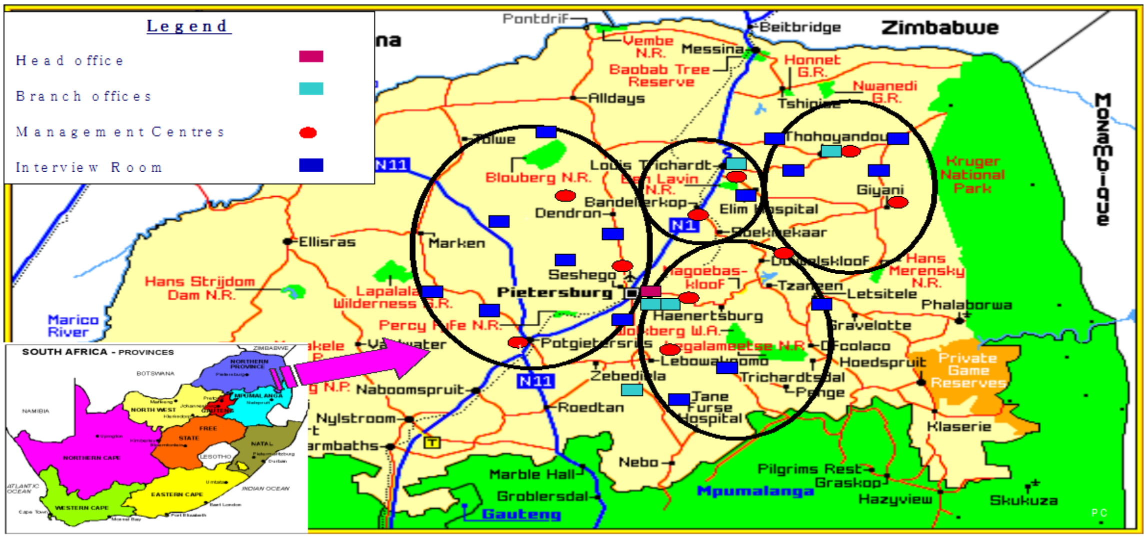
(Diagram 4) Senior Executive Team

4.2. Facilities

PSA operated out of the following rented premises:

- A head office based in Bendor Business Park in Pietersburg;
- 4 administration branches (2 in Pietersburg, 1 in Thohoyandou and 1 in Louis Trichardt); and
- 10 Field Management Centres throughout the Northern Province, providing coverage of approximately 60% of the Northern Province. These centres were used by managers daily for debriefs and on Thursdays for agent interviews.

The facilities were for staff and agent use, customers are serviced in the privacy of their own homes. The map below shows the geographic extent of the operation.



4.3. Administrative And Operating Systems

4.3.1. The Branch Information System

The core operational system was the BIS system, an internally developed, bespoke computerised record management system designed to specifically meet the needs of the PF business. BIS ran on industry standard hardware, Hewlett Packard servers ran Unix operating systems coupled with Wyse terminals and OKI printers. BIS was designed to be easy to learn and user friendly, as well as being a fast, flexible but robust system. The BIS system was designed to be installed at office level, where it could then meet local needs in terms of weekly data processing and production of management information in a self-sufficient manner. Documented system operating, administrative and clerical training procedures enabled the BIS system to be supported on a local level.

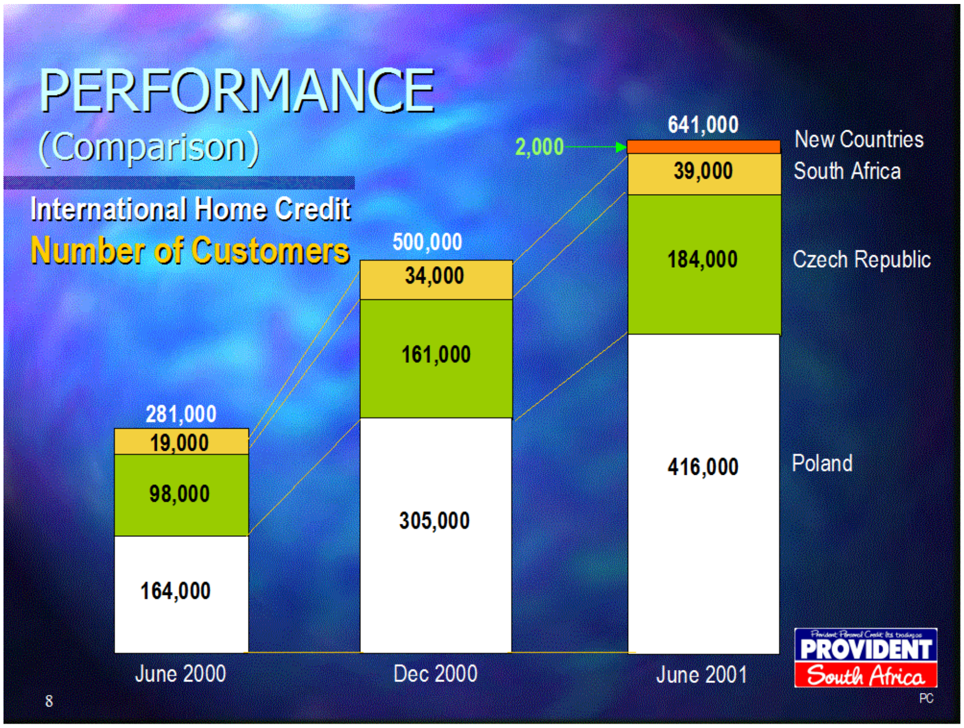
4.3.2. Key Operating Features

Information regarding agent performance was entered directly into the system on a weekly basis, which included collections, issues, new accounts, etc. and once reconciled to the agents' administrative returns the data was processed, updating customers accounts and the data was then retained on the BIS system in the local office. A copy of the data was sent via a secure modem link to the UK for consolidation and analysis within Provident's central systems.

In addition to allowing the production of the forthcoming week's agent collection sheets, the updated data could be used for the:

- ☞ Management of customer accounts, through:
    - o monitoring individual customer and agent performance
    - o identification of marketing opportunities
    - o production of weekly pre-set and ad hoc management reports, such as:
    - o operational performance at management, agent and customer level
    - o customer performance analysis
    - o identification of slow paying customers
    - o identification of exceptional customer and agent performance
    - o management of work loads

5. Historical Performance



At the beginning of 2000 Provident SA had 11,000 active customers supported by 250 self-employed agents and 36 full-time staff. Twelve months later, in January 2001, PSA had over 34,000 active customers, 620 self-employed agents and 113 employed staff, of which only 2 are UK ex-pats. And PSA kept on growing. The RSA Company moved from a small Pietersburg-based operation, to be in a position to serve over 60% of the Northern Province and be rated as a leading micro-finance organisation in the Province.

The customer target levels for the pilot was; 1st year 5,000 customers, year 2, 15,000 customers, year 3, 35,000. Whilst customer targets were met repayment levels, bad debt, fraud levels and sales levels were not. This impacted on the overall profitability of the operation.

5.1. Staff training and development

PSA started by employing a local DM who in turn recruited self-employed agents (typically 12 in number) from the local communities where they wanted to operate. After the initial training an agent would then recruit customers within approximately a 5km radius of where they live.

Managers started with three-day induction training and then over the next 9 months were taken through 4 further three-day seminars aimed at developing themselves, their skills and knowledge. All training had been adapted from the UK Provident training programmes, which had been developed over the last 120 years.

5.1.1. Agents

Whilst UK norms were 130 customers on average per agent, RSA struggled to get to 50, which had a significant negative impact on the growth models. The reasons for the differences were:

- The UK business is a mature business than that in RSA.

- The nature of the employment differs between RSA and the UK. Housewives in the UK are prepared to earn relatively small amounts of money for additional family income – effectively a second income - but in South Africa given unemployment levels, the commission paid was likely to be the principle source of income of the agents, although a high number of agents had other sources of income from their own spaza shops, hawking activities etc.
- Whilst PSA found it easy to recruit agents the difficulty was to recruit the right type and quality of agent.
- The commission structure was geared to provide incentives for the agent to grow the number of customers quickly. Once agents reached 50 customers they tended to reach a comfort level and keep the customer numbers constant.

Whilst agents complained about commission levels, those agents who did perform well earned commission levels which were deemed to be very satisfactory.

Over 80 per cent of the agents, who were self-employed independent contractors, were women, of which 85 per cent were unemployed before joining PSA. Established agents earned in excess of R1, 500 per month in commission and on average each agent had 48 customers, but anticipated to increase to an average of 80 customers as the business grew. The average age of agents was 36 years. Agents were self employed and only paid on commission. Whilst, it was relatively easy to recruit agents, retaining good agents was a problem due to lack of managers' expertise in recruitment, training and staff development. Whilst agents were trained at HO initially, field managers failed to adequately provide ongoing training and development in the field.

Agents' training started with a one-day induction at one of the branch offices. Over the following three to four months the agents were taken through three one-day seminars aimed at developing their agency. The training of agents had also been adapted from the UK Provident training programmes.

5.2. Arrears control and bad debt provisions

5.2.1. Arrears control

It was PSA's policy to manage arrears customers by customer visitation and a system of arrears letters whilst complying with relevant legislation. In addition, management provided support and advice to agents on the collection of difficult accounts.

The following were methods used to achieve PSA's policy:

- Weekly monitoring of customers through BIS arrears control Exception Reports. The reports were reviewed weekly by management for action;
- Investigation of untraced removals (customers moving from current address without notifying PSA of their new address) by management;
- Arrears visitation by management and completion of arrears action sheet. The action covers amongst others; the reason for arrears, the collected rates and arrangements for subsequent payments; and
- 3 standard arrears letters were used in addition to the visitation, depending on the stage of the arrears, namely,
- A polite reminder;
- Urgent demand; and final demand.

5.2.2. Provision for bad debts

The BIS system categorised customers to the number of payments not made during the previous 12-week period. Thirteen stages from zero to 12 were used, with each stage reflecting the number of payments not made during that timescale.

The provision for doubtful debts was triggered when a customer reached stage 4. The provision rates on the total receivable amount were as follows:

Table 6. Provisioning Rates

Stage 5:1 per cent
Stage 6:2 per cent
Stage 7:5 per cent
Stage 8:10 per cent
Stage 9:20 per cent
Stage 10: 30 per cent
Stage 11: 60 per cent
Stage 12: 90 per cent
> Stage 12: Fully provided for

5.2.3.Lapsed Customers' Analysis

Table 7 provides an analysis of PF's customers

Total	**29,698**	
Male	7,260	24.4
Female	22,438	75.6
Customers' age structures	**No of customers**	**%**
18-30	5,344	18.0
31-40	10,326	34.8
41-50	8,067	27.2
51-60	4,026	13.6
61-65	1,949	6.6
Quality customers' segmentation (Based on company quality level measurements)	**No of customers**	**%**
100% quality	6,788	22.9
81-99% quality	3,818	12.9
67-80% quality	2,625	8.8
Below 67% quality	14,962	50.4
Occupational segmentation	**No of customers**	**%**
Self employed	24,776	83.4
Other	4,922	16.7

Table 7: Customer Analysis
Notes:

Although the tables above show that about 30 000 customers had paid their loan, they do not indicate what percentage of that 30 000 had renewed their loans and what percentage had not. Cumulatively, over 80 000 customers had been recruited by Provident South Africa since its inception in South Africa year to date. Nevertheless, only 39 015 customers, about 50 per cent were still active.

5.2.4.Reputation Audit Overview

In September 2001 Opinion Leader Research conducted a PSA reputation audit on behalf of Provident Financial. The research objectives were to:

- To develop an understanding of reputation amongst key stakeholder audiences.
- To establish expectations of Provident Financial as a recently arrived and growing financial services provider in South Africa.

5.2.5. Reputation Audit Results

It appears from the responses from the reputation report that PSA had some relatively glowing reports yet the underlying fact was that they were not achieving satisfactory levels of profitability. The respondents were able to see the headline figures that showed high growth figures. Some respondents would have seen the operational set up and been taken out with good agents. Where good agents and staff were involved the operation was very successful. The problem was that there were not enough good agents.

Reputation audit responses included:

- Amongst those who had knowledge of PSA, it was perceived as well managed and ethical.
- Staff was viewed as experienced and efficient.
- Provident's home delivery service was seen by many as its greatest reputational strength.
- It was also seen as the main difference between PSA and other micro financiers.
- Provident's presence had brought specific economic benefits to Pietersburg and the surrounding area, which add to its reputation amongst the local community.
- Access to credit for self-employed individuals had empowered people and provided an opportunity to improve living standards.
- Those with a close relationship to PSA felt that the cost of borrowing from the company was too high.
    - Some attribute this to the number of agents and area managers
- Provident employees felt that the company cared for and motivated its staff.
- Agents were less positive, and felt somewhat 'out on a limb'.
    - This was due in part to their self-employed status, which left them excluded from benefit and employment protection schemes.
    - They were also critical of what they felt were low rates of commission. Agents were paid a 5% commission on everything they collected.
    - The primary concern amongst agents was their security when carrying large sums of money. Initially theft levels were lower than in the European countries Provident operated in. However, when the programme grew fraud and theft increased to levels higher than in Europe. This was mainly due to a lack of control in recruitment, under-resourcing the security function and fraudulent staff.

6. Strengths And Weaknesses Of The PF Model

6.1. Historic financial performance

Outlined in Appendix 1 is a breakdown of the historical performance with a balance sheet, profit & loss account, cash flow statement and income statement

6.2. Problem identification

At end of the year 2001 PSA could not achieve the year's operational and financial targets. PSA therefore conducted a critical review of its situation and identified that poor collection performance, unacceptable levels of bad debt, and fraud had been the principal problem and these had threatened the business' viability.

Provident's exposure to South Africa had been limited by its shareholders to a maximum of 3 per cent of the group's pre-tax profit, which on the basis of the 2000 results amounts to approximately £5 million. Given the problems identified PSA could have traded itself out of trouble even with greater cash injections, however profit levels would have been lower and on this basis unacceptable to the PF board.

It was unlikely that Provident would have been able to motivate an increase in this limit. Due to investor pressure to disinvest from South Africa, caused by the very negative view held by international investors of the risks associated with investing in South Africa. This had been exacerbated by the volatile regional situation, due to the political and economic turmoil in Zimbabwe and the ongoing conflicts in the DRC and the Great Lake region. Investor sentiment towards sovereign risk, together with PSA having reached its investment ceiling, had led to Provident shareholders applying pressure on its management to reduce its exposure to this region.

The analysis further revealed that the current market situation could not be improved to the extent where the business in its current form or structure would become viable, and given this the business had to close down. Provident therefore decided to dispose of its interest in the South African micro-finance business, which was subject to exiting in a responsible manner with minimal disruption to PSA's staff, agents, and customers.

6.3. Problem justification

Several formal and informal audit tools had been employed by PSA during the course of its operations. These gave indications about why various PSA corrective measures to resolve the above problems had proved ineffective. The summary of underlying causes, obtained from the findings of internal and external organisational audits conducted during the period of PSA's operations include those outlined below:

6.3.1. Personnel issues

- **Limited size of quality labour force in the Northern Province.**

PSA set its salary package for staff, especially field managers, at what was seen to be a very good level. Despite this PSA were unable to recruit sufficiently experienced and educational qualified personnel to grow the business at the budgeted levels set by the UK. Because of the rural nature of the customer target base people had to live within a reasonable traveling distance of their territories.

Very few potential field staff had sufficient management experience to cope with the rate of development of the business. The key to the business model was the need to pass on the skills transfer from ex-pats. In other new country entries three ex-pats were used. In South Africa only one ex-pat was used. This then did not enable the skills transfer to be effective enough for the speed of development of the business.

Self-employed agents were not a real problem to recruit and systems were developed to help ensure proper checks were undertaken. Problems arose where field managers did not follow the policies and procedures. Agents were taken on who then were not suitable. These agents either recruited the wrong type of customers or defrauded the Company. The system broke down where field managers took shortcuts on recruitment and where there was lack of accountability from more senior managers. The recruitment systems were seen to be robust and worked well where the policies and procedures were followed correctly.

- **Inadequate staff and agent commitment and accountability.**

Lack of agent and staff commitment stemmed from the poor recruitment of staff and agents. As previously stated the recruitment policies and procedures were adequate, however short cuts in the recruitment process and the inability to recruit the right quality staff and agents led to problems with commitment and accountability. Managers lacked the experience to make people accountable. This in turn caused commitment problems. The friendly / sociable culture also played a part in the problem. People did not feel comfortable with telling people off and taking them through the disciplinary process.

- **Lack of control of field management control systems.**

Field management control systems were the backbone of the operational model. These systems had been tested through out the Company over a number of years. However, when field managers failed to implement and control the systems problems arose. Again this goes back to the earlier problems identified such as recruitment and accountability.

- **Outside interest – conflict of interest & dual responsibilities**

Despite field managers being paid over average remuneration there was a preponderance of managers who continued to have outside interests, which conflicted with PSA business interests. A number of managers came from an insurance background and they continued to write policies when they should have been working for PSA.

6.3.2.Field Operations

- **Rapid outreach**

The rate of expansion was too great for the quality of staff in place. The financial model was built on a number of key variables and key drivers. The key variables included; monthly targets for new customers, lapsed customers, agents, collections, sales values, rate values, and product mix. Key drivers included; Quality – bad debt as a percentage of sales, number of missed payments. Productivity – agent / customer ratio, field manager / agent ratio, staff / customer ratio.

All these key drivers and variables were entered into the financial model, which then identified levels of profitability over certain periods. The financial model then drove the rate of expansion. The model was reviewed every 3 months and amendments made. The model was geared to break even after 3 years. However there were a number of variables that were over estimated. This meant that adjustments had to be made with other key drivers and variables to compensate. Values of loans for new customers and lapsed customers issued were a great deal lower than estimated. To compensate for this the speed of expansion was increased.

Where Provident was concerned it was the profit model that drove the expansion plan. Levels of satisfactory profitability were determined and then everything was worked backwards. Numbers of staff and agents to make the model work were then recruited!

Internal research was conducted as to why values of loans and lapsed customers were lower than expected. Focus group meetings and ad hoc marketing meetings were held. In the early days agents concentrated on recruiting customers only. This was a fault of the commission structure. Later on agents again found it easier to recruit customers rather than to retain customers. Customers on the other hand wanted larger loans quicker, but restrictions were placed on early loan values to stop agents issuing too much too soon and over indebting customers. This in turn placed pressure on staff and agent recruitment. Short cuts were taken and poorer quality staff recruited to ensure that the expansion plans were met. This, as previously outlined, caused a number of related problems as targets were chased.

- **Ineffective and inadequate measures for bad debt recovery process.**

Arrears management systems were again set in place early on. These systems and controls had been previously developed in the UK over a number of years. It was found that the RSA legal system was not geared up for the swift dealing with of small loan defaulters. This was seen by a large number of customers as a weakness to take advantage of. The inability of the legal system to deal swiftly and effectively with defaulters caused an increase in bad debt. News traveled fast in the rural areas and managers and agents had little recourse with serious non-payers. For a while PSA became known in some areas as a 'soft touch'. Non-paying customers were taken to court but the length of time the courts took to process made the deterrent factor inoperable. Non-paying accounts were outsourced to debt collection agencies that had a limited impact.

- **Inconsistent territorial structures and large geographic territories.**

Due to the rapid expansion plan territories were extended into large geographic areas to allow for managers and agents to chase the new customers. This meant that agent's territories were allowed to expand instead of restricting them to the 5km radius. This caused problems of agents not being able to effectively collect over such wide distances. Sometimes agents would call back a number of times to collect the repayments. However if the customer lived a taxi ride away then the agent would be less likely to chase the customers for payment. This then put pressure on the field managers to support agents over a wider geographical area.

- **High incidence fraud levels among agents and staff**

In the first year of trading PSA fraud levels were in line and in some cases better than those of other countries where PF operated. However when the significant expansion took place there was a significant increase in fraud levels. Reasons for this go back to the issues raised earlier about quality of recruitment. Poor quality staff and agents led to the increase in control. Frauds were exacerbated by the lack of accountability and implementation of controls. This was again compounded by the poor response and interest from the South African Police Service (SAPS) and the length of time it took to get cases through the courts. The deterrent of the RSA judicial system was ineffective. Again PSA was seen as a soft touch. Levels of fraud occurred primarily in the field where the handling of cash was greatest. Again systems and controls were in place and adequate. What caused the problem was the accountability and implementation of those systems, which was mainly due to the lack of quality staff and agents.

6.3.3. Marketing issues

- **Mono-product orientation**

The initial design of the product was purely what was introduced in other countries. A short-term product aimed at testing the market place. A push marketing strategy was employed with all the products. The key driver to the product development was the need to attain the financial model targets. Longer-term products were developed in line with customer feedback but not enough research was undertaken to understand the dynamics of the market. Amendments to products were effected on the basis of anecdotal evidence and financial model driver.

- **Inadequate "South Africanisation" of the UK model**

All the policies, procedures and manuals for the PSA model were adopted from the UK. These systems had been developed over a significant number on years but based on a well-established business with well-established and trained staff. When somebody new started as a field manager in the UK they would have a significant number of established managers to help them skill transfer and help them through the learning curve. Changes were made to Africanise the systems etc. but no account was taken of the fact that there were so many new staff and too few people to transfer skills.

- **Inadequate customer motivation and loyalty**

Rates of lapsed customers remained high throughout the time PSA operated. It was only when a marketing manager was employed (September 2001) and some market research was undertaken that it was discovered that there was little motivation or loyalty for customers to remain as clients with PSA. Agents were also not motivated to retain customers they had recruited. The majority of agents could not understand the principals of keeping and developing existing customers. The benefits of retaining customers were that agents already had knowledge of the customer. Customers could have larger amounts if their repayment patterns were satisfactory and agents could earn more commission from existing customers because of the larger loans being disbursed.

6.3.4. Socio-cultural issues

The key socio-cultural issues identified as weaknesses were the lack of repayment and savings culture in most sections of the South African community and particularly in the rural areas. The historical background of the previously disadvantaged communities and the ineffectiveness of South African Legal and Justice system

6.3.5. Interventions

Potential operational solutions to these issues and problems were identified and implemented. Some were proven to have a positive impact but the inherent problems of staff quality did not give sufficient time to allow large enough improvements to the operation. Some of the operational solutions included the following:

- Maturity period of loans has been shortened. This was to help improve the quality of business and improve cash flow.
- Tightened lending and field operations criteria. Again aimed at improving collections and quality of business written.
- Resolved poor performing agents. 20% of the poorest performing agency force was removed to help improve the business.

- ☞ High levels of police, political and community leaders were involved in trying to resolve fraud cases.
- ☞ Another 2 ex-pats were drafted in to improve accountability. This proved too little too late.
- ☞ Cost control review took place followed by large cost reductions
- ☞ Introduction of Visit Control Systems (VCS) to improve the level and efficiency of audit visitation.
- ☞ Territories, geographic demarcations and restructuring of staff was undertaken to help improve the efficiency of field managers.
- ☞ Improvements to recruitment and training methods were introduced, but there simply was not a sufficient pool of suitable staff and agents to recruit from.
- ☞ Improved and continuous internal and external communications to help inform staff and agents of the reasons for so many changes.
- ☞ Introduction of post office banking. This was aimed at taking more cash out of the system. This would help stop fraud and the temptation to steal.

With these corrective measures PSA's management committed itself to a more responsible, and stricter control and corrective measures.

6.3.6.Closure of Business

The decision to close the business was a very difficult one, as Provident had invested significant resources into meeting the credit needs of tens of thousands of customers and provided hundreds of employment opportunities across many communities. However, the combination of the above factors had created an unfavourable trading environment, and the situation would always threaten the continued viability of the business. The Management of PSA used their best endeavors to mitigate the impact of these factors but all attempts to rescue the business proved futile. The last resort was a closure.

6.3.7.Responsible closure

PSA had always viewed its business model as social responsibility oriented. Based on this sense of responsibility, PSA's leadership entered into a Management Buy-Out agreement with local South African Seniors Managers so as to collect the outstanding PSA quality loan book at a fee. This was after a number of attempts to sell the operation to a number South African financial Institutions.

The possibility of closure of PSA's business was announced in mid-November 2001 and consultative process and SA labour law requirements were pursued. The aim of this approach was to ensure that responsible closure takes place.

The objective of this agreement was to secure the future of selected PSA staff, agents and customers since the MBO had the vision to "South Africanise" PSA's micro enterprise finance model. This was successfully implemented and in effect helped to fairly mitigate against the adverse outcomes of PSA's closure in December 2001. However due to lack of internal funding the MBO closed in March 2002 and the remaining staff was made redundant.

7. Conclusions

7.1. Findings

Generally, access to SME finance is a major problem for entrepreneurs throughout South Africa. This is especially true in rural areas and even truer for women. PSA's product impacted directly on the vulnerable group in rural areas and directly addresses access to enterprise finance with an innovative product.

PSA had the ability and the systems to expand access to its potential target market. The uptake of its existing financial products by the clients is a powerful indication of the need and is reflected in the growth of PSA during the period of its operation. Nonetheless, this opportunity could not be exploited due to continued threat to the viability of the business as specified in the problem statement.

Furthermore, no formal study had been undertaken of the impact of the PSA's provision of financial services. However, anecdotal evidence indicates that customers were diversifying their livelihood activities and, therefore, some were formalising their businesses by moving from informal premises to more formal ones. This implied a perceived quality of service attached to the products of PSA. It was also clear that the agents had a respected standing in the communities in which they operated and that for more than 80 percent of agents it had meant a move from unemployment to working on a full-time basis.

7.2. Lessons Learned

The above experience and international experience had conclusively shown that a high correlation exists between success in microfinance, and institutions that understand and continuously study their market. This means that established MFI's need to adjust to new directions and objectives. The process will however differ depending on the setting of different MFI's.

7.3. Recommendations

Further experience suggests that a thorough study of each potential area for expansion is imperative to ensuring success. Other principles that can be considered in ensuring success in MFI's operations are as follows:

☞ **Sticking strictly to the basics – existing client service and strict delinquency management.**

There is a need to ensure that arrears management is enforced from day one and that sufficient back up support from the SAPS and the judicial services. Once clients identify that there is a weakness with delinquency management the word spreads. Too much emphasis was placed on the development of the business and not the control of the business.

☞ **Drawing on the best practice – Customer orientation and continuous product innovation.**

A pull marketing strategy is clearly the way forward. Insufficient time and money was spent on developing this area. Little customer feedback was used to develop the products introduced by PSA. It was a case of use what had been used elsewhere!

☞ **Effectiveness in the organisation-wide recruitment processes.**

This is a critical area to get right. People are the most important aspect in the success or failure of the business. Unfortunately the availability of quality staff was a major issue in the development of the business.

☞ **Provision of more practical oriented training to staff and agents.**

UK originated training models were used in the training of staff. Whilst they form the basis of good foundation training it was found that there was a need for a more practical approach.

☞ **Continuous innovation and refinement in business approach to lending**.

The UK approach was to stick as close to the business model as possible. There was a clear need to be more innovative in how the model should be adapted for the local environment.

☞ **Leadership and staff participation**

Again the issue of quality of staff impacts throughout the business model.

☞ **Managers and staff attitudinal change**

☞ **Managing Change - Reformation through market research**

Little or no money was budgeted for market research

☞ **Task oriented incentive schemes based – Should mix quality and quantity**

7.4. Remaining Challenges to RSA MFI's

The remaining challenges to RSA MFI's can be summarised as follows:

- ☞ The development of effective staff, agents and customers
- ☞ Positive social–cultural behaviour change
- ☞ Effective fraud prevention
- ☞ A paradigm shift in leadership and investors
- ☞ Effective decentralisation of outreach
- ☞ The impact of the judiciary on industry fraud; and
- ☞ Recruitment of experience, responsible and committed staff and agents

In the light of above, it can be concluded that many critical success factors that determine operational and financial sustainability still remain controversial and debatable. This implies that each MFI has its own unique critical success factors that may need continuous monitoring and refinement.

APPENDIX 1

The financial information set out below is extracted from PSA's audited annual financial statements for the years ended 31 December 1999 and 2000.

1.1. Income statement

(R'000)	Notes	Period ended 31 December 2000 12 months	1999 12 months	1998 10 months
Turnover	1	18,120.8	3 555.2	571.7
Cost of sales	2	(7,515.7)	(2,030.9)	(261.7)
Gross profit		10,605.1	1,524.3	310.0
Administrative expenses	3	(16,804.4)	(6,927.1)	(2,559.2)
Net loss for the year		**(6,199.3)**	**(5,402.8)**	**(2,249.2)**

Notes:

Turnover

Turnover represents the portion of charges paid by the customers on the amount of credit advanced, as determined by the revenue recognition policy.

The 2000 cost of sales includes the following bad debt charge:

Movement in bad debt provision	1,076
Actual bad debt write-off for the year	2,955
Total charge for the year	4,031

Administrative expenses

Administrative expenses include the following credits:

	2000	1999	1998
Profit on sale of fixed assets	9.9	-	-
Interest received	43.7	9.3	4.6

1.2. Balance sheet

		As at 31 December		
(R'000)	**Notes**	**2000**	**1999**	**1998**
Assets				
Non-current assets				
Property, plant and equipment		1,313.9	576.9	495.1
Current assets		32,573.8	5,763.5	1,111.1
Installment credit receivables		22,288.0	4,593.4	553.0
Other accounts receivables		134.9	115.7	103.7
Bank and cash balances		10,150.9	1,054.4	454.4
Total assets		**33,887.7**	**6,340.4**	**1,606.2**
Equity and Liabilities				
Accumulated loss		(13,851.3)	(7,652.0)	(2,249.1)
Head office loan account	1	46,750.4	13,438.5	3,416.3
Total equity		**32,899.1**	**5,786.5**	**1,167.2**
Current liabilities		988.6	553.9	439.0
Accounts payable		988.6	553.9	423.8
Bank overdraft		-	-	15.2
Total equity and liabilities		**33,887.7**	**6,340.4**	**1606.2**

Notes:
1. The head office loan is interest free, unsecured and not subject to any fixed terms of repayment. This agreement is reviewed from time to time.

1.3. Cash flow statement

(R'000)	Period ended 31 December 2000 12 months	1999 12 months	1998 10 months
Cash flow utilised by operating activities			
Net loss before net interest charges	(6,239.1)	(5,409.1)	(2,253.6)
Adjustment of non-cash items			
- Depreciation	318.1	122.8	64.6
- Profit on sale of fixed assets	(9.9)	-	-
Operating loss before working capital charges	**(5,930.9)**	**(5,286.3)**	**(2,189.0)**
Working capital changes	(17,279.1)	(3,922.4)	(232.8)
Increase in accounts payable	434.7	130.0	423.9
(Increase) in accounts receivable	(17,713.8)	(4,052.4)	(656.7)
Cash utilised by operating activities	**(23,210.0)**	**(9,208.7)**	**(2,421.8)**
Interest received	43.7	9.2	4.6
Interest paid	(3.9)	(3.0)	(.1)
Net cash flow utilised by operating activities	**(23,170.2)**	**(9,202.5)**	**(2,417.3)**
Cash flow utilised by investing activities	(1,045.3)	(204.6)	(559.8)
Cash flow from financing activities	33,311.9	10,022.2	3,416.3
Net increase in cash and cash equivalents	9,096.4	615.1	439.2
Cash and cash equivalents at beginning of year	1,054.3	439.2	-
Cash and cash equivalents at end of year	**10,150.7**	**1,054.3**	**439.2**

Management accounts

The financial information set out below was extracted from the management accounts for the seven months to 31 July 2000 and 2001:

1.4. Profit and loss account

(R'000)	Notes	Seven months ended 31/7/01	Seven months ended 31/7/00
Issue			
14 week		592	5,490
23 week		19,421	13,417
33 week		17,866	1,646
Total issue		**37,879**	**20,554**
Collections		47,015	19,902
Gross Revenue		17,019	6,602
Commission		(2,352)	(994)
Net Revenue		**14,667**	**5,608**
Bad Debt		(10,134)	(1,592)
Cost		(15,186)	(9,235)
Total Cost		**(25,320)**	**(10,827)**
Loss before interest		**(10,653)**	**(5,219)**
UK interest charge	**1**	**(2,136)**	**(828)**
Pre tax loss		**(12,789)**	**(6,047)**

Notes:

1. UK interest charge

The UK interest charge was an internal management accounts charge only and was not formally charged or included in PSA's statutory accounts.

1.5. Balance sheet

(R'000)	Notes	As at 31/7/01	As at 31/7/00
Fixed Assets		2,150	1,200
Amounts due from customers		31,985	14,952
Provision for bad debts		(2,291)	(1,139)
Deferred revenue	2	(8,497)	(3,393)
Net installment credit receivables		21,287	10,420
Other debtors		145	67
Cash at bank		8,176	3,008
Current Assets		29,608	13,495
Trade creditors		(1,852)	(119)
Accruals	1	(3,078)	(1,691)
Current liabilities		(4,930)	(1,810)
Net assets		26,828	12,885
Head Office Loan		53,469	26,584
Accumulated loss		(13,852)	(7,652)
Loss for the year		(12,789)	(6,047)
Equity		26,828	12,885

Notes:
Accruals included UK recharges and interest charges noted above.

Deferred revenue equals the portion of service charge that was recognisable in future periods.

1.6. Service Charge

An all-inclusive service charge was levied, on all products. The charge encompassed the whole service offered by PSA. This charge was fixed regardless of the time period over which the loan was collected. There are no additional charges levied should the customer default on a payment or take longer than the contracted term to repay the loan.

The following table discloses, for each product, the charge per R1, 000 loan:

Product term (weeks)	Charge per R1 000 (R)	Nominal monthly interest rate (%)
14	450	12.4
23	562	12.2
33	624	13.9

1.7. Age analysis as at 31 July 2001

Age analysis of repayments receivable (R'000)

Total	Future pmt	Current	30 to 60 days	60 to 90 days
31,985	23,127	5,886	2,530	442

Age analysis of debtor balances - excluding unearned interest (R)

Total	Future pmt	Current	30 to 60 days	60 to 90 days
23,488	17,344	4,083	1,755	306

Age analysis by number of debtors

Total	Future pmt	Current	30 to 60 days	60 to 90 days
32,599	9,064	10,539	9,120	3,876

The above analysis has been prepared in the format required for the regulatory Micro Finance Regulatory Council ("MFRC") reporting and adapts a weekly repayment pattern into a monthly pattern as required by that format.

The attached analysis has therefore been prepared as follows:

Current	Customers in provisioning stages 0 - 4
30 to 60 days	Customers in provisioning stages 5 - 8
60 to 90 days	Customers in provisioning stages 9 - 12

A customer is fully provided for after 12 weeks consecutive non-payment.