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Financial Services and Poverty Reduction

-A case study of the use and impact of microfinance services among women street traders in Durban, South Africa

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DECLARATION

This dissertation represents original work by the author and has not been previously submitted in any other form to another university. Where use has been made of the work of others, it has been duly acknowledged and referenced in the text.

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ABSTRACT

This dissertation analyses the role of financial services in an attempt to understand how they might reduce the vulnerability to income risk for women street traders in Durban, South Africa. The street traders are exposed to income risks such as unpredictable markets, high levels of crime and lack of possibilities for business development. The stated hypothesis for this dissertation is that 'good' financial services may help poor individuals and households to better handle income risks and thereby lower the vulnerability to risks and reduce poverty.

The access to financial services for the street traders in South Africa is rather limited and commercial banks are only willing to facilitate clients that have collaterals with an economic value. There are thus alternative financial institutions, such as microfinance organisations, that use social collateral like, for example, group-lending and frequent repayment schemes. This dissertation will discuss the use and impact of financial services on poverty reduction with a particular focus on a microfinance organisation and savings.

The dissertation will consist of a literature review, a theoretical framework and an analysis of the findings from a case study. The literature review discusses the relation between risks, vulnerability, poverty and financial services in order to provide an introduction to the problem behind the stated hypothesis. The theoretical framework describes the cost of an imperfect market, why formal financial institutions fail the poor, solutions to the problem used by informal and microfinance institutions and the impact financial services have on poverty. The case study is based on a qualitative method through focus group discussions and individual in-depth interviews with clients in a microfinance organisation. To analyse the differences in saving behaviour and business related issues, the clients are divided into two groups with regards to how long they have been using financial services. One group consists of 'old' clients that have access and use the credit and deposit facilities accessible, and one group of 'new' clients that have just started and still have no access to the services.

The findings show that 'old' clients have a higher level of income and more advanced businesses according to skill/capital intensity. Risk related to income and

expenditures that the street traders mentioned are sensitive to the state of the economy, unbeneficial stock, weather conditions, seasonal trends, business agreements, crime and trade permits. Regarding savings, the street traders used a wide range of saving alternatives such as insurance schemes, bank accounts, money collectors, rotating credit and saving clubs and cash savings. There were thus a lack of 'good' saving opportunities and even the deposit schemes offered by the microfinance organisation was not used due to lack of trust and accessibility. Both the 'old' and the 'new' clients were thus aware of the need of savings in order to protect themselves for future income and expenditure risks.

The main conclusion is that the use of financial services through the microfinance organisation and other institutions may have helped the 'old' clients to develop their businesses and reach a higher income level. There is thus a lack of 'good' financial options for the street traders and their position is still very vulnerable.

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TABLE OF CONTEXT

1 INTRODUCTION

Women street traders in Durban, South Africa are exposed to risks regarding their income-sources and their livelihood. Markets are unpredictable, the level of crime is high, and possibilities for business development are low. There is a lack of social protection and other institutions to lower the level of vulnerability in the informal sector. One such institution is the management of money and financial services. The cash balance gained after a day of work is most commonly used for daily needs, but also saved in informal institutions such as rotating saving clubs or in cash at home. Friends, family members, or informal credit lenders are often the only source for credit.

The basic ideas of financial service are to smooth consumption for individuals, either by helping to access past income stored as savings or access future income by lending (Rutherford, 1999). Thus the inability to access financial services is very likely to keeping poor people poor and conversely it may be argued that access to such services may contribute to breaking the poverty trap either to borrow money for beneficial investments, save money for future expenditure, or to use insurance schemes.

The purpose of this dissertation is to analyse the role of financial institutions in an attempt to reduce the vulnerability to income risk for women street traders in Durban South Africa. The stated hypothesis is that 'good' financial services may help poor individuals and households to handle income shocks and lower their vulnerability to risk. Financial services can be viewed either from a client perspective or from the institutional side and I find it useful for the purpose of this dissertation to analyse both sides in the search for a 'good' financial solution. The focus will be on a microfinance organisation and on savings as a particular service. A microfinance institution is a non-governmental organisation that provides credit and saving facilities to uncollateralised individuals in less developed countries.

The case study is based on a *qualitative method* through focus group discussions and individual in-depth interviews with clients in a microfinance organisation, Foundation for International Community Assistance (FINCA).

This dissertation will provide useful knowledge about financial service at a micro level as a base for further development of 'good' financial service in developing countries generally and in South Africa particularly.

1.1 The Problem

Figure 1.1 is an illustration of the background problem and shows the relation between risks, vulnerability, poverty and financial institutions. These risks could be divided into three categories; structural, emergency, and life- cycle risks (Cohen and Sebstad, 2000; Wright, 1999a). Since the poor often have little protection by the government and there is a lack of other adequate institutions to support them their level of vulnerability will be high. Ray (1998) argues that the fundamental feature of poverty is that it affects the access to markets, which also holds for the financial market.

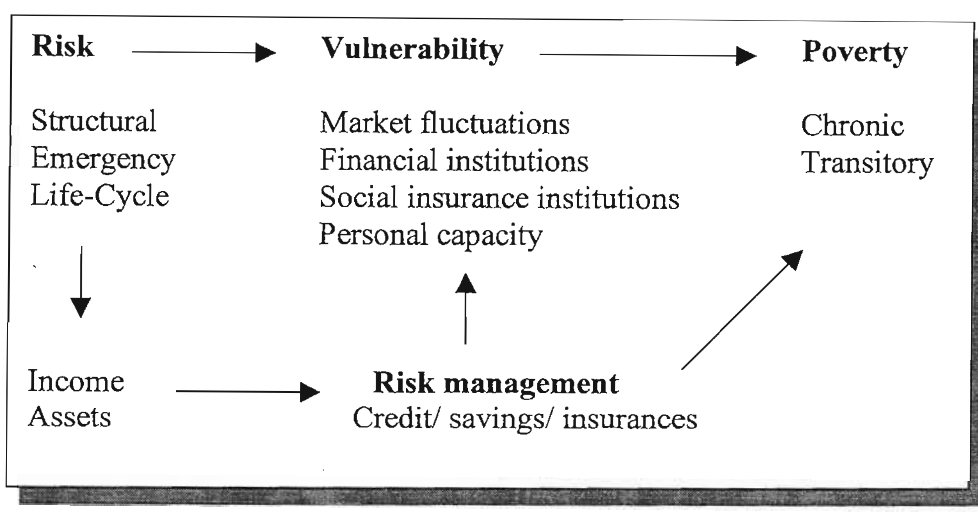

Figure 1.1. Illustration of the relation between risk, vulnerability, poverty, and risk management

Financial institutions are in this illustration seen to have an important role as a risk management tool in order to reduce vulnerability. Matin, Hulme, and Rutherford (1999, p. 3) argue that to "provide poor people with effective financial services helps them deal with vulnerability and can thereby help reduce poverty". This is the main argument of the dissertation and will be the focus throughout the paper. The three main services provided by financial institutions are lending, saving and insurance. In this dissertation savings will have a particular role in order to limit the study and also since savings is the base for all financial services.

Financial institutions can be divided into three different categories, formal, informal and semi-formal. The formal banking is often lacking in providing service to poor individuals since they demand collaterals with an economic value to secure repayment rates and financial sustainability (Hulme and Mosley, 1996). Microfinance organisations are semi-formal institutions that often use social collaterals through group-lending contracts in order to reach poor individuals and households. They build on models that have been used among the poor for ages in informal institutions, such as rotating credit and saving clubs, in order to accumulate money for a particular reason (Bouman, 1995).

'Good' financial services need to include factors such as financial sustainability, impact on poverty, and satisfaction of the clients. There is a conflict in the literature about what an appropriately designed financial service would be. The conflict arises from different academic disciplines. The neoclassical economic theory will argue that an imperfect financial market has social welfare losses (Morduch, 1995; Wright, 1999b). On the other hand, the development theory points to the importance of informal structures in poverty reduction. As often, there is no right or wrong in this debate and the important question is, as Townsend (1995) points out, whether market and non-market institutional arrangements are jointly providing an optimal allocation of risk bearing systems.

1.2 Purpose of the Dissertation

As the background problem suggests, financial service can be used as a tool to handle risks and lower the vulnerability for low-income individuals. The purpose of this dissertation is, through a theoretical review and a case study, to investigate the stated hypothesis; that appropriately designed financial services may reduce vulnerability of low-income individuals and households and thereby reduce income poverty.

1.3 Method and Demarcations

The theory chosen, to capture the problem, is neoclassic economic theory. The theory chosen is relevant for the purpose of the dissertation since it describes the cost of an imperfect market, why formal financial institutions fail the poor, solutions to the problem used by informal and microfinance institutions, and the impacts financial services has on poverty.

The method for the case study is a qualitative method based on group-discussions and individual in-depth interviews with clients in a microfinance organisation, FINCA. To analyse the differences, in saving behaviour, risk management and business related issues, the clients are divided into two groups with regards to how long they have been members in the microfinance organisation and using financial services. One group consists of 'old' clients that have access and use the credit and deposit facilities accessible, and one group of 'new' clients that have just started and still have no access to the services.

The main limitation for the dissertation is that the case study only focused on a microfinance organisation as a financial institution and saving as a particular financial service provided. This demarcation was done in order to conduct a reasonable study in relation to the time and resource limits of a dissertation. Also the concept of poverty had to be reduced to only include income and assets for the sake of the arguments, but in the discussion section other factors of poverty such as health and education will be mentioned. Even if the case study concerns women street traders the dissertation will not focus specifically on gender related issues in the theory.

1.4 Structure

Chapter two is a further development of the problem outlined in the introduction and a literature review of studies done in the subject field. Areas discussed are; the nature of risks facing individuals and households in a developing country; the concept of vulnerability and poverty; the importance of income and assets in relation to poverty reduction; and the role of financial service as a risk management tool, with a particular focus on savings.

Chapter three, the theoretical framework, is divided into four main sections. The first section describes how the lack of financial options, such as borrowing and savings, may lead to high costs in form of income losses and depletion of assets. The second section describes why formal financial institutions fail the poor. The third section discusses informal financial solutions and the economics behind microfinance organisations. The last section will discuss the impact different institutions have on poverty reduction and will also include a discussion of 'good' financial solutions.

Chapter four is a background section for the case study and deals with the informal economy, the legislations, and women street traders in South Africa. Chapter five outlines the method used for the case study and discusses the choice of financial institution, the choice of sample, and the validity of a qualitative study.

In chapter six the results are presented under the three main headings, findings regarding income and consumption, findings regarding savings, and findings regarding the role of the microfinance institution. After the findings, chapter seven will link the literature review, the theory chapter and the introduction to the case study with the results in a discussion. The last section in chapter seven will outline the main conclusions for this dissertation.

2 RISKS, POVERTY, AND FINANCIAL SERVICES

This chapter is a further development of the background problem, illustrated in figure 1.1 in the introduction. It will include a literature review on the relation between risks, vulnerability, poverty, and financial services in order to provide a better understanding of the case study and why the theory chosen in the theoretical framework is relevant for the purpose of the study. First, in section 2.1, the nature of risks facing individuals and households in a developing country will be outlined. Then, section 2.2, will deal with the concept of vulnerability and poverty. After that follows a section, 2.3, on the importance of income and assets in relation to poverty reduction. The last section, 2.4, will discuss the role of financial service as a risk management tool, with a particular focus on savings.

2.1 The Nature of Risks

To design financial services that reduce people's vulnerability, it is important to understand the nature of risk and the risk management strategies individuals' use. Based on this information, suitable financial services can be developed to assist the best ways of coping with risks. The nature of risk depends upon many factors and has complex interactions, which together create the risk environment facing households and individuals. Risks can be divided with regards to how often the risk appears and the effect of the risk; if it is covariant and affects all households in the community or idiosyncratic, i.e. only affecting some households (Chen and Dunn, 1996; Cohen and Sebstad, 2000). One popular way of differentiating risk in the literature is by dividing it into three main groups: structural factors, crisis and emergencies, and life cycle events (Cohen and Sebstad, 2000; Wright, 1999a). The following paragraphs will follow that structure and also include a discussion of specific risks related to the urban environments and gender related issues.

Structural risks can be divided into a macro and a micro level. On a macro level, structural risk relates to long-term or permanent changes in the economy (Wright, 1999a). An example of this is economic reforms, which may affect the household economy in the form of increased school fees and cost of health care. Seasonal swings in commodity demand are a structural risk that may affect urban traders (Cohen and Sebstad, 2000). On a micro level, risk relates to the market; unfavourable prices, lack of financial services, and poor infrastructure are risk areas that urban traders face. Structural risks also include the risks of asymmetric information and opportunistic behaviour from business partners, creditors and competitors (Cohen and Sebstad, 2000). Microenterprice in the informal economy in urban settings may also be exposed to risks of confiscation by municipal authorities due to lack of property law and permit regulations (Barnes, 1996). Besides the above, crime and an unsafe environment are also structural risks facing urban street traders in less developed countries (Dunn, Kalaitzandonakes, and Valdivia, 1996).

Crisis and emergency risks relate to health and crime. Health risks result in both increased expenditure for health care and loss of income if the sick person is an income source for the household. Furthermore, while the health factor may be occasional, it may also be permanent as in the case of HIV/AIDS (Dunn, Kalaitzandonakes, and Valdivia, 1996).

Income risks related to life cycle events include childbirth, weddings, funerals, festivals, and education. Life cycle expenditures can, in comparison to emergency expenditures, be easier to anticipate and thereby plan for (Wright 1999a).

Related to risks are also the differences between rural and urban livelihoods. Most studies concerning risks in low-income countries are related to agricultural activities, because of the relative importance of agriculture as the prime income source (Besley, 1995). Differences between urban and rural poor can be defined through different characteristics; the one relevant for this discussion is commoditisation. The high commoditisation in urban areas makes labour an important asset, either through formal or informal employment. Another aspect of commoditisation is that the household in urban settings has to pay for food and rent, in contrast to relying on subsistent production (Moser, 1998).

Women tend to be exposed to more risks associated with domestic factors than men. These include violence within the home and lack of cooperation with their spouses. Other risks women face related to the domestic environment are their limited role in household decision-making, limited access to and control over household resources, and a heavy domestic workload. Women also tend to have lower levels of individual assets, limited mobility, knowledge and skills, and also low self-confidence and self-esteem. Gender, which influence issues relating to ownership of land and housing, are also important risk factors, which influence women's possibilities to manage an enterprises, start up enterprises, and get access to credit. Women may also be concentrated in a narrower range of enterprise types then men, which increases their risks due to the fact that they have fewer opportunities to generate income (Cohen and Sebstad 2000).

The effect risks have on income and poverty depends on the individuals' level of vulnerability to a certain risk, which the next section will underline.

2.2 The Concept of Vulnerability and Poverty

Vulnerability and poverty are important concepts when discussing financial services as a tool for risk management. The difference in definition between the concept of poverty and vulnerability is that poverty measures are often fixed in time and generally are a static concept. Vulnerability, on the other hand is more dynamic in nature (Moser, 1998). The concept of vulnerability explains the effect risks have on an individual's well being and includes factors such as access to formal institutions, market fluctuations, and social insurance, but also depends on the individual's personal ability to handle crises and to adjust to new situations (Moser, 1998).

The connection for all discourses on poverty is the notation of a poverty line, some kind of critical threshold of income and consumption. Morduch (1994) classifies poverty as either chronic or transitory. These definitions are sample specific. If, for example, a household is poor in every period in a sample, it is characterised as chronically poor and otherwise transitory. Transitory poverty is classified as a failure to find protection against stochastic elements in the economic environment. If x represents a household's permanent income, c the current consumption, and z the poverty line, then the transitory poor could be written as $c < z < x$. This implies that poverty arises only because it is not possible to borrow against future income. In the case of chronic poverty both $x < z$ and $c < z$, i.e. permanent income and consumption are in this case below the poverty line. The impact of financial services on poverty requires assumptions about the distribution of permanent income. Consider the case where the distribution of x is unimodal and shocks are additive so that current income is the sum of permanent income and transitory shock, $y = x + \varepsilon$. If shocks are symmetrically distributed around zero and households cannot smooth income, then an income stabilisation program can in itself lower the head count of poverty and the cost of poverty alleviation if permanent income is above the poverty line $(x > z)$. In sum, Morduch argues that not only will a financial development program address stochastic poverty directly, but it will also help reduce some of the heterogeneity of the poor, which will make targeted poverty alleviation programs more effective.

In relation to poverty, income and assets are two very important variables, especially in an urban environment where money is the sole determination of ones material success and to a large extent one's level of well-being. The importance of income and assets will be further discussed in the next section.

2.3 The Role of Income and Assets in Poverty Reduction

All households face risks related to their income source as described above. The possibility to cope with the risks are related to income level, but also depend on other factors such as personal capability to handle crises and to adjust to new situations as described above. Cohen and Sebstad (2000) writes that the capacity of a household to bear risk has implications for decisions about taking risks and how the household members manage their household economic portfolios. By economic portfolios they are referring to the total income and assets available for use.

Physical assets represent a store of value that can be drawn upon in times of need and the acquisition of such a store is a goal of households everywhere. It varies in terms of quality and properties and the value may increase, decrease, or stay constant. Physical assets include livestock, food stores, gold, and consumer durables (Barnes 1996). Moser's (1998) article *The Asset Vulnerability Framework: Reassessing Urban Poverty Reduction* describes the role of assets for urban poor, and divides the assets of urban poor into five categories: labour, household relations, human capital, productive assets, and social capital.

The first important response to income decline in a household found in Moser's study is to mobilise labour by increasing the number of workers. Women's multiple responsibilities as income earners and domestic keepers means that they assume a disproportionate share of the burden of adjusting to adverse economic circumstances. Human capital assets in the urban context are related to economic and social infrastructure provision in the form of education and health care (Moser, 1998). The skill and capabilities of the enterprise owner represent the store of wealth brought to the final product.

Housing is an important production asset for the urban poor and can be compared to land for the rural poor. Housing insecurity, which results from a lack of formal legal title, such as in informal settlements, creates vulnerability. Tenure security and legal rights give households incentives to upgrade their living and to use their housing productively (Moser, 1998). Physical assets tend to depreciate in value in the long run, but physical assets that have a productive value, such as a sewing machine, increase income in the short run (Barnes, 1996).

The next section will briefly give an insight into why savings may be a particularly effective financial service in line with poverty reduction.

2.4 Risk Management and Savings

The concept of risk management can be understood simply as how individuals handle the risks they face. The risk management strategy focused on in this dissertation is the use of financial services, particularly savings, and how this affects income and assets.

The literature offers a wide rage of studies about strategies to protect against risks facing the poor in developing countries (Cohen and Sebstad 2000; Rutherford 1999; Humle and Mosely 1996; Dunn at al. 1996; Chen and Dunn 1996; and Moser 1998). The most common division of risk management is into ex ante and ex post strategies; either act precautionary and insure against future risks, or deal with the consequences afterwards. In relation to microfinance, maintaining the access to a source of credit could be an important coping mechanism and a key factor that drives clients to repay their loans (Cohen and Sebstad 2000). There is also a difference in positive and negative coping strategies. Often people that are more vulnerable with fewer options need to use negative coping strategies, which permanently reduce their resource base and increases their vulnerability. An example of a negative coping strategy could be selling productive assets, such as technology. Positive coping strategies include mobilising labour, reducing consumption, finding new sources of income, using cash savings or seeking help from relatives and friends (Cohen and Sebstad 2000).

In recent years the trend in microfinance has been a change in focus from credit to saving and insurance schemes, which is a change from an institution-centred view to a people-centred view. This dissertation follows this current trend by focusing on savings and argues that savings will help people reduce their risks and thereby become less vulnerable.

Studies have been done about how people handle their money and about specific saving strategies both in formal and informal saving channels (Bouman, 1995, Rutherford, 1998; 1999 and Wright, 1999a; 1999b). The most commonly discussed are saving at home, joining a rotating saving and credit club, money collectors, microfinance institutions, and formal banks. Wright and Mutesasire (2001) discuss the weakness of informal savings and the need for better saving facilities. By this they mean that saving is a risk in itself if provided by informal options, so if microfinance institutions could offer a safe saving possibility it may lead to a better use of savings as a risk management/ coping strategy.

Savings have a multiple meaning as Hulme and Mosely (1996) point out. Saving strategies could include consolidating savings, building stocks of food, money or other valuables, adopting risk reducing technologies, making social investments, making human investments in education and health, and making physical investments in housing, equipment and land.

Rutherford (1999) argues that people need lump sums to insure against risk, costs, emergency and future expenditure. There are three basic patterns through which savings can be converted into useful large sums of cash: saving up, saving down, or saving through. In the first case, cash is stored until the deposit has accumulated into a sum large enough for the wanted expenditure. Saving down refers to borrowing and repaying the loan. Saving up and saving down is based on the same concept with the difference of when the saving is done before or after the use of the money. Saving through is a mix of saving up and saving down.

Box 2.1 "Three facts and one conclusion"

Fact one: Poor people can save and do save, even if the amounts are often small and irregular.
Fact two: Poor people need usefully large lump sums of money from time to time, for many different purposes.
Fact three: For most poor people, those 'usefully large lump sums' have to be built, somehow or other, out of their savings – because there is no other reliable way to get hold of them.
Conclusion: Financial services for poor people are largely a matter of mechanisms that allow them to convert a series of savings into usefully large lump sums.

Source: Rutherford (1999)

As described above low-income individuals and households in a developing country are exposed to risk regarding their incomes and assets. Financial services can, through borrowing, saving, or insurance, help people to get a more stable income and through this assist them in securing their livelihoods. The next chapter will describe the theory chosen to underline the argument behind the hypothesis that 'good' financial services can help to reduce the vulnerability among poor individuals.

3 THEORETICAL FRAMEWORK

Risk related to income and consumption is an important characteristic of the economic environment, and there are most likely significant behavioural consequences from exposure to such risk. As the problem section in the introduction suggested, the link between risks, vulnerability, financial services, and their effect on poverty is the central concept in this dissertation. The theoretical framework will take these arguments further and in section 3.1 outline the theory of why 'economically speaking' there is a cost of an imperfect market that will affect income and asset accumulation among households. The chapter will also, in section 3.2, look into why the formal financial market is lacking in providing services to the poor. After that follows a section, 3.3, of alternative solutions for financial services offered by informal institutions and microfinance organisations. This section will outline the economics behind group-lending and other alternative solutions used by microfinance organisations. The last section, 3.4, in this chapter, deals with the impact different financial institutions may have on poverty and contains a discussion of 'good' financial solutions.

3.1 The Cost of an Imperfect Market

An imperfect market is very likely to have social costs. In the perfect market case, households will not be vulnerable to income shocks due to the fact that income risk will be diversified away and have no impact on consumption levels. Consumption smoothing is the term that describes the money management of income risks and activities, such as borrowing, lending or insurance against risks. With perfect markets for consumption smoothing, households will make income-earning choices that produce the highest expected value, and then use credit and insurance mechanisms after income shocks occur to achieve consumption smoothing. If consumption smoothing is perfect, the economic theory of full functioning markets will also find that production and consumption decisions are separable. Production choices will be made to maximise profits without concern for risk. When the assumption of the benchmark theory is correct there will be no need for income smoothing, but when the assumptions are violated, income smoothing can and should play an important role in dealing with risk (Morduch, 1995). The next section will explain how the cost of an imperfect market may affect the incomes and assets among households. The main literature used is Morduch's (1994) article *Poverty and Vulnerability*.

3.1.1 Impact on Income and Assets

To describe how the lack of market solutions for financial service exacerbates poverty through income losses, Morduch (1994) uses a two-period model of a poor household. First, the model shows the outcome on income when the household can use borrowing and saving facilities to smooth their income. Then the model shows the impact on income when a borrowing constraint is introduced. The model will show that when a borrowing constraint is introduced the household will get a lower income than if they would be able to borrow money, since they will not produce or invest optimally due to larger precaution to future economic shocks.

In the first case when households have no borrowing constraint, the production decision may be characterised as a portfolio-choice problem in two periods. The production decision in period one depends on the consumption in period two. No insurance is available and the only way to protect consumption is through borrowing or saving.

In period one, households make a productive decision in which risks are balanced against expected income. The actual income, Y_1, is received in the end of period one when period one's consumption C takes place. In the second period, income Y_2 is known for certain. In the first period the household chooses which share of resources $0 \leq \beta \leq 1$ to allocate to a safe activity with a positive return, s. The rest is allocated to a risky but more profitable activity. The first period has two possible outcomes either the risky activity has a positive return h or, the risky activity has a negative return l. Each outcome occurs with probability 0.5 and $(h+l)/2 > s > 0$ i.e. the expected returns to the risky activity are higher than the returns to the safe activity. This implies that the first period income is either high or low:

$$Y_{1H} = \beta s + (1-\beta)h, \textit{ with probability } 0.5$$
$$Y_{1L} = \beta s + (1-\beta)l, \textit{ with probability } 0.5$$

If the outcome is low in the first period the household chooses consumption to maximise utility $U(C_{1L})+U(C_{2L})$, subject to the constraint that all assets in the second period are consumed: $(Y_{1L}-C_{1L})(1+r)+Y_2$ at interest rate *r*. Optimal consumption is chosen according to the standard condition $(1+r)U'(C_{2L})=U'(C_{1L})$ i.e. the optimal utility of consumption is the same in both periods with optimal net borrowing b_L *. Lifetime utility in a two period model is then in the low income scenario and the high income scenario $U_L(\cdot)$ respectively $U_H(\cdot)$.

This result relies on the ability to borrow or save money without any constraint. To show the effect of an imperfect financial market, a borrowing constraint is introduced and the household can only borrow a fraction of *Y*, represented by α. In reality this scenario may be due to the lack of collateral with an economical value, which is representative for the poor. The borrowing constraint will bind when $\alpha Y_2 < b_L$ * i.e. the borrowing constraint is less then the actual need of net borrowing to be able to smooth consumption adequately. In this case $U'(C_{1L}) > U'(C_{2L})(1+r)$ i.e. the optimal utility of consumption in period one is larger than the optimal utility of consumption in period two due to the borrowing constraint. The corresponding welfare loss from the inability to protect first-period consumption is shown by the function:

$$\delta(Y_{1L};\alpha,Y_2)=U_L(.)-[U(Y_{1L}+\alpha Y_2)+U(Y_2-\alpha Y_2[1+r])]\geq 0 \qquad (2.1)$$

By using the envelope theorem, an increase in first period income reduces the effect of the borrowing constraint such that $\delta'_{Y1}(\cdot)\leq 0$. Similar to the Lagrange-multiplier approach the endogeneity of the borrowing constraint is captured explicitly.

With regards to the above example the question of how the household will choose the optimal amount of risk-taking is of interest. The borrowing constraint binds when income shocks are bad but not when income shocks are good, the household chooses the resources, β, to maximise expected lifetime utility:

$$\max_{\beta} 0.5U_H(\cdot)+0.5[U_L(\cdot)-\delta(Y_{1L};\alpha,Y_2)].$$

The first order condition simplifies to:

$$U'_H(\cdot)/[U'_L(\cdot)-\delta'_{Y1}(\cdot)] = -(s-l)/(s-h) \quad (2.2)$$

Even if reduced risk-taking lowers expected income, it will secure consumption when shocks are bad. This can be seen by the role of δ'(·) in the denominator of the left-hand side in equation (2.2). The presence of the borrowing constraint makes the denominator larger than it would be otherwise. Thus, the numerator must also be larger than otherwise. Expected profits are sacrificed for greater self-protection. By similar reasoning, $d\beta / d\alpha \leq 0$ i.e. less risk is taken as the borrowing constraint is tightened.

In sum, poor households with restricted access to consumption credit will pass up risky but profitable opportunities, even if they can secure adequate credit for production purposes.

With the same example as above Morduch (1994) shows how the lack of market solutions for financial services also exacerbates poverty through depletion of assets. In the case above, it is assumed that poor households smooth consumption by borrowing against future income. In this case imagine that the household can sell an asset A, for example a sewing machine.

Rather than taking $Y2$ as given, let,

$$Y_2 = f(A), f'(A) > 0$$

then, in the face of credit rationing and bad income shock, the household can sell the asset, where the gain in period one consumption is balanced by a fall in period two. The result will be that since productive assets are depleted to protect consumption today, poor households will face lower expected income in the future.

The two examples used to illustrate the cost of an imperfect market are based on the assumption that, purely economically speaking, poverty arises because it is not possible to borrow against future income. The next section will deal with the question of why formal financial institutions fail the poor. After that a section of alternative solutions for the problem of 'collateral' will be discussed in relation to informal and microfinance institutions. The last section in this chapter will link the three first sections to the implications of an imperfect market on poverty.

3.2 The Lack of a Formal Financial Market

Formal financial markets fail the poor when households are unable to borrow for socially beneficial projects that have an excess of social benefits over social costs, as discussed in the section above. This section will describe why formal financial markets fail the poor. The main literature used in this section are Hulme and Mosley's (1996) study *Finance Against Poverty – effective institutions for lending to small farmers and microenterprises in development countries;* Ray's (1998) article *Development Economics;* and Ghatak's (1999) example, of how a 'risky' borrower will raise the interest rate and by this exclude 'safe' borrowers, from the article *Group lending, local information and peer selection.* Alternative solutions for 'collaterals' will be discussed in the next section, 3.3, in relation to informal and microfinance institutions were Ghatak's example will be used again, for an explanation on how group lending also includes the 'safe' type, leading to a lower interest rate and a higher repayment rate.

Hulme and Mosley (1996) summarise four reasons for market failure of financial institutions. In the first case, borrowers are unwilling to borrow because of risk-aversion, although the expected value of their profits outweighs the expected cost of their investment, including interest and insurance payments. In the second case, no insurance institution is willing to compensate for lenders' and borrowers' risk-aversion by offering insurance against non-repayment due to natural hazard. In the third case of market failure, no lender is willing or permitted to pass on the extra cost associated with lending to unknown borrowers. The last explanation, case four, Hulme and Mosley mention that lenders may fail to lend to socially beneficial projects because they are not privately profitable. This may occur for two important reasons, either by a discrepancy between market prices and scarcity prices, or because of the inability of lenders to recapture the financial value of benefits, which they confer to other lenders.

Ray (1998) points to the problem of information and argues that there are two major reasons why banks discriminate against poor borrowers. Firstly, there is a lack of information regarding the use of the loan. Secondly, the information regarding repayment decisions is lacking due to weak legal enforcement systems.

Hulme and Mosely (1996) continue their article with the definitions of 'break-even' in a financial institution, which is of importance for a further discussion of alternative ways of collateral, such as group lending, which the informal and the microfinance sections deal with. The 'break-even' condition for any financial institution over a period of time is simply that net income must be at least equal to total expenditure. Lending to individuals with no collaterals with an economic value results in transaction costs being very high and leads to a high interest rate.

Formal lenders who follow the criteria of 'break-even' are governmental banks, commercial banks and credit bureaus. The 'break-even' condition will be different for a financial institution in a less developed country. The borrowing rate and the administration costs will be higher, which will impose a high interest rate. For example, if the borrowing rate is ten per cent, the administrative cost is five per cent, and the average default rate is 38 per cent, the 'break-even' interest rate would be 85 per cent. Often countries have an interest rate ceiling for banks to follow, which will give another reason why financial institutions are unwilling to offer a borrowing service. Even if the ceiling were to be removed, there is still doubt that institutions with interest rates close to 100 per cent would survive because higher interest may actually exacerbate the rate of default (Hulme and Mosely, 1996).

3.2.1 The Economic Implication of Moral Hazard and Adverse Selection

Both Hulme/ Mosely and Ray's arguments are based on the market failure of imperfect information due to moral hazard and adverse selection. Moral hazard is an *ex post* contracting situation and cause of transaction cost that occurs when one party's behaviour are poorly observable and when the incentives of the parties may be less than perfectly united. Adverse selection is a form of *ex ante* opportunism in which one party has personal information at the time of conciliation that reduces the value of the contract to the other party (FitzRoy, et. al. 1998).

Ghatak (1999) shows how the problem of moral hazard and adverse selection will discriminate against the 'safe' type of borrower due to high transaction cost which will lead to a high level of interest rate. Imagine two borrowers' that have no assets to put up as collateral. Both borrowers' are risk neutral, but one borrower is 'risky' and one is 'safe'. The 'risky' borrower will have a higher return on the investment, but also a higher chance to fail. The bank has no information about whether the borrower is a 'risky' or a 'safe' type.

The borrowers want to invest in a project that has an uncertain outcome and requires one unit of capital. If they choose not to undertake the project, then they earn a wage income m. The 'risky' borrower has a probability of success p_r and a net return R_r, and the 'safe' borrower has a probability of success p_s and a net return R_s. The 'risky' borrower is less likely to be successful ($p_r < p_s$), but have a higher return when succeeding. Assume that the expected return is equal for both 'safe' and 'risky' borrowers:

$$p_r R_r = p_s R_s \equiv \overline{R}.$$

Both investments are socially profitable in that expected returns of the cost of capital, p exceeds earnings from wage labour: $\overline{R} - p > m$. Because the borrowers lack collateral with an economical value the bank must set the interest rate high to be 'break-even' and cover the per-loan capital cost, p. Due to the information problem, the bank cannot distinguish between 'safe' and 'risky' borrowers and the interest rate will be set to cover the average probability to success in the population $r\overline{p} = \rho$. Since the bank cannot distinguish between 'safe' and 'risky' borrowers, they will both face the same interest rate, r.

As a result of the higher interest rate, the 'safe' types will have a lower net return on their investments and will only take the loan if the return will exceeds their fallback position $\overline{R} - rp_s > m$. By this logic the 'risky' types drive out the 'safe' types and this second best scenario ends with only 'risky' types borrowing, even if 'safe' types have socially valuable projects.

The lack of information about the borrowers and requirements of a break-even condition will, as discussed above, lead to a lack among the commercial banking sector in providing their services to uncollateralised individuals. In the next section alternative methods to secure repayment of loan will be discussed.

3.3 Alternative Financial Services

As a response to the lack of formal market solutions, informal and semi-formal financial institutions have been developed. This section will look into the informal solutions, such as money collectors and rotating saving and credit clubs, and into semi-formal solutions, such as microfinance. As discussed above, the problems of financial service provision to the poor could be summarised according to the lack of information. Three categories of how the lack of information will affect the banks' ability to secure their financial sustainability could be outlined. The first category is due to the problem of adverse selection; how the lender can get information about what kind of risk the potential borrower is. The second category is due to moral hazard; how to make sure the borrower will utilise the loan properly, so she will be able to repay the loan. The last category is about how to find methods to force the borrower to repay the loan, if she is reluctant to do so (Ghatak and Guinnane, 1999).

Table 3.1 outlines the different methodologies used by formal, informal, and semi-formal financial institutions in order to secure repayment. The following section, 3.3.1, will discuss these alternative methodologies used to get around the information problem as used by two informal financial institutions: money collectors and rotating savings and credit clubs. The last mentioned institution has played an important role in the development debate and is, to a large extent, the design behind microfinance organisations as will be discussed in section 3.2.3.

Table 3.1 Financial institutions and different repayment methodologies

	Formal	Informal	Semi-formal
Type of institution	• Bank • Insurance company	• Money collectors • Rotating saving and credit clubs	• Microfinance organisations
Methodology used	• Economical collateral • Interest rate	• Social collateral • Local information about the clients • Group-lending	• Social collateral • Group-lending • Frequent repayment • Progressive borrowing • Gender targeting

3.3.1 Informal Financial Institutions

In this section money collectors and rotating saving and credit groups will be discussed.

Money collectors are usually individuals that lend their own money and use alternative collateral as security. Even if low-income individuals may have a lack of collateral that has an economic value as demanded by banks, they may have 'alternative' collateral to offer; things that have value for a specific individual. For example, a farmer may have a plot of land to offer but the cost of selling the land in case of default is too high for the bank to consider. But there may be an informal lender willing to give a loan that considers the land as collateral for example, a landowner who has land close to the farmer may be interested in giving a loan. Another example is shop owners in urban areas that give loans to street traders in acceptance of their commodities as collateral. Another reason why informal moneylenders may succeed in lending money to poor borrowers refers to the problem of information as mentioned above; the moneylender has better information regarding the characteristics and activities of the customers (Ray, 1998).

Self-helping groups using lending and saving can be found all over the world. These institutions have a variety of different names and methodologies[1]. The main purpose is to get access to a sum of money faster than would have been possible with individual savings. The self-helping groups are rather simple in terms of functions, procedures and organisations, which have made them targets in the development debate. The groups are voluntary and autonomous with their own objectives, organisation patterns and rules. They have their own control and are independent of legal authorities (Bouman, 1995).

In the rotating saving and credit club, the deposits are collected and then either given to one of the group-members right away, or saved and then equally distributed when the cycle is finished. The life span of the cycle equals the number of the members. During the time of the cycle it is often possible to borrow against the deposit (Bouman, 1995).

Rotating saving and credit clubs build on social collateral that hinders members from failing to continue contributing or running away with the money. The groups tend to be homogenous according to income, occupation, and age and the members are, in the most cases, friends or neighbours. The homogeneity of the group reduces the information problem of sorting out 'risky' or 'safe' members. Social collateral and homogeneity will be further discussed according to microfinance in the next section (Bouman, 1995).

A rotating saving and credit club can have a daily, weekly, monthly, or yearly span. Recently in some countries, there have developed relations between the informal saving and credit clubs and formal banks, whereby the banks make accounts available to saving groups who are saving for a specific purpose, for example school fees (Bouman, 1995).

A model of how rotating saving and credit clubs will raise group members expected utility is further discussed under the section of poverty impact. The next section will look into microfinance and the economics behind group-lending.

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[1] In South Africa, a rotating saving and credit club is called a Stokvel (Bouman, 1995).

3.3.2 Microfinance Institutions

Microfinance institutions are non-governmental organisations that provide loans and saving possibilities to uncollateralised individuals in urban and rural areas in less developed countries. The main purpose and assumption of such activity is a reduction of poverty. They use alternative dynamic incentives to secure the repayment, such as group lending, frequent repayment schemes, progressive borrowing, gender targeting, and/ or compulsory saving schemes. Microfinance in this dissertation is classified as a semi-formal financial institution since they are dependent upon external funds to reach a financial 'break-even' situation.

3.3.2.1 The Economics of Group-lending

The method most commonly used by microfinance organisations is the group-lending that is an indirect method of reducing the risk of lending without 'economical' assets as collateral. Instead, the group lending mechanisms build on 'social' assets (Morduch, 1999). The basic point is that group members have more information about each other than the bank does and by self-selection sort the 'bad' borrowers from the 'good' ones through positive assortative matching (Ray, 1998).

Recall the example given of 'risky' and 'safe' borrowers by Ghatak (1999) in section 3.2 above, which showed that the lack of information about the borrowers leads to a discrimination against 'safe' borrowers. Ghatak continues in this example and shows how group lending may be instrumental in improving repayment rates, decreasing interest rates and raising social welfare. Recall that the bank has no information about whether the borrower is a 'risky' or a 'safe' type, but the borrowers have 'perfect' information about each other. The group lending methodology provides a way to decrease the cost of imperfect information that would be impossible with individual lending contracts.

Consider a voluntarily formed group of two individuals. They invest individually but they have a joint liability contract for the loan. Each borrower pays nothing if her project fails, and an amount r^* if her project succeeds. In addition, the other group member pay's a joint liability payment c^* if the fellow member fails in her project. Since 'safe' types always are preferred as partners because of a lower default rate, 'risky' types end up with other 'risky' types. In such a way it will work out that the group building will lead to assortative matching with the same types ending up in groups together. The group-lending contract provides a way to charge different effective fees to 'risky' or 'safe' types, even though the contracts have the same nominal r^* and c^*. The expected net return for a 'safe' and a 'risky' type is then:

$$\overline{R} - p_s\left(r^* + (1 - p_r)c^*\right).$$

If r^* and c^* are set properly the group-lending contract provide an effective way to price discriminate (Morduch, 1999).

Another way group-lending is beneficial for the lending institution is due to moral hazard. Group contracts may deter the borrower from taking risks that undermine the bank's profitability (Besley and Coate, 1995). The key is that in group-lending contracts, borrowers get incentives to engage in a safe activity. The bank can again 'afford' to lower the interest rate, raise the expected repayment rate, and raise expected utility (Stiglitz, 1990).

There are also benefits other than adverse selection, which encourage the financial institution to lend to a group. One is that the administration cost will decrease due to administration of one larger loan instead of a larger number of smaller loans. However, two problems related to group contracts flow from the above benefits. Firstly, while the bank will benefit by lowering administration costs and seek large groups, in large groups the pressure against individual failure may also decrease. A second problem is that group members may use each other and default rates may lead to social conflicts (Hulme and Mosely, 1996).

The following section will discuss other types of methodologies used by microfinance organisations to secure repayment rates.

3.3.2.2 Other Repayment Methods used by Microfinance Organisations

One direct method used by microfinance organisations to reduce the repayment insecurity is frequent repayment schemes. The most typical form is to collect installments every week at a point nearby the borrower's enterprise (Hulme and Mosely, 1996). The advantage of a frequent repayment scheme for microfinance organisations is that it screens out undisciplined borrowers, thus giving early warning to loan officers and group members. Explained more formally, since the repayment process begins before return of investment, weekly repayment necessitates that the household has an additional income source to rely on. Thus the bank is effectively lending partly against the household income, which benefits the bank as well as households with diversified income (Morduch, 1999). The condition to consider in this case is if the banks costs are increased by this kind of arrangement, i.e. the actual supervision of labour. If, however, the frequent repayment scheme brings about a more proportionate reduction in the default rate and improved cash flow for the organisation, then it may actually be affordable (Hulme and Mosely, 1996).

Another alternative mechanism to secure high repayment is progressive borrowing. The lending institution starts with a small loan size which progressively increases as the borrower proves a good repayment rate. The repeated nature of the action and the threat of being excluded, help maintain a high repayment rate. This mechanism is more beneficial in areas where individuals are less mobile. In an urban environment, borrowers may use opportunities to borrow without collateral and fail to repay the loan. Another critique of this method is that the incentives to pay back the last loan may be low, since there are no more incentives to perform well (Morduch, 1999).

An additional dynamic incentive that needs to be mentioned is the advantage of lending to women due to ex post moral hazard. One reason for this may be women's lower mobility. Also, women may feel a stronger responsibility for money management since their misfortune reflects upon the entire household. The high success rate of repayment for microfinance that only have women clients may also be due to the fact that women historically and culturally have been discriminated against, and excluded from the financial market (Morduch, 1999).

In the last decade the trend in microfinance has been a change from pure credit institutions to institutions that also include savings (Fiebig, Hannig and Wisniwski, 1999), as described in chapter two. Both compulsory and voluntary saving schemes may create a win-win situation for the lender and the borrower. Three arguments may be highlighted. Firstly, compulsory savings schemes provide a partial form of loan insurance. Savings increase both the size and the liquidity of the saver's net worth, which provides an effective insurance to the saver against consequent default and insolvency by the borrower. Secondly, saving may act as a screening devise. The existence of a savings deposit will provide the lender with free information by distinguishing those potential borrowers who are most likely to repay. A good saver may get better access to further loans. Thirdly, the borrower may feel more obligated to repay instalments and, in so doing, the default rate may decrease (Hulme and Mosley, 1996)

Thus far this dissertation has presented evidence for why the lack of a formal financial market may increase the problem of poverty. It has also discussed why the commercial banking system is failing the poor, and provided a brief overview of alternative financial solutions such as informal institutions and microfinance organisations. In the next section the impact that rotating saving and credit clubs and microfinance services may have on poverty will be discussed.

3.4 The Poverty Impact

This section will connect the above discussion and outline the effect financial institutions, with a special focus on microfinance, may have on poverty reduction in the form of increased income, asset building and welfare. The section ends with a discussion of what constitutes 'good' financial institutions in relation to poverty reduction.

3.4.1 Microfinance and Poverty Reduction

As was discussed above, rotating saving and credit clubs provide a meaning to joint savings to meet expenditures related to the life-cycle events or indivisible goods. Besley, Coate and Loury (1993) describe a model with indivisibilities to show how rotating saving and credit clubs will increase the welfare among its members. The sum is that welfare increases by group saving, because financial intermediation reduces the members' utility cost compared to individual savings. This is also applicable for how microfinance organisations impact on poverty reduction.

High repayment rates and successful lending, of microfinance organisations world-wide, have accumulated enthusiasm from donors and international development organisations. However, the 'real' impact on poverty reduction has rarely been tested, which may be due to the complexity of the poverty concept. Changes in income could easily be measured, but even an increased rate of income does not necessarily show real influence on poverty reduction. An organisation that lends to individuals that are around or above the national poverty line may show an increase in income because the borrowers are able to use the loan in productive investment. On the other hand, organisations that target individuals under the poverty line may not show as large an increase in income because the borrowers use the loan for smoothing consumption. Yet this second case may in fact have a 'better' impact on 'poverty' alleviation than the first (Hulme and Mosley, 1996).

Hulme and Mosley (1998) show in their study of 13 microfinance institutions in seven developing countries that there is a systematic positive relationship between impact and household income, which may vary in level according the design of the methodology used. Two measures are used to decide financial performance among the institutions: the Subsidy Dependency Index[2] and the proportion of loans more than six-month months in arrears. The two measures were correlated. For example, the lowest indices of subsidy dependence have the lowest late repayment rates. The financial sustainability correlates not only with the market interest rate and the availability of saving rates, but also with the frequency of loan collection and the existence of 'material incentives' to both borrowers and those employed within the organisation to maximise repayment rates.

If the better performing financial institutions become a benchmark in further development of microfinance organisation, then the core poor may gradually become

[2] The Subsidy Dependency Index, SDI, measures the extent to which interest rates would have to be raised to reach a 'break-even' condition in an environment free of all subsidies (Hulme and Mosley, 1998).

excluded from the schemes and the net impact on poverty reduction will not be as efficient. Alternative methodologies, such as flexible consumption loans and voluntary saving schemes may increase the average rate of return on loans even for individuals under the poverty line. To really measure the impact on poverty the income measure has to be extended to include vulnerability (Hulme and Mosley, 1998).

Hulme and Mosely (1996) ask the accurate question of why income-generating programmes with poverty reduction goals have a hard time targeting the core poor. They also give two possible answers. First, it is an administrative problem to target the poor, due to that there are high information costs in finding the 'real' poor. The second explanation is due to political reasons. For example, non-poor individuals with political power may insist on becoming borrowers and in so doing, push borrowers out of group schemes designed for poor, who have little or no political power.

The AIMS[3] studies, by Cohen and Sebstad (2000), Dunn, Kalaitzandonakes, and Valdivia (1996), Barnes (1996) and Chen and Dunn (1996), have analysed the impact microfinance may have on assets in relation to poverty reduction. According to Barnes (1996) microfinance programs may have the following beneficial consequences:

- The loan may be used directly or indirectly to accumulate an asset, which may lead to increased income and further accumulation of assets. The benefit derives from a loan-based acquisition of assets and depends on the rate of return to capital versus the loan rate and the degree of leverage in financing the acquisition of a consumer durable.
- The loan funds may assist a household to better manage its existing asset base or reduce its liabilities. Access to credit may enable households to meet the demand for cash without having to sell important assets.
- Access to credit may permit households to take risks.
- Microfinance programs may have a positive effect on savings if they offer voluntary saving schemes.

[3] Assessing the Impact of Microenterprice Services, AIMS.

- A microfinance client is likely to gain self-esteem and greater control over resources as a direct or indirect result of program participation. Increased empowerment, in turn, is likely to influence the accumulation of more assets.

With regards to possible links between children's' education and household access to credit, the impact was measured through increased expenditures on school fees, school attendance, children's school enrolment, or educational attainment. In some cases in the AIMS study, credits had an impact on increased boy's schooling. One study suggests that credit may have a negative impact on child education, because of increased demand for child labour when family business expands (Barnes, 1996).

According to Barnes (1996), the benefits with a voluntary saving scheme are likely to lead to a shift from non-interest bearing cash saving to interest bearing savings instruments, an increase in the absolute amounts saved, lower risk to saving and lump-sum expenditures on assets or consumption. Microfinance institutions may lead to reduced vulnerability by increased income, changing the composition of individual and household assets, and increasing women's human and social assets.

Thus in sum, rotating saving and credit clubs and microfinance services can have a clear impact on poverty and on the well-being of the clients. There is however, also a risk to being involved in group-lending contracts, which include factors such as social exclusion and debt. The next section will discuss the concept of 'good' financial solutions.

3.4.2 'Good' Financial Solutions

There has been a longstanding debate over the effects of risk management through market versus non-market institutions. Neo-classical economic theory argues that an imperfect market will lead to welfare costs. A development approach may argue that changing from informal to formal institutions may lead to increased vulnerability in the short run. Wright (1999b) and Morduch (1995) criticise the weakness and high costs of informal saving, while Dercon (2000) on the other hand, points out that the introduction of formal ways of risk sharing may break up informal traditions and lead to increased vulnerability. Ruthven's (2002) study of the financial services used by dwellers of an informal settlement in West Delhi also points out that financial institutions other than formal may serve as a more important way to secure against risks in certain circumstances. Institutions mentioned as most important in the case of West Delhi are networks of relationships. Both these arguments underline the need for the development of well-designed financial services. The key question is as Townsend (1995) points out, whether market and non-market institutional arrangements are jointly providing an optimal allocation of risk bearing given the degree of idiosyncratic and covariant risk.

Another discourse surrounding the literature is the debate about the role and function of microfinance organisations according to economic sustainability versus poverty reduction. As was discussed above, according to Hulme and Mosley's (1998) study the impact on income among the 13 microfinance organisations researched showed that institutions with a high financial sustainability measure also had a high change in income among its members. This does not, however, imply that they have a better poverty target than institutions that have a higher SDI. If the members are around and above the poverty line they may be able to undertake productive investments and greater risks than individuals that are under the poverty line, thereby generating a higher income. This finding has important implications for the ability of microfinance institutions to reduce poverty in relation to the sustainability versus poverty reduction debate. If the financially better performing institutions become a benchmark in the further development of microfinance organisation, then the especially core poor may be excluded from schemes and the impact on poverty reduction unlikely to be as efficient.

As a final conclusion of what factors include a 'good' financial institution; it should have a high poverty target, should be financially sustainable, and should be a tool by which the clients can lower their levels of vulnerability and develop their businesses. The following chapter will give a background to the case study and put women street traders in South Africa in context before the findings will be presented.

4 INTRODUCTION TO THE CASE STUDY

This chapter gives the background context for the research and includes a literature review of the informal economy, policies and legislations in the SMME[4] sector, women street traders, and the financial sector in South Africa. The statistics for saving behaviour in South Africa are based on consumers with permanent income and formal occupations, and thereby exclude workers in the informal sector. The formal view of saving capacity among low-income households in South Africa is thereby virtually non-existent. This is one of the reasons for the lack of financial services provided to low-income individuals in South Africa today. Other reasons relate to the historical and political environment.

4.1 The Informal Economy

The development in global labour trends since 1970 has been growth in atypical employment due to globalisation and urbanisation. Employment has taken more informal and flexible forms in both developing and developed countries (Portes, Castells and Benton, 1989). Moser (1998) describes two long-term trends in the composition of the household. Firstly, the global trend tends to be an increase in the number of households headed by women, and secondly there have been an increased number of extended households. The poorest households are often extended households, which make a high dependency ratio and low per capita income. Chen, Sebstad, and O'Conell (1999) argue that a shift from formal into informal employment is a general feature of many transition economies.

As a consequence of increased global integration, production patterns have changed along with the labour structure. The recent trend in policies related to the labour market is a 'hands-off' approach with less direct government intervention and regulation. As a result, women appear to have moved from the manufacturing sector into the low-wage informal sector. This can be explained by structural factors, such as poor investment in women's human capital (Moser, 1998).

Lund (1998) uses the International Labour Organisation's definition, from 1972, of the informal sector and according to this definition the informal sector is characterised by ease to enter, small scale enterprises, family ownership, the use of labour-intensive technology, and use of indigenous resources. Mehra and Gammage (1999) describe informal activities in a rural and urban context. Rural informal activities include farming, cottage industry, tool making, and garment making. In urban areas, informal activities mostly concern street trading and small-scale manufacturing enterprises.

The trends in the labour market in South Africa are consistent with international trends. However the apartheid history is another factor that has shaped the development and the nature of the informal economy in the country. As a result, a large number of South African women are engaged in the domestic service sector instead of other micro enterprise activities (Valodia, 2001).

The Department of Trade and Industry aims to increase the competitiveness of the local economy in the global market. The practice of rapid fluctuations in workforce size has resulted in a growth of flexible work in the form of independent contract workers, temporary workers, and part-time and casual workers. The re-segmentation of the labour sector is moving from one based on racial segregation towards one based on class segregation between well-paid formal workers and low-paid informal workers. The problem is that now the majority of flexible and informal workers tend to be women, and they occupy the least lucrative and most vulnerable positions (Valodia, 2001).

Lund (1998) describes the link between gender, race and the position of women in the labour market in South Africa. Lund concludes that women do most of the unpaid labour connected to the household; that there is a bias against women in access to skilled works and training; that women are over represented in rural agriculture; and that women also have a more narrow perception than men about what kind of work they are able to do.

Valodia (2001) states that while the informal sector has been researched from many different aspects, the state response to gender issues and the political implications of this in the informal sector in South Africa today is still not well known. The Industrial

[4] The Small, Medium and Micro enterprise sector

and trade policies of South Africa do not take due cognisance of the structural position of women in the labour market. As a result, policies fail to target the growth of the informal and flexible market. Employment in the formal sector is declining as the unemployment rate increases and the informal economy expands. Statistics show that 57 per cent of workers in the informal sector are women and 70 per cent of the women are engaged in low-skilled work in domestic and elementary occupations such as street traders (Valodia, 2001). The White Paper on the SMME sector estimates that one-quarter (four million) of the workforce in South Africa is engaged in the informal sector (Lund, 1998).

4.2 Policies and Legislation in the SMME Sector

At the macroeconomic level, the Government's (1996) Growth, Employment and Redistribution (GEAR) strategy has a dual effect on the labour market. With its emphasis of neo-liberal thinking, it protects the formal sector with high minimum standards and relatively high wage levels while for 'the rest' there are low standards and no minimum wages (Valodia, 2001). There is generally a conflict of interest between the aim to protect vulnerable workers and the policies that promote small enterprise development through market liberalisation. To develop small enterprises, labour legislation needs to be flexible and less costly for the entrepreneurs. But it is also in this sector that the workers are more vulnerable and need social protection (Valodia, 2001).

The Department of Trade and Industry is responsible for the implementation of policies regarding the small, medium and micro enterprise (SMME) sector. The White Paper covering the SMME sector distinguishes between four enterprises. The survivalist enterprises are characterised by individuals unable to find a job. The next stage is that of micro-enterprises, which consist of owners, family members and maybe one or two employees. The next two steps are small and medium enterprises. There are different policies and support strategies for each of the different levels. Even if the White Paper on SMME has as a key objective to support all women in all business sectors, and also to recognise that most women are concentrated in the survivalist sector, the Department of Trade and Industry in reality offers very little support to women (Valodia, 2001). The survivalist enterprises tend to be treated as an invisible sector within the national policy (Lund, 1998).

Three institutions have been set up to support the development of the SMME sector. The Centre for Small Business Promotion (CSBP), which has as its key role to implement the small business policies and strategies. The Ntsika Enterprise Promotion Agency is responsible for non-financial assistance. Khula Enterprise Finance Facilities provides financial services to the SMME sector. These institutions, set up to support the SMME sector, are clearly not targeting the survivalist sector. Additionally, the financial institutions set up to help micro entrepreneurs have no real relevance for survivalists. This is a critical barrier, especially for the development of women survivalists in the informal sector (Valodia, 2001).

CSBP, Ntsika, and Khula are located in the economic departments of the national government. The Local Business Support Centres are being established at the local government level (Lund, 1998). Durban has a separate department for informal trading, the Department of Informal Trade and Small Business Opportunity, DITSBO. Durban is also the city in South Africa that has secured the most funding for infrastructure development with regards to the informal sector (Skinner, 1999).

The Labour Relations Act (1995) regulates the relation between employers and employees and also between trade unions and employees. The problem, for the survivalist sector, is that the Act only regulates clear and concise relationships between workers and their employees. Therefore, the Act excludes the majority of unorganised workers and almost all women in informal and flexible occupations. The Basic Condition of Employment Act (1997), on the other hand, is supposed to regulate the minimum standards for those who are not subject to collective bargaining. All workers, including vulnerable groups like farm and domestic workers, are included in this legislation. The Act regulates minimum wages, occupational conditions, and working hours (Valodia, 2001).

The Business Act introduced in 1991 recognised street trading as a new area within the informal economy. The Act sought to reduce the powers of local authorities to develop laws that could restrict street trading. In 1995, the Act was devolved to a provincial level. Local governments and the policies for local economic development thus currently have an important influence on street traders (Skinner, 1999).

4.3 Women Street Traders in Durban

Lund's (1998) article shows that there are approximately 19 000 workers involved in street trading in the whole Durban metropolitan area and of these, 60 per cent are women. The major percentage of women working as street traders in Durban falls into the 25 to 49 years age group. The education level within the group is low and there is a clear link between low levels of education and working in the informal economy, however the younger women tend to have more years of education than the older women. Women street traders also tend to be the main breadwinners and the heads of their households. Problems the street traders face are related to accommodation, health, childcare, and the risk connected to their business, such as lack of adequate infrastructure and exposure to crime. Women engaged in the informal economy face risks related to their daily lives and their businesses, and the most important issue for these street traders is how to protect themselves against, and cope with, risks they face. The current government structure is not providing sufficient social protection for women working in the informal economy, despite some being eligible for grants, such as the Old Age Pension, the Disability Grant, and the Child Support Grant (Lund, 1998).

Skinner (1999) explores the institutional environment that street traders face in different cities in South Africa. She notes that there have been substantial changes in the policy regarding women street traders since the transition to democracy in 1994. Examples of improvements include women's movements, the recognition of the informal economy in South Africa's economy, and the effort to integrate street trading into urban planning. In order to push for the integration of the informal economy into government policy, as well as to allow for women street traders to make their voices heard, it is important that street traders be organised and encouraged to express their common interest. Lund and Skinner (1999) discuss the need for, and the barriers to, organising women in the informal economy. One example of a trade union organised by women in the informal economy in Durban is the Self Employed Women's Union (SEWU), which is a trade union for women with no permanent job, but who are working in one way or another. The union, which is run by democratic structures and is controlled by the members, organises women by building unity among those whose work is not recognised; by working as a negotiating unit and developing negotiating skills; by assisting with legal advice; by assisting in solving problems such as child care; and by developing lobbying and leadership skills (SEWU, 1997).

Skinner (2000) has analysed the support needs and the current policy support available for street traders in Durban, with a focus on training. She argues that training can enhance productivity and lead to higher incomes and also assist some poorer people over subscribed activities. Training may also help people cope with risks in times of crises and in general, give better survivalist skills. In Durban, the Metropolitan Council established a Local Business Support Centre, LBSC, in 1997, which supports micro- and small businesses. The survivalist sector was, however, excluded because of no existing expertise in the sector, however at the time LBSC was established, there were discussions about a special support programme for the excluded sector, which has since been shelved due to other pressures (Skinner, 2000).

As a result of the lack of government protection and support for the survivalist sector, financial services as an optional risk management tool specifically for this sector will be discussed in the next section.

4.4 Provision of Financial Services

Many obstacles face individuals striving to make a living off what they can trade on the street. Skinner (2000) reveals that 40 per cent of women street traders mentioned lack of capital as being a major obstacle. Due to the lack of a formal financial market that provides services to the survivalist sector, there is thus a need for policy reforms that address women's financial constraints. Street traders are without social protection and policy support for the development of their businesses, which makes the environment in which they are working and living in extremely vulnerable. As an alternative to government protection and business support, financial services could provide street traders with credit, savings and insurance facilities. Due to historical/political reasons and the risk involved in providing financial services to people with no assets, there is a lack of access to formal financial services for low-income individuals as the financial institutions are structured today. There are two major roles the financial market could play: Providing saving facilities as a form of insurance against risks and providing credit and support for the development of the survivalist businesses.

Related to social security is the use of savings as a social protection strategy. SEWU's membership survey 1997 showed that 46 per cent of the members belonged to a saving club, locally known as a stokvel. It also showed that urban members are more likely to belong to a saving club than rural members are (Lund, 1998).

The critical point to delivering viable credit at this level is the importance of protecting the clients and at the same time creating a legal system, which is conducive to the development of such financial institutions. The regulation around financial services is important because of the high risk of illegal credit institutions and other debt traps (Valodia, 2001). Khula guarantees loan provisions for SMMEs and lends to retail financial institutions. Khula's regulations have made it hard for microfinance institutions to register with them and to provide financial services to the SMME sector.

Skinner (2000) concludes that financial service providers are reluctant to service low income enterprises if significant incentives are not given. However, there is not just a need for informal financial providers, formal banks also need to become more user-friendly to survivalists and small enterprises. The government has to put regulations in place that put pressure on banks in regard to this, for example by placing target percentages of poorer clients. International examples show that the provision of saving services need to be such that the money saved is easily accessible, the institution staff are friendly, small deposits are accepted and that the institution also offers related financial services (Skinner, 2000).

5 METHOD OF THE CASE STUDY

The case study conducted has as its purpose to analyse the impact of financial services as a strategy to handle income risks and reduce vulnerability among women street traders in Durban, South Africa. In order to keep a strong focus for the study, demarcations have been done according to the type of financial institution and service provided. Thus the institution chosen is a microfinance organisation, FINCA, and specific service is saving/deposit schemes. Section 5.1 discusses the choice of method, in 5.2 the choice of financial institution is outlined, section 5.3 discusses the sample for the study and 5.4 the source of information, and the research questions are outlined in 5.5.

5.1 Qualitative method

The model suggested by Morduch (1994) in the theoretical framework that analyses the impact of financial services on poverty reduction is quantitative and includes statistics of income levels, assets and the institutional performance. The welfare cost of an imperfect market could also, as Morduch (1995) suggests, be measured through the demand for insurance, the level of savings under uncertainty, and other welfare measures. An impact study could be done either through a quantitative or a qualitative study, the differences are thus that a quantitative study answers the question of 'how' and a qualitative study focus on 'why' (Svenning, 2000). For the purposes of this case study, it is neither the performance of financial institutions nor the cost of an imperfect market that are the focus, but rather the impact financial services have on the street traders ability to improve their well-being. The requirements of this case study thus indicated the need for a qualitative rather than quantitative method.

Well-being can be analysed though income levels, enterprise development, asset levels, and household status with regards to health and education. These factors could also be measured through a quantitative survey study, however there are three factors of note that could lead to problems in a large quantitative survey. Firstly, the complexity of vulnerability would be hard to capture and measure through a questionnaire. Secondly, there are some technical issues, such as language barriers and illiteracy, which would make a questionnaire type survey extremely difficult in a country such as South Africa. The last factor concerns the time, scope and resources used for the dissertation. A quantitative study would need infinitely more time and resources than a focussed qualitative study.

Another reason for choosing a qualitative study is that the concept and understanding of poverty has become more complex and changed from a focus on income and consumption measures to a focus that also includes assets, risks and vulnerability. The emphasis on the ability to cope with risks via assets, on human capital and informal insurance, and on opportunities available, marks a convergence of different disciplines and bridges the gap with more qualitative approaches. A qualitative method will, in this case, capture the complexity and dynamics of street trader's coping strategies and saving behaviour, and will thus help reach a higher level of validity.

The qualitative method is based on focus group discussions and individual in-depth interviews, in this instance with women street traders that are members of the microfinance organisation, FINCA. To analyse the impact of financial services on saving behaviour, risk management and business related issues for women street traders, two groups are chosen to highlight the differences; one group of women that have used financial services for at least a year and one group that have not yet started to use the financial services.

5.2 The Choice of Financial Institution

The main reason to base the study on clients from a microfinance organisation is that it is a growing development approach. Another reason is simply that formal banks exclude street traders as customers due to the requirements of formal income needed to open accounts. The microfinance organisation chosen is the Foundation for International Community Assistance or FINCA. FINCA is a non-profit organisation with a mission to create employment and raise family income. FINCA is an international organisation with activities in several countries and with a head office in Washington DC, USA. FINCA's headquarters in South Africa is in Durban but its clients are spread throughout the peri-urban and rural areas of Kwa-Zulu Natal province.

FINCA's credit schemes are based on a solidarity group lending approach and are only available for women. The whole group is responsible for the repayment of loans and ensuring that the credit schemes work properly. Since FINCA is not registered as a formal bank they are not allowed to name their saving services for 'savings' and instead they offer 'deposit' facilities for their clients who use the credit schemes. There are two compulsory deposit accounts, one group investment fund (GF) and one personal investment fund (PIF).

5.3 The Sample

The sample consists of three group interviews and 27 in-depth individual interviews. The group interviews were conducted only with 'old' microfinance clients to get a basic understanding and background knowledge for the individual interviews. Within the group of individuals there are two subgroups relating to how long the clients has been using financial services. This created one sub-group of 15 'old' clients that have access and are currently using the credit and deposit facilities accessible, and another sub-group of 12 'new' clients that have just joined the organisation and do not yet have access to services. It was not the same clients that participated in the group interviews that took part of the individual interviews. The individual interviews were selected randomly from clients waiting for their credit groups. The women were participating voluntary.

There were several reasons for choosing to focus on women street traders. Firstly, poverty studies have shown that women are a better target in poverty reduction strategies than men (Hulme and Mosely, 1996). Many microfinance organisations world-wide have, as a result of this fact, as well as the fact that women have demonstrated higher rates of loan repayment, chosen to focus on women. Another reason is that a higher percentage of the street traders in Durban are women (Lund, 1998). Both the 'old' and the 'new' sub-groups of clients are from a similar socio/economic background and work in the informal economy as street traders in the city centre of Durban.

The reason for choosing an urban environment instead of a rural setting is that most studies done about risks, risk management and coping strategies, except Moser's

(1998) study of urban poverty reduction strategies, are based in a rural setting, thus creating a gap in the literature. One reason for this is that a higher percentage of the world's poor that live in a rural environment. Additionally, the first microfinance institutions started as village banks with the purposes of helping farmers reduce income risks due to weather conditions. However, South Africa has a growing informal sector in urban areas, which also motivates for the choice of an urban study. The choice of street traders in the informal economy is based on the lack of financial services and government protection that this sector faces, which results in high risks and vulnerability for the people involved.

5.4 The Source of Information

All interviews took place at the chosen microfinance organisation's meeting hall in Durban city centre. The interviews followed an open interview questionnaire and took half an hour to one hour each. The questionnaire was fairly strictly followed and all questions were captured at all interviews. A translator was used since most of the women were first-language Zulu speaking, although most of the women did understand some English and the translator was only needed to explain some answers. One translator was used for the group-interviews and another translator was used for all the individual interviews. All the interviews were anonymous in order to allow the client to speak freely and to not be held responsible for negative comments regarding FINCA.

There are a number of factors that might have had an influence on the nature of the answers given during the interviews. These need to be noted. Firstly, the history of Apartheid in the country, with its resulting unequal power relations, may have meant that a white interviewer from the northern hemisphere would have elicited different responses than a local black interviewer. Additionally, the location of the interviews may have affected the nature of the responses since the women might have wanted to portray themselves as 'good' clients. Even if the interviewee participation was totally voluntary, the desire of the women to perform well within the organisation may have made them extremely reluctant to respond negatively or to question the role of the interviewer. Lastly, the sensitive nature of financial issues may have had an influence on the answers given.

The characteristics of the groups interviewed are not comparable to the characteristics of the individual interviews. All three groups interviewed started their loan cycles in year 2000 and are selling fruit and vegetables at Durban Station and Victoria markets. All these groups have been very successful in repaying their loans. They have no personal bank accounts but they do save in stokvels. The group interviews were done a couple of months before the individual interviews in order to inform the direction and basis for the individual interviews and are therefore not presented separately in the findings.

The benefits to doing the interviews at FINCA's meeting hall were that there were no disturbing moments and other interactions occurring during the interviews. There was also no stress for time since the women had already set-aside time to meet with FINCA, but as pointed out above, one limitation was clearly that the women may have thought that they needed to take part in the interviews in order to get good records for FINCA.

5.5 Research Questions

Key Question: Can financial services, savings in particular, serve as a way to handle income risks and lower vulnerability among women street traders in Durban, South Africa?

Hypothesis: Appropriately designed financial service, savings in particular, may assist in reducing the vulnerability to income risks of low income individuals and households.

The interview questions were based on the four main questions:

1. What is the nature of risks relating to income and expenditure?
2. What strategies are used to deal with risks and to reduce vulnerability?
3. How and why do people save money?
4. What is the role of financial institutions in providing saving facilities?

6 FINDINGS FROM THE CASE STUDY

The findings will be presented with regards to the two different groups of women; 'new' and 'old' clients. The division is done to point out differences between women that have been engaged in financial service for at least one year and women that just started. Some of the findings will be presented graphically. The chapter will be divided into four main sections. In section 6.1, findings regarding income and consumption will be outlined. Section 6.2 deals with saving channels, motives of saving, optimal saving institutions, and link savings to risks. Section 6.3 will outline the role and impact of the microfinance organisation FINCA. In the last section 6.4 a summary of the findings will be presented.

6.1 Findings Regarding Income and Consumption

Income discussed in the research considers the actual cash flow the street traders earn every week. The income section is divided into source of income, level of income, and factors that effect income. Factors that effect income are described as different constraints/risks to income and are presented in table 6.1. The findings regarding consumption constraints will be separated into areas with regards to household, education, future, and enterprise, as shown in table 6.2.

6.1.1 Source of Income

The majority of the women had no other source of income than what they earned daily from their businesses, except women with young children who received a child grant. The majority were the head of the household and had no husband or partner to contribute to the income. The source of income can be divided into two main groups depending on skills and capital involved. In the first group, the low skill/capital group, women buy stock and sell the goods on the street. This group includes fruit and vegetables traders, traders that sell various commodities, and traders that sell second hand clothes. The second group involves a higher degree of skills and capital and is divided into fashion designer and tuck shop[5] owner. The fashion designers owned a sewing machine and designed their own clothes that they either sell themselves or employ a sales person. The tuck shop owners owned a shop and had a higher range of commodities.

Figure 6.1 shows the division of income source between the total sample and also the division of 'new' and 'old' clients according to occupation. The figure shows that 'old' clients are more likely to be engaged in a high skill/capital activity and 'new' clients have a higher representation in low skill/capital activities.

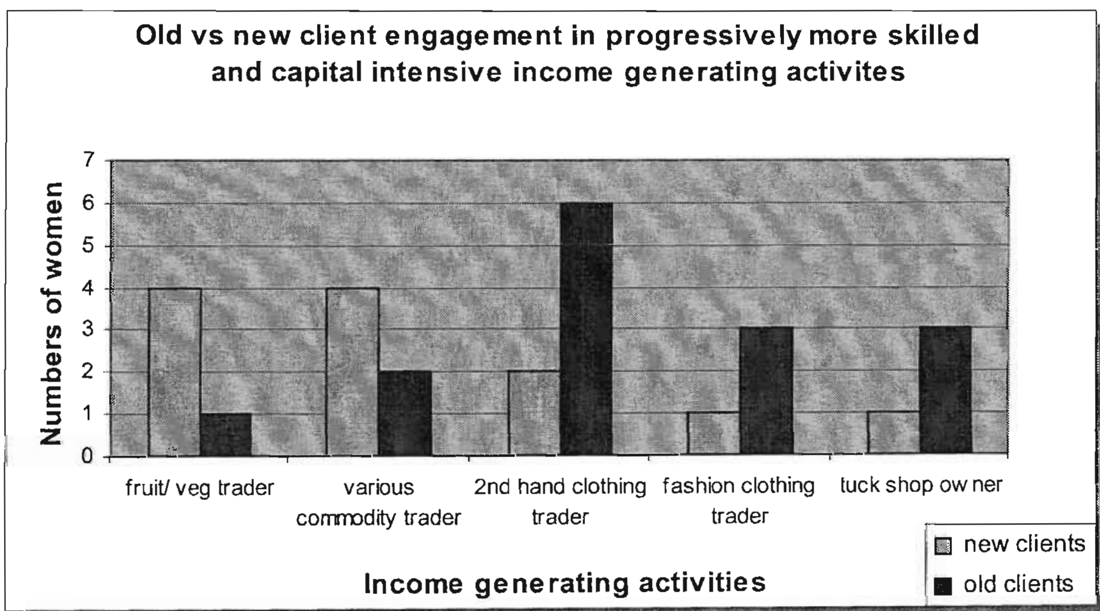

Figure 6.1. Income generating activities among 'new' and 'old' clients (n=27)

6.1.2 Levels of Income

The research showed that there is a relationship between the level of skill/capital activities and the level of income as is shown in figure 6.2. High skill/capital activities tend to have a higher return of income and low skill/capital activities a lower income return.

[5] A tuck shop is a simple but permanent stall.

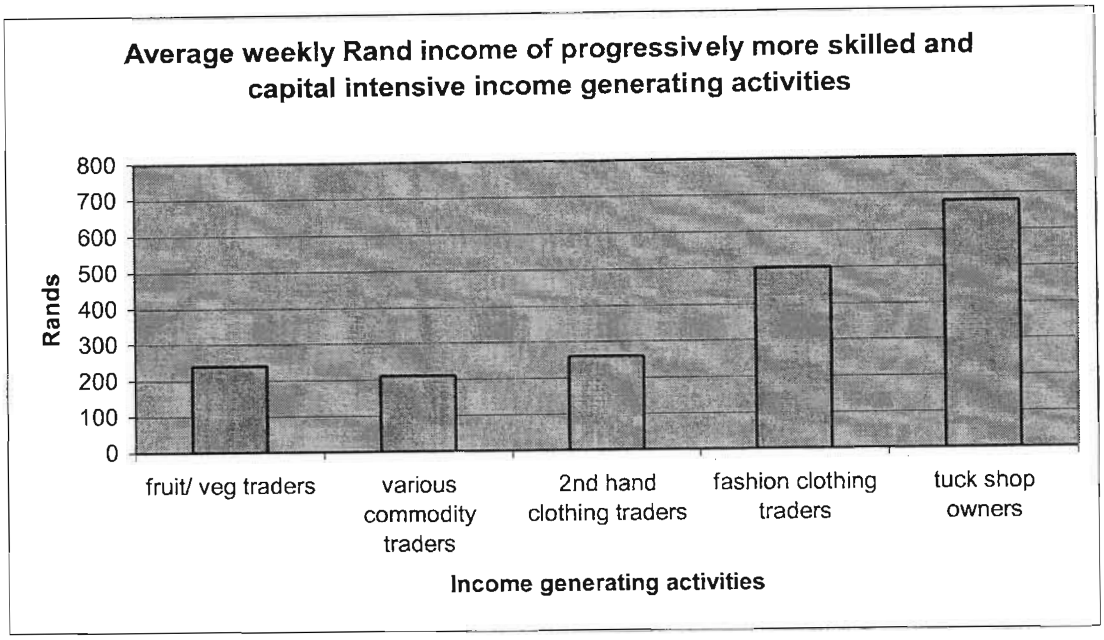

Figure 6. 2. Average level of weekly income in Rands (n=27)

6.1.3 Risks Related to Income

Table 6.1 is a summary of risks related to the source of income. The rows show differences regarding the five types of enterprise groupings. The columns show differences in 'new' and 'old' clients.

High skill/capital enterprises were more dependent on the state of the economy. If the unemployment rate is high and people in general have less money, their goods are not a priority for the consumer. Low skill/capital enterprises sell basic goods that people always need and therefore they were not affected by the state of the economy.

Risks associated to the market were related to strong competition, unstable market prices, and problems with business agreements with the customers. Especially the second hand clothing traders thought it was to high concurrence. The traders make oral instalment agreements with their customers. The agreement only builds on mutual trust and there are no legal or regulation systems to secure the repayment. Oral instalment agreements are most common among the clothing traders, but occur in all enterprise groups.

There were high risks regarding an unbeneficial stock. The traders often bought stock in bulk and they did not know if it was a good or bad stock. The second hand traders bought a bulk of stock with different clothes and were lucky if they got children's clothes since they sell better then other clothes. Another risk regarding the stock is the engagement in FINCA. If you fail to pay back instalments, FINCA may reclaim the stock as a repayment security.

The weather conditions affect all trading that takes place outside. Rain damages the clothes and sun damages the food. It is hard to find cover for the stands in both sunny and rainy weather. A sunny day tends to bring more people out to work and shop.

Time is one factor that affects the level of income in all enterprise groups. All types of businesses are dependent on customers to buy their products. Customers, on the other hand, are dependent on wage income. People often get paid in the end of the week, in the end of every second week, or in the end of the month. This makes weekends better business days and especially the last weekend of the month. Concerning the year, October to December are high-income months and January is the lowest income month. Also holidays and school breaks are times for good business. There were some differences between the enterprise groups regarding 'good' times depending on what they sell. The low skill/capital group were more dependent on people's payment days and the flow of customers passing their stands. The traders selling goods for tourists were dependent on holidays and tourist seasons. The traders involved in the second hand clothes and fashion design follow the yearly seasons and had a higher income level during October to December.

Crime was very common among all groups. The most frequent crime was the risk of getting the cash balance stolen in the end of the day. The crime situation also makes the traders close their businesses early. This applies especially to the tuck shop owners that lose a fair amount of income because they cannot have their tuck shops open at night. Tuck shop owners often need to bribe the police to be able to sell alcohol without a permit, which can be very expensive.

Another income constraint concerned trade permits that were needed to sell goods at a certain site. These permits are expensive and sometimes hard to get. As a result, trading was taking place illegally and the traders will have problems with the police. As a solution the traders hide their stock and help each other to look out for the police.

Table 6.1. Income risks

	New clients	Old clients
Fruit and vegetables	• Stock may go bad • Lack of income to buy new stock • High cost of business agreements • Customers are unemployed • Crime	• The weather factor effects the condition of the fruit and vegetables • Unbeneficial stock
Various commodities	• High concurrence at the market • Keep the price lower then the average market price • Lack of income to buy new stock • Problem with the police. Lack of trade permits	• FINCA may confiscate the stock if failing with repayments • Not enough income to buy more stock • Problem with the police. Lack of trade permits
Second hand clothes	• High cost of business agreements • Risk when customers order clothes and don't pick them up • No access to safe savings opportunities • High cost of transport. Need to travel far to find better markets • Unbeneficial stock (no children clothes)	• High cost of business agreements • Problem with the police. Lack of trade permits • The weather condition may ruin the (clothes) stock • Crime • Unbeneficial stock (no children clothes and little to offer) • Income loss when sick
Fashion designer	• Not enough income to buy fabric for the clothes, so not enough clothes to sell • Crime	• High cost of business agreements • Income risk when the sewing machine brakes down • Income loss when sick • Customers are unemployed • Too high concurrence at the market
Tuck shop	• Unbeneficial stock • Food stock goes bad	• Lack of income to buy new stock • High stock prices on food • Need a permit to sell alcohol • Bribe fees to police • The weather condition. • Crime • Lost income due to crime at night. Need to close early.

6.1.4 Expenditure Constraints

Table 6.2 points out the differences regarding expenditure constraints between 'new' and 'old' clients divided into household, education, finance, and enterprises. There was not a big difference among 'new' and 'old' clients regarding household expenditure constraints. One difference was obvious and concerns the housing situation. 'New' clients seem to have more problems paying for water, house rent, and basic needs. 'New' clients also wanted to buy a house, compared to 'old' clients who already owned a house and wanted to improve it.

Both groups had problems with healthcare costs and funeral expenses. School fees were, in most cases, hard to pay in the beginning of the year and some women never manage to pay. In some cases the children no longer attended school. Also other school expenditures, such as school uniforms and transport fees, composed a large amount of the household expenditures.

The daily profit from the business goes first to household expenditures and then to cover business related costs, such as stock. According to financial services the engagement in different credit companies, as well as furniture and linen-draper's companies often leads to debts and economic stress due to repayment of instalments. In one way or another all the clients expressed a problem with repayment of their credit from FINCA.

Table 6.2 shows expenditure constraint with regards to enterprise development. Both 'new' and 'old' clients wished to improve their business with regard to higher skill/capital intense activities. There was a common picture of what kind of business that is better off. The low skill/capital group wanted to start with more advanced stock or buys a sewing machine to start make their own design. To own a tuck shop was highly ranked. The fashion designers and the tuck shop owners also wanted to improve their businesses either by investing in a better sewing machine or sell more advanced food and rebuild the shops. One difference between 'new' and 'old' clients is that 'old' clients seem more optimistic to invest in new stock and technology. They also had more knowledge in how to improve their business and how to finance the investments.

Table 6.2. Expenditure constraints

	New clients	Old clients
Household	• Water • Basic needs • Build a house • Improve the house • Furniture • Healthcare and burial costs	• Electricity • Basic needs • Improve the house • Transport fees • Healthcare and burial costs
Education	• School fees • Save money for future education of children • Course fees for own education (computer)	• School fees • Save money for future education of children • School transport cost
Finance	• Instalment to FINCA • Payment to stokvel • Instalment to furniture and fridge company • To pay policies and insurance schemes	• Instalment to FINCA • Payment to stokvel • Instalment to furniture and fridge company • Instalment for house loan in formal bank • To pay policies and insurance schemes
Enterprise: **Fruit / vegetables**	• Improve the business • Open a tuck shop • Sell bedding • Buy a sewing machine	
Various commodities	• Buy more stock • Improve the business • Start with second hand clothes • Training in business development	• Buy more stock • Improve the business • Buy a larger variety of stock • Permit cost
Second hand clothes		• Improve the business • Start another business • Buy a sewing machine • Permit cost
Fashion design	• Improve business • By a tuck shop	• Improve business • Buy stock • Buy a better sewing machine • Salary to workers • Start a sewing school • Start to sew and sell cloths to schools and companies
Tuck shop	• Improve business • Buy a sewing machine • Make a kitchen for cooking	• Improve business • Buy stock • Rent to storage space for stock • Build a bigger shop • Turn in the shop to a take away food business • Salary to workers

6.2 Findings Regarding Savings

The findings regarding saving are divided into four paragraphs; in 6.2.1 the different saving channels used by the street traders are described, paragraph 6.2.2 outlines the motives of savings, and in the last paragraph, 6.2.3, optimal saving channels are discussed. FINCA's deposit scheme will be dealt with in a separate section and are therefore not taken into account here. Formal bank accounts discussed in this section include all other accounts than FINCA.

Box 6.1. Quotes from the street traders relating to savings

"You need a lots of guts and motivation to save and you also need to be empowered"

"It is hard to save. I have little money in my purse and too many needs"

"As a human being you must always have money at the bank, because you can't live without money"

"You must always have money to help you afford the things you can't afford at the moment"

"My dream is a bank for people like me, where we can save money and take loans: A peoples bank"

"You must save something at the bank, it is like a law"

"If I don't save I lose. I tell my self I have to save"

6.2.1 Saving Channels

The different saving channels used among women street traders were divided into formal and informal ways of saving cash. In the formal group, policies/insurance schemes, bank accounts, and stokvels connected to a formal bank are included. In the informal group cash saving, money collectors, and shorter stokvels are represented.

'Old' clients had, in general, a more diverse saving behaviour than 'new' clients. 'Old' clients also had a higher percentage of using formal savings, such as yearly stokvels, policy, and insurance schemes, and bank accounts. The most common way of saving for both groups was in cash at home. Six 'new' and seven 'old' clients mentioned separately that cash saving was the most common way of saving and it is most likely that all clients save a fair amount of money in cash. Businesses that belonged to the high skill/capital intensive group did also have more formal saving channels.

6.2.2 Motives of Saving

As table 6.3 suggests, there were not big differences in saving motives among 'new' and 'old' clients. The main motives relate to future expenditures in the form of pensions, funeral, and for 'times of sorrow'. Costs concerning education were also a motive for saving. A majority of the women thought of education as a way out of low-income activities and wanted their children to get a better opportunity to get high skilled work. The motives of savings were more related to the household than to the enterprise, although some of the clients saved to be able to develop their business. Savings for stock were often managed through cash saving day-by-day. Most of the clients found it easy to save money, but some had meet problems when they wanted to open a bank account. Either they tried and been neglected or they cannot afford to pay for a bank account. They also found that they have little knowledge and education of how savings and banks work. The problem of saving was also related to motivation. If the traders had something left over after the day, there was always something that needed to be paid for. It was therefore hard to motivate to save money for future expenditure when you need to use the money today.

Table 6.3. Motives of saving

	'New' clients	'Old' clients
Household	• Expenditures for running the house • To be able to buy a house • To support relatives and family in rural areas • Single parent and no one else to support her	• Expenditures for running the house • To be able to buy a house • To buy a car • Single parent and no one else to support her
Education	• School fees • School uniforms • School fees for higher education	• School fees • School uniforms • School transport fees • School fees for higher education
Crisis and emergency and Life cycle events	• Times of sorrow • Funerals • Pension • Functions	• Health care • Funerals • Future needs • Pension • December holiday
Financial	•	• For repayment of FINCA loans • To be able to use your own savings instead of borrow money
Enterprise	• For times of bad business • If you lose your job/ out of business • To be able to buy stock	• For times of bad business • To be able to buy stock

6.2.3 Optimal Saving Solutions

All clients mentioned formal bank accounts as the best way of saving money. Also, insurance schemes were ranked high. The main reason was that they had a high trust in banks and insurance companies. It was seen as a safe place to keep money to avoid crime and unnecessary use. Interest rates were an important factor, but not a necessary factor for choice of bank. Another reason for preferring banks to stokvels was that you are treated as an individual instead of a group. If you save money at the bank you may also be able to use their other services, such as credit and funeral schemes.

Insurance and policies are seen as an investment for the future and a good long term saving solution.

6.3 The Role and Impact of FINCA

This section will conclude the findings regarding the credit and the deposit schemes provided by FINCA. The findings are mostly drawn upon responses from the group with 'old' clients since the 'new' clients had not started to use the facilities. The 'new' clients were, though, asked about motives of taking a loan and how they found the training. In paragraph 6.4.1, the administration is discussed with regards to methodology, communication and information. Paragraph 6.4.2 outlines the findings from the use and impact of the deposit schemes. Table 6.5, which is presented in the end of this chapter outlines the main objections found regarding the methodology, communication, information, and the credit/saving schemes. The table also include a column with solutions to the outlined objections that the clients mentioned.

6.3.1 Administration, Methodology, Communication and Information

The group size is between 8 and 15 individuals and the lending cycle is often eight weeks long. The interest rate is 8% for loans up to R2000 and then 7% for loans up to R12000. The max level of loan amount is R12000. They repay the loans every week and the repayment includes the interest rate plus the loan amount divided on 8 weeks.

FINCA uses an empowerment methodology and the group members chose one member to be the head of the group. This person is then responsible to fill out all the forms and collect the repayments and to deposit the amount in a formal bank account at ABSA that FINCA is cooperating with. The credit officers are facilitators and help out if a problem arises.

The cooperation between FINCA and ABSA has three purposes. Firstly, to make the transaction process easier and quicker for both the clients and for FINCA. Secondly to reduce the risk of dealing with cash both for FINCA and for the clients. And lastly to get the clients used to a formal bank system. The ABSA cooperation does not give the clients better access to their personal deposit and they still have to apply a week before to withdraw money.

Before starting a credit group there are four weeks training where the clients comes once a week and simulate a meeting and get information about the schemes and FINCA. Then the group continue attending the meetings and get access to small loans. First two people get loans and then two more and so on until FINCA recognise the group as reliable clients. The loan is individual but the whole group is responsible for the common performance of the group.

The pass-book is the book where the clients note all the transactions with FINCA. It is divided into cycles; one cycle is one credit round. The pass-book is a security for the clients and a way to compare their transactions with the credit officers' notes and, in so doing, give the clients power and control over their finances.

As a security for repayment rates, beyond the 'social collateral' through the group-lending, FINCA has compulsory deposit schemes attached to the credits. All members of a group have to deposit a certain percentage of the loan amount and when a credit cycle is finished you are supposed to get the deposit back, assuming the group as a whole has good performance records. If the records are unsatisfactory, FINCA may use the deposit as a security fund. The clients also sign a partnership agreement, a pledge of assets, a solidarity agreement, and make up by-laws within the group when starting. If some clients fail, FINCA may also confiscate the assets noted in the pledge of assets.

The objections regarding the credit schemes concerned the weekly repayment agreement and the use of the credit. The majority of the client's think weekly instalments are too frequent and would prefer two weeks or monthly repayment. One reason for why the clients think they fail to repay their instalments is that the credits are not used for business purposes and thereby, may not lead to increased income return.

Clients would prefer FINCA to be stricter with outlining the purpose of the credits. The 'new' clients seemed more clear with the purpose of their loans and mentioned business development and benefits, such as the funeral scheme, as motivations for starting with credits. Regarding the training, the 'new' clients were in general more positive about the information, but would like to have more training in empowerment and be able to share ideas around business management.

There seems to be a lack of understanding, among the clients of the methodology and the compulsory deposit schemes. The information provided by the credit officers, about the credit and deposit schemes, seemed to be misleading in some cases. The clients thought that FINCA would contact the member who had not repaid the loan and confiscates their stock before using the other members' money to cover the loss of payment. The clients also found it hard to get clear answers about why they were not receiving money from their personal deposit schemes and found the deposit schemes confusing.

Box 6.3. Quotes from two clients according to the relation with FINCA

"It feels like we are working for FINCA. We have to bring them money every week. Sometimes the profit is the same as the instalment, then we need to borrow money to live off."

"I made a decision that this is my last loan, I have discovered that in the end of the day I'm the one working for FINCA."

6.3.2 The Deposit Schemes

FINCA has two compulsory deposit schemes connected to the credit, one group fund (GF) and one personal investment fund (PIF). To access money from PIF, the clients have to apply one week ahead. The clients also have to give a reason for why they want to withdraw the money.

One of the 'old' clients used the deposit scheme more than what is compulsory. The rest only deposit 2% as required. Some clients also mentioned that sometimes they do not even deposit the compulsory amount. The motives of using the deposit scheme were; because it is compulsory, to be able to access more loans, to show that you are a responsible client, and to be able to get access to a government house.

The main reasons for not using the deposit scheme more than necessary were related to trust, accessibility, and lack of knowledge. Since nearly all clients have experiences in losing money through their deposit schemes due to the failure of a group member, they know their money is not secure at FINCA. Since the information about where the money went is lacking, they have low trust in the deposit scheme. Another reason is the accessibility to the money. The clients did not know why it takes a week to withdraw money, but they thought it was due to administration. They have asked the credit officer, but were given no answer.

The clients' view of why FINCA has a compulsory deposit scheme linked to the credit is quite the same as the motives of deposit; solve FINCA's problem with repayment security, a measure of how responsible the clients are, as an educational tool to show that savings form a part of a business plan.

One client pointed out the contradiction that FINCA teaches them how and why to save, but then they cannot save because of trust and accessibility. The clients would deposit more if the money were safe and accessible. The interest rate does not seem to be an important incentive to savings.

Table 6.5. The main objections

Main objections regarding:	Comments:	Solution:
The administration • Methodology • Communication • Information • The meetings	• Too much responsibility on the group members • The clients feels like they working for FINCA • Hard to get answers from the credit officers about why they not receiving money they applied to withdraw from PIF. • Miss-information about what happens if someone fails to pay back. • High cost for transport fees • Time consuming	• FINCA could work together with the communities, so if members fail to pay FINCA could easy find them instead of taking from the group. • If FINCA could make the clients follow the methodology the clients would not need to suffer that much.
The credit scheme • Repayment • Purpose	• Too frequent repayment • The credit is used for other purposes than productive activities.	• Two weeks repayment • Monthly repayments • FINCA could be more strict with the purpose of the credits
The deposit schemes • Access • Personal • Trust and security	• Hard to receive money • The money is not personal. And if some group member fail to pay, FINCA may use the money • The clients cannot trust FINCA to secure their deposits.	• Make it more accessible • Introduce purely personal deposit schemes • Introduce voluntary deposit schemes

6.4 Summary of the Findings

- The source of income can be divided into two main groups regarding how skill/capital intensive the businesses are. 'Old' clients are more likely to be engaged in a high skill/capital business than 'new' clients.
- The average weekly income level is higher according to level of skill/capital involved in the business.
- Differences among 'old' and 'new' clients regarding income risks were that 'old' clients were more sensitive to the state of the economy than 'new clients. Other risks that affected both the groups were unbeneficial stock, weather conditions, seasonal trends, business agreements, crime, and trade permits.

- According to expenditure constraint, a main difference is that 'old' clients seemed to own houses, but 'new' clients still lived in informal settlements. Both groups had problems with health and school fee costs. They also felt that they never had enough to buy stock and to develop their businesses. Engagement in different credit companies, including FINCA, seems to be a constant pressure on the consumption. One difference between the two groups is that 'old' clients seem more optimistic to invest in stock and new technology and they seem to have more knowledge in how to improve their business and how to finance investments.
- Saving channels used were policies/insurance schemes, bank accounts, money collectors, stokvels, and cash savings.
- 'Old' clients have, in general, a more diverse saving behaviour than 'new' clients. They also use more formal institutions. The most common way of saving for both groups is, however, cash at home.
- The motives of saving seemed to be rather same between the two groups. The main motivation for savings is to improve the household rather then to develop the business. Most of the clients find it easy to save money, but they had poor options where to save the money. The clients found that they have little knowledge and education of how savings and banks work.
- Nearly all the clients would prefer to use formal bank accounts for savings. They had a high trust in banks and insurance companies. Another important reason for why banks are preferred to group-lending is that you are treated as an individual instead of a group member.
- There seemed to be a lack of understanding among the clients of the group-lending methodology and the compulsory deposit schemes. A reason for this might be due to poor information from the credit officers.
- The majority of the client's thought weekly instalments were too frequent and would prefer bi-weekly or monthly repayment.
- The client's would prefer FINCA to be stricter with the purpose of the loan. The credit was more often used for household consumption than for business development.
- Only one client used the deposit scheme to save more money than is compulsory. Some clients even mentioned that they deposit less money into

the deposit scheme than is compulsory. The motives to deposit money were thereby because it is compulsory, but also to show that they are good client's and can access more loan.

- The main reasons for not using the deposit scheme are related to trust, accessibility, and lack of knowledge.

7 DISCUSSION AND CONCLUSION

The discussion and conclusion chapter attempts to link the literature review and the theoretical framework with the findings. The chapter is divided into four main headings. The first section, 7.1, 'The livelihood among women street traders', will mainly link to Chapter two and discuss risks, assets, and savings as a risk management strategy. The second main heading, 7.2, 'The role and impact of FINCA', will relate to the theoretical framework and be divided into three sections including; administration, methodology, communication and information, the impact on income, assets and business development, and the use of the deposit schemes. The third main heading, 7.3, will include a paragraph related to chapter four about challenges for South Africa according development of the informal sector and provision of financial services. The last section, 7.4, outlines the main conclusion for the dissertation.

7.1 The Livelihood among Women Street Traders

This section will link the findings to chapter two, risk, poverty, and financial services. In section 7.1.1 the nature of risks facing the street traders will be outlined. 7.1.2 will describe the importance of assets and paragraph 7.1.3 will discuss savings as a risk management strategy.

7.1.1 The Nature of Risks

The nature of risk described in chapter two, as will be discussed in this section, is structural factors regarding to macro- and micro- economic impacts, and risk related to health and the crime environment the street traders face

Wright (1999a) points out that structural risk on a macro level may have long-term effects on the economy. The high level of unemployment in South Africa has effects on the street traders, since the traders are dependent on customers, which in their turn are dependent upon wage income. The street traders that are involved in high skill/capital activities point out that customers seem to have lower purchasing power due to the high unemployment rate. Traders in the low skill/capital rank did not feel the same problem. Reasons for this may be that the basic needs the low skill/capital group sells will always be consumed, even in bad times, but on the other hand more, luxurious goods provided by the high skill/capital sector are an optional exclusion.

High skill/capital enterprises are also more sensitive to seasonal swing, especially fashion designers, which have a higher income October to December. Another macro-economic factor that Cohen and Sebstad (2000) discuss is education expenditures and its effect on the household economy. School fees and other expenditures regarding education of children were one of the scarcest consumption needs among all women. In some cases, the women had to take the children out of school due to unpaid fees.

On a micro level, structural risk is related to the market, law and regulation, such as is described in Cohen and Sebstad (2000). This also applies for this study and the traders mentioned risks related to the market, such as, unfavourable business agreements and problems with an unregulated market. The traders use oral payment agreements with their customers and the only security for repayment is trust. The implication of this for the traders is loss of income due to a disadvantage bargaining position.

Another structural risk on a micro level relates to the problems of the unregulated market, which leads to free competition. This may affect the market prices to the benefit of customers, but at a high cost for the trader. When income is unstable due to uncertain market prices, the trader cannot calculate the income level and make strategic plans for future investments. The number of traders in the informal sector has also increased in the latest decade. The women selling second hand clothes have a particular problem with the high number of traders at the market, since during the last years there has been an increased trend in trading second hand clothes.

The lack of social and economic infrastructure provided by the local government is a structural risk that has a great impact on women street traders. They have no access to childcare and need to bring their young children to work, which may have limited effects of business development. Also, the lack of infrastructure provision in form of waste disposal, water provision and facilities makes it hard to run their businesses.

One issue regarding the trading place that Cohen and Sebstad (2000) bring up in their paper is the risk of getting the stock confiscated due to lack of trading permit. This was also the case in the study and the traders mentioned that it was hard to get hold of a permit due to high cost and regulation. As a result some of the traders traded illegally and always had to look out for the police and hide their commodities.

Weather factors have a great impact on urban street traders, as Dunn, Kalaitzandonakes, and Valdivia (1996) point out. The weather conditions did affect the street traders in two ways, either with regards to the number of customers out shopping, or with regards to the quality of the stock. A sunny day will lead to a higher income due to a higher number of customers around, but on the other hand, a sunny day will damage the stock for the fruit and vegetables traders. Rain, too, may have a devastating affect, especially for second hand clothes trading. The obvious solution to the problem of weather, namely finding some sort of cover, is often times expensive, as well as voluminous, and leading to difficulty in storage and maintenance.

Dunn, Kalaitzandonakes, and Valdivia (1996) conclude that health implications have an effect on both income and consumption. The study shows that health issues might result in income loss. There is often no one to take care of the business and no income compensation schemes offered by insurance companies or the state. Crime is another factor that has a large impact on women street traders. The most common crime is having the cash balance or the stock stolen. Since there are no safe storage spaces, as mentioned above, the traders have to bring the stock home, which increases the risk of being mugged in their homes. The traders have organised themselves against crime in order to reduce the risk of getting the daily cash balance stolen, but crime remains prevalent.

7.1.2 The Importance of Assets

Moser's (1998) 'asset vulnerability framework' underlined the importance of assets with regards to urban households in a development country. This case study of the women street traders underlines Moser's conclusions of the importance of assets.

Moser argues that labour mobilisation is the first action when the household income decreases. It often takes the form of increased women and children labour. In the average household structure among women street traders in the study, the women are already the head of the household and there is no one else in the household who is able to work and thereby leaving little room for labour mobilisation. Two long-term trends in household structure in less developed countries are an increase in households headed by women and households organised around extended families. This trend is applicable among women street traders; with the average household composition being a single woman economically responsible for her own children, other relatives, and a couple of related children that lost their parents due to HIV/AIDS.

The importance of housing as an asset described in Moser (1998) clearly underlines the findings from the study. The most important finding with regard to housing was that the 'old' clients own houses in a higher range than the 'new' clients, who tend to rent accommodation or live in informal settlements. Houses are used in a productive sense, as sewing studios and home-based shops. The most common expenditure constraint regarding consumption mentioned in the interviews involved housing both for 'new' and 'old' clients. 'New' clients wanted to be able to buy or build a house while 'old' clients wanted to improve their already existing house by installing toilets and adding furniture.

7.1.3 Savings as a Risk Management Strategy

As described in chapter two, the literature offers a wide rage of studies about strategies to protect against risk in a less developed country. Financial services are one strategy to both be able to protect against future income risk through savings or to cope with already existing risks through borrowing. Also, insurance schemes are an important financial service that is a direct action against future risks. Bouman (1995), Rutherford (1998; 1999) and Wright (1999a; 1999b) describes different saving channels used in less developed countries; cash saving, joining a rotating saving and credit club, money collectors, microfinance institutions, and formal banks. These saving channels were also the ones used by the street traders in the study. 'Old' clients used more 'formal' saving channels than the 'new' clients. This may be a result of 'old' clients having been engaged in financial institutions longer and also having more advanced businesses with a concurring higher income level.

Regarding the conflict between the use and impact of formal or informal institutions in the poverty reduction debate, Dercon (2000) argues that by introducing formal institutions, important informal institutions may break, which will lead to even more vulnerability. Ruthven's (2002) study too, shows the importance of informal financial institutions. Morduch (1995), on the other hand, argues that the cost of an imperfect market may spill widely. One reason for the different approaches may be that the studies of risk and vulnerability often are done in rural environments. Since informal financial institutions often build on social capital and community relations, the urban environment where the street traders live and work might have less important informal financial institutions. The stokvels are however, an important institution in both rural and urban settings, but the findings from the case study seemed to indicate a demand for formal institutions. Regardless, the commercial banking system is failing the women street traders. Some of the women mentioned that they attempted to open a bank account only to be turned away due to lack of formal income.

When discussing savings, the use of stokvels with a daily, weekly, monthly, or yearly span seem to be very important for the street traders. As Besley, Coate, and Loury (1993) suggest, a rotating saving and credit club could lead to a welfare gain among its members, especially if the good is nondurable, such as a sewing machine or a kitchen tools. The stokvels described in the findings are a common way of saving and often have a certain purpose. The weekly stokvels were designed mostly to cover basic needs while the yearly stokvels have a wider array of purposes including school fees or household equipment.

Recently in some countries there has developed a relation between rotating credit and saving clubs and formal banks, where the banks make accounts available to groups savers often linked to a purpose, for example school fees savings (Bouman, 1995). This is also true in a South African context and nearly all of the clients were engaged in stokvels connected to a bank.

A comparison between tables 6.1, 6.2, and 6.3, in the findings, showing the risks related to income/consumption and the motivations for savings may implicate if savings is used as a risk management tool among the street traders. Table 7.1 present an overview of main linkages with respect to household, finance, and enterprise. The table will not show any differences between 'new' and 'old' clients but will give a general view of the link between risks and the use of financial service with respect to savings.

Table 7.1 Links between risk and savings

	Income risks	Expenditure constraints	Motives of saving
Household		• Household expenditures • To buy or improve a house • School expenditures • Health care • Funeral	• Household expenditures • Buy or improve a house • To support family • School expenditures • Health care • Funeral • Pension
Finance		• Instalments • Stokvel payment	• For instalments
Enterprise	• Market conditions • Damage on stock • Agreement costs • Crime	• Improve business • Buy stock • Permit costs	• For times of bad business • To have if you lose your business • To be able to buy stock

Most of the risks regarding income and expenditure constraints are mentioned in the motives of savings, which may implicate that savings are recognised as a risk management strategy among the street traders. Still savings are not used as efficient as it could and the problem with savings comes down to the lack of income and access to good saving opportunities. The main saving strategy among the street traders are still cash saving at home and due to the risk of crime and the easy access the money get used.

Formal bank accounts are viewed as the best option to save money, but it is still expensive and complicated to open a bank account. The knowledge about formal banking also seems to be lacking. The motives of savings are more linked to household expenditure than to use for business development. Reason for this may be that caring for your household is prior to investments in your business.

7.2 The Role and Impact of FINCA

The risk situation explained in the study is much more complex then to be solved with a simple financial institution solution, but there are elements in the risk picture described that could be related to the lack of access to 'good' financial services. If the street traders would be able to save money, take credits and use insurance schemes their ability to handle income shocks might be smoother. This section will link the findings to the theory outlined in chapter three. 7.2.1 describes the administration, methodology, communication and information, 7.2.2 relates to the impact on income, assets and business development, and the last paragraph 7.2.4 will discuss the use and impact of the deposit schemes.

7.2.1 Administration, Methodology, Communication and Information

According to Morduch (1999) there are different ways of alternative methods financial institutions can use to secure repayment rates, such as group-lending, frequent payment schemes and compulsory saving schemes. FINCA has adapted some of these methods discussed in the theory. The main method discussed in this section is the pros and cons of group-lending.

Ghatak (1999) shows in his example how also the 'safe' borrowers are included when using group-lending due to adverse selection and reduced problems with moral hazard. According to FINCAs group-lending schemes it gives clients that are poor but 'safe' an opportunity to take credit. In the commercial banking sector this same clients would have been excluded. The basic understanding of the group-lending methodology is that group members have more information about each other than the bank does and by self-selection sort the 'risky' borrowers out from the 'safe' ones through positive assortative matching (Ray, 1998).

There is also a risk with group-lending and Hulme and Mosely (1996) argue that repayment failure in a credit group may lead to social exclusion and conflicts. This depends on which basis the group is formed, if they are friends from before or new to each other, or how well the group understands the methodology and the purpose behind group-lending. Bouman (1995) describes how homogeneity reduces the information problem further due to solidarity level. The study showed that groups that are more homogeneous and for example trade on the same street or are old friends perform better as a credit group.

The successful groups interviewed were all old friends and had their businesses close to each other. Strong moral obligations meant that they were more likely to help each other with repayments. One group that was newly started had big problems with group members running away from their repayments and now the rest of the group had to pay for the failure. The failure of the groups was often related to lack of understanding of the methodology of group-lending and frequent payment.

One of the reasons for the lack of understanding of the group-methodology is due to misinformation from the credit officers. Reasons for misunderstandings between clients and the credit officers may result from pressure by the credit officers. The credit officers have a large responsibility to form groups, give them training and later be responsible for the credit group. The decentralised responsibility method that FINCA uses regarding the responsibility of the credit officers may be both beneficial and costly. The benefits are that the credit officers may take more responsibility for the success of the groups. The cost is due to large pressure on the credit officers, which may lead to misinformation and lack of communication with the groups. The credit officers at FINCA worked on a wage system that was built upon how many groups they formed, and perhaps more importantly for the discussion, how well the groups performed. Maybe just the latter would be to prefer since the amount of groups is unimportant if they all fail.

The advantage with a frequent repayment scheme for microfinance organisations is that it screens out undisciplined borrowers, which give an early warning to credit officers and the other group members (Hulme and Mosely, 1996). The objections, from the clients, regarding the frequent repayment scheme that FINCA used is also a evidence for the lack of understanding of the group-lending methodology. The clients did not understand why they had to pay back every week and they would rather prefer two weeks or monthly repayment schemes. The clients suggested themselves that FINCA should provide more training, maybe that is a solution of how to increase the knowledge of how the methodology of group-lending work, or maybe the four week training have to be more accessible.

7.2.2 Impact on Income, Assets and Business Development

In Morduch's (1995) example regarding the cost of an imperfect market, he explains how the lack of adequate financial services affects the income and assets among low-income households. Both examples are implacable on women street traders and it is clear that their income and asset level are hold back due to lack of possible income smoothing options. In comparison between the two groups of 'old' and 'new' clients the 'old' clients have a higher income- and asset level than the 'new' clients. This finding may be due to the fact that the 'old' clients have been using financial services through FINCA for a longer time.

Hulme and Mosely (1996) point out a risk with credits and business development that are relevant for the findings. Credit requires regular repayments, which means that the loan needs to give a positive return on the investment. The clients did not specifically use the loan for productive activities such as business development and therefore they did not obtain any positive return of the credit. There is thus a difference between 'new' and 'old' clients regarding the purpose of the credit. The 'new' clients seem to be more focused of using the money for business development compared to the 'old' clients. Reasons behind this finding may be that 'new' clients are more eager to get the loan they applied for and learned in the introduction meeting that the credit are suppose to be used for business development.

Another related issue is due to repayment and especially the frequent repayment scheme. The clients mentioned that the productive investment does not give returns in one week and often the credit is needed to cover for income loss and for basic needs. The findings showed that clients with already existing enterprises have a higher chance to benefit from taking a loan with FINCA. Two clients had used their first loan to start up a business and they had a hard time paying back since it takes a long time to get positive return on a new business. The findings also showed that the clients did not invest their credits optimally. Their investments tended to stay on the safe side and therefore did not reach optimal income.

Lack of skill and knowledge related to business management are a risk that affects the income among low-income individuals in less developed countries (Cohen and Sebstad, 2000). The study showed that a majority of the street traders often felt that they were lacking in knowledge and skills regarding business development.

7.2.3 The Use and Impact of the Deposit Schemes

As the literature review suggests, saving is an important way of protecting against risks among low-income people, which were discussed above. FINCA has two compulsory deposit schemes that are linked to the level of credit. The purpose of the deposit schemes is mainly to secure repayment rates and the clients do not use the compulsory deposit scheme to save more money then needed.

Both compulsory and voluntary saving schemes may create a win-win situation for the lender and the borrower, but Barnes (1996) argues that if deposit schemes provided by microfinance organisation are going to be beneficial for the clients they must be voluntary in nature. Since the clients lack trust with regard to FINCA's management of the deposits, they do not feel encouraged to deposit more then needed. The accessibility to the money remains a problem for the clients. One argument mentioned by the FINCA management regarding the accessibility of the deposits was protecting the women's savings from family members and friends. The women could, in this case, use the inaccessibility of the money as an excuse to not lend or give money to family members or friends and instead keep them for own use. The clients interviewed did not found pressure of family and friends to be a problem. At least the problem of accessing the deposit exceeds the benefits and thereby the clients may not need to be 'protected' by FINCA.

The common thought among the clients was that formal banks provide the best channel of saving, because the money is in a safe place and they can access their money when they want. For FINCA, voluntary saving schemes could probably attract more clients to deposit money in the schemes. Another important step for the future of microfinance institutions will be figuring out ways to link saving schemes to school fees, funeral, health insurance, and development of businesses. And how to make a saving plan based on income fluctuations. For example, save more in December when income is high to secure the increased expenditures in January or save every weekend or the last week in the month when people have more money.

7.3 Challenges for South Africa

As Skinner (2000), Valodia (2001) and Lund (1998) point out, South Africa faces major challenges in formal job creation, but also, which is increasingly important, to promote opportunities and protect the informal economy. Not only the government needs to recognise the informal sector, but also the commercial banks and insurance companies as well. It is hoped that they may gain in the long run if they are able to introduce low-income earners into their services.

Street traders need to be included in the national and local policy and legislation as much as any other business. Street traders face the same challenges as other entrepreneurs, such as business skills, literacy, and access to financial services. Durban is the city in South Africa that has allocated most financial support to the street traders. It is still, though, hard for the street traders to make their voice heard and the infrastructure is far from satisfying the major sanitary and accommodation problem. Even if SEWU has negotiated with the formal banks to lower their costs and make their services more accessible, it is still not feasible for the majority of the street traders in Durban to get access to personal saving accounts.

7.4 Conclusion

As the case study of women street trades in Durban, South Africa, shows, the risk environment is rather complex. Institutions such as ones that insure social protection, law, and financial services are lacking and thereby put the street traders in a very vulnerable position.

Financial services may lead to reduced vulnerability by increased income, changing the composition of individual and household assets, and increasing women's human and social assets. Savings have been argued for in this dissertation as one of the most important financial services. According to Rutherford's (1999) three facts and one conclusion, as was outlined in Box 2.1, he argues that financial services are largely a matter of mechanisms that allow the poor to convert a series of savings into usefully large lump sums. Women street traders are lacking in 'good' options of financial services and particularly saving opportunities. FINCA is one option but as long as they not offering voluntary, secure and accessible deposit options the clients will not start to deposit more money then required.

As the findings showed there is a clear link between business development, income return, and how long the clients have had access to financial services. Financial service may in the case of street traders be an important way to break out of the low income trap.

It seems that street traders have been recognised as an important sector in the economy, but there is still a lack of policies targeting women street traders directly. The government need to respond to their main goal of poverty reduction with well-designed policies targeting the vulnerable in the economy. The government also need to put more pressure on the commercial banking sector to use alternative methods so even the poor could be recognised as their clients. Also the microfinance sector must get supported in the attempt to develop 'good' financial services in order to reduce poverty.

Better mechanisms through financial services to cope with risk may not only lead to greater efficiency in production, it may also play a role in improving education and health conditions.

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