The Role of Co-operatives in Economic Growth and Poverty Reduction in South Africa

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Just as governments need economic growth policies and models, communities at grassroots level also need them to improve the livelihoods of their members. In this article, I present a business model that I have developed with Mrs Wezi Ximiya to address the economic development of poor people in rural communities through cooperative structures.

Interventions to establish cooperative village banks in South Africa in the early 1990s lie at the heart of this economic development model. However, these co-operative institutions met with mixed success, and during 2002 we developed a new strategy and operating model to address the form, function and implementation process for these pro-poor financial co-operative institutions.

1. Introduction

The South African economy has to deal with the incongruity of two separate economies. The 'first economy' or formal economy deals mainly with large businesses fostered and maintained during the apartheid era. Due to the segregation and exclusion policies of the previous government, an informal or 'second economy' formed around the economic activities of the mainly non-white South African population.

In the hands of Minister Alec Erwin, the Department of Trade and Industry has had much success in managing the first economy in the past ten years. As a result, South Africa enjoys sustainable growth and economic stability of a kind not seen in many decades. This success has led the government to refocus and bring the 'second economy' into the mainstream economy of South Africa. The President appointed a new minister for trade and industry, Mr Mandisi Mpahlwa, to ensure that the department addressed the second economy, helped it to grow, and thus reduced the poverty experienced by many poor South Africans (Department of Trade and Industry, 2006). Its strategic framework defined a number of key objectives to address the imbalances of the past: integration of the two economies through increasing the contribution of small enterprises, emphasising co-operative structures, facilitating broad-based black economic empowerment, and supporting women's enterprises (Department of Trade and Industry, 2006).

The purpose of this article is to discuss a co-operative economic development model that I developed with Mrs Wezi Ximiya to support government initiatives aimed at reducing poverty and stimulating economic growth in poor rural areas. Mrs Ximiya was one of the first implementers of the village banking co-operative model in South Africa in the early 1990s, and put great effort into the establishment of a self-regulator for 40 banks with an average customer base of 50,000 clients over two years. For various reasons the success of these co-operative financial institutions was mixed, and a lack of funding resulted in the collapse of the self-regulator in 2002.

Following this, we developed a new strategy and operating model to address the short-comings of the strategy, form, function and implementation of the existing village bank models. We deliberately chose not to implement existing best practice models such as ASA (ASA, 2006) or the Grameen Bank (Grameen Bank, 2006), but rather to develop a strategy and operating model that specifically suited South African communities. Our previous experience with international models, as well as the lack of local micro-finance success stories, supported our strategic decision to follow a bottom-up approach based on developmental micro-finance and social development experiences.

In Part 2 of this article we give an overview of two important government interventions that drive the implementation of this model in poor communities. In Part 3 we offer a quick overview of the history of South African co-operatives and early government interventions to uplift poor white South Africans after the Anglo-Boer War in the early 1900s. Against this background, in Part 4 we discuss the essential components of the economic development model, including the purpose, key objectives, and operating model.

As we shall show, the success of our economic development model depends on capacity-building interventions. So in Part 5 we explain the various components of capacity-building in the co-operative, and how it should be approached to ensure a successful co-operative intervention. To measure is to know

- so in Part 6 we present the key measurements, giving insight into the success or failure of the intervention.

Practical lessons learned during implementations are crucial to understanding the model. In Part 7 we cover the lessons learned from various initiatives in rural, peri-urban and urban communities. In Part 8 we end by discussing the cornerstone of our model: the aim of alleviating poverty and stimulating economic growth in poor communities.

2. Poverty Reduction Interventions

What does ‘poor’ mean? The World Bank says that it is the “inability to attain a minimal standard of living”, quantified as living on 1 USD or less per day. This means that if a community, household, or individual is unable to access sufficient resources to satisfy its basic needs, it is poor (Landman, 2003).

The United Nations report on human development (United Nations, 2005) argues that the definition of poverty should go beyond pure economics to include vulnerability and social, cultural and political deprivation. These factors are important — but their inclusion in the definition makes poverty much more complex and multi-faceted than just the inability to “attain a minimal standard of living”. In this article, I accept that **the level of income** for an individual indicates access to basic services, and thus forms **the** most important indicator of poverty levels (Landman, 2003).

From 1994, the first democratically-elected government faced unprecedented levels of unemployment and poverty, in particular amongst the historically disadvantaged black communities. It is difficult to comment on the position of poverty in the first decade of democracy, since various researchers contradict each other on what has happened. One group shows that poverty has **increased** (South African Institute for Race Relations, 2006), while another, from the University of the Stellenbosch (Steyn, 2006), argues that poverty has **decreased** through the massive introduction of social grants by the South African Government. The issue is further complicated by the argument whether a daily income of 1 USD or 2 USD should be used.

Academic arguments aside, the government has taken on the responsibility to devise and implement strategies to promote economic growth and job creation — both of which are essential for reducing unemployment and poverty. It has launched many initiatives on national and provincial levels; in this article we focus on two important national drives, as they underpin the importance of the economic development model.

These initiatives differ in their aim and focus, but they both focus on the member of the community who faces poverty on a day-to-day basis.

2.1 The South African micro-finance APEX Fund

Since several factors impact on poverty and on attempts to reduce it, the Department of Trade and Industry has implemented several programmes that are directed at economic growth and job creation to increase household incomes and reduce poverty. One of these is the development and promotion of small businesses. One strategy focuses on providing access to finance so that households and individuals not served by conventional banks can engage in productive activities that generate household income (the Department of Trade and Industry, 2006).

In continuously seeking new and improved ways of achieving economic growth, the department reviewed its own ten-year performance in supporting finance access programmes for small businesses. It concluded that existing finance support programmes have not fully met the needs of potential entrepreneurs, especially those who are currently unemployed and those who are low-income earners. It also recognised that financial services required by very small and micro enterprises (VSMEs) are very different from those required by small and medium enterprises (SMEs). So the department has earmarked the provision of financial services to VSMEs, the unemployed and low-income earners for greater attention, focus, and consideration. This is to provide the financial services needed to address second economy issues.

As a result, the Department of Trade and Industry has created the South African Micro-Finance Apex Fund (SAMAF, 2006). Its aim is to bring renewed focus and energy to this sector by wholesaling the lending of funds to partner organisations. These include the old village banks, which would be helped to convert to co-operative banks. At the time of writing, the Act had not yet been passed by Parliament (National Treasury, 2006).

2.2 Social Development Pilot Exit Strategy Programme

The National Department of Social Development aims to align itself with national economic development initiatives. In doing this, it creates social assistance programmes that shift grant recipients from being welfare cases towards having the necessary social capital for economic development (Department of Social Development, 2006).

The objective of any social assistance programme should be to create an economic movement in the life of the recipient. This economic movement needs to be linked to an economic development programme that sustains the movement, so that recipients can exit the programme and allow new participants to enter. Recipients will be linked to a group with a common bond to enable the group to graduate from the programme, so that they can continue with their lives without any dependency on future social grant schemes.

The department launched the social assistance programmes with these objectives in mind – except for one crucial link: building in an exit strategy that moves the individual from receiving grants to being economically sustainable. Without this strategy, self-reliance and economic development in the community cannot be achieved.

In 2003 almost six million South Africans were receiving grants. That number reached almost ten million in 2006 (Department of Social Development, 2006). This is obviously a cause of concern among stakeholders in government and in the private sector – especially for the Minister of Finance, Trevor Manuel, and the Minister for Social Development, Mr Zola Skweyiya.

One of the solutions is to create an **effective, sustainable livelihoods programme** that will enable participants to start achievable economic activities in their communities, thus reducing their dependence on social grants and moving them into sustainable economic activity (Van Rensburg, 2006b). This strategy will enable the government to bring new people into the programme without increasing the cost of social grant delivery to the communities. The same economic model that supports the Department of Trade and Industry's initiative is used to create an exit strategy for grant recipients.

3. Historical Overview of South African Co-operatives

When the Anglo-Boer War ended in 1902, agriculture in the former Boer republics came to a complete standstill. This was due in large part to the British army's destruction of infrastructure and its practice of killing livestock to derail the Boer guerrilla forces (Department of Agriculture, 1999). Farmers could produce very little at the time; they mostly sold their produce to the nearest general dealer, who fixed the prices and at the same time supplied the farmer with groceries, clothing, and farming requisites. In the former provinces of the Transvaal, Cape Province, Free State, and Natal, government-supported interventions focused on starting co-operatives to ensure the economic reconstruction of the country.

The South African co-operative movement was slow to develop in the first few decades, but eventually it led to the establishment of successful agricultural and financial services industries. The biggest corporations in South Africa today have their origins in co-operative movements. Although converted to public entities in recent years, SANLAM (www.sanlam.co.za, 2006), Old Mutual (www.oldmutual.co.za, 2006) and ABSA (www.absa.co.za, 2006) started as co-operatives to empower and uplift the Afrikaner people after the Anglo-Boer war. Their primary co-operative focus was on financial services, delivering insurance and banking services to their members (Department of Agriculture, 1999).

A governmental strategy to uplift and build wealth in an economy by using co-operatives is not futile, as the previous paragraphs explain. The same strategy to invest capacity, infrastructure and capital in the second economy through co-operative interventions has already been successful; and the interventions discussed in Part 2 will, we hope, achieve the same kind of success.

In the next Part, I present the economic development model as one that supports the development and implementation of programmes intended to reduce poverty and stimulate economic growth in rural and mostly poor communities. This brings strategy, form and function to interventions such as the provision of effective financial services for VSME's and sustainable livelihood programmes.

4. Economic Model for Community Development

The economic development model I present here does what the name implies: it develops the economy of a community to the extent that poverty is reduced and economic growth is stimulated (Goldsmith, 1969). This includes the key objectives of the model, the formal structure of activities, and the implementation approach of the model.

In the general context of economic development, the aim is not to change the macro picture, but rather to change basic socio-economic actions at a community level. In developing the model, we assumed, from practical experience, that many communities in South African society are deprived of access to basic goods, services, resources, and skills that are available in the formal or first economy (Landman, 2003). Our practical implementation of the first version of the model showed this assumption to be valid, and it became the cornerstone of subsequent versions of the model. This approach also exposed the fact that first economy businesses tend to move resources from these rural communities to the first economy, thus exacerbating resource starvation in these poor communities (Goldsmith, 1969).

Recent national poverty hearings confirm that poor people's aspirations include achieving a better life, and having access to basic services, employment, and increased consumption (Landman, 2003). Adopting these common themes, our model supports the ultimate goal of poverty reduction and economic growth through a number of objectives.

4.1 Objectives of the economic development model

The first objective is to achieve greater **self-reliance** for the individual, and through this, for the community at large. The second objective is to improve local enterprise **opportunities** for both job- and wealth-creation, using various economic and business development strategies such as business process outsourcing (BPO) to link first and second economy revenue flows.

Through proper management of the economic vehicle, the third objective is for the community to attain **self-generated** sustainable economic growth, thus ensuring that they also achieve the fourth objective, **maximising** community resources. This means that community resources, whether social, capital, or land, must be included in the economic interventions to add support for growth.

Finally, the fifth objective of the model is to retain and re-circulate **resources** within the community and the region, to allow for the accumulation of assets (Khandker and Shahidur, 1998).

Viewed together, these five objectives define what the economic development model strives to achieve within its target socio-economic and demographic areas.

4.2 Structure of the economic development model

As mentioned earlier, we have developed the economic development model by using principles, processes and methods learned from practical experience to construct the model framework. Our practical experience included lessons from formal banking experiences nationally and internationally, as well as developing, implementing and running village banks in the second economy.

In subsequent implementations, we extended the model to include consumer co-operatives, buying and selling fast-moving consuming goods (FMCG) in rural and peri-urban areas. Building on this, we added full micro-finance activities to the model, resulting in a full suite of services: savings (village banks), credit (micro-credit), shares (co-operatives), and bulk buying (consumer co-operatives).

In all of these cases the model gave rise to three important concepts: **trading storehouses**, **eco-community pillars**, and **collaboration**. This accords with a study done by R Levine (Levine, 1997) that found that financial intermediaries have five basic functions: savings mobilisation, risk management, investment opportunities, corporate governance, and product and service exchange facilitation.

a. Trading storehouse

The concept of a 'storehouse' is easily understood by the South African communities in which the model is deployed. Instead of using first economy terms such as 'supply chain' to depict supply and demand streams, the term 'trading storehouse' is used.

From our experience of implementing the model, primary supply chains (trading storehouses) in a community are normally quite easy to identify from community needs. In general they emerge when a co-operative movement is mobilised in the community. In all instances of co-operative mobilisation, we identified **financial services** or **FMCG activities** as primary trading storehouses. Secondary trading storehouses, focusing on agriculture, housing, health, education, security, and transport, quickly emerged. In advanced co-operatives, members will elect to invest in these trading storehouses as businesses, taking the first steps into wealth creation – moving from consumer to investor (Khandker and Shahidur, 1998).

b. Eco-community pillars

The concept of trading storehouses rests on the four pillars of an eco-community: **economic flow optimisation**, **community needs**, **entrepreneurial support and development**, and **community communication**.

The first pillar, **economic flow optimisation**, aims to maximise economic inflows into the community and minimise economic outflows to ensure that resources remain and circulate in the community in the best possible way. Instead of draining resources from the community, resources are leveraged and used **within** the community to reduce the cost of attaining growth in the community.

The second pillar focuses on **community needs**. These are those basic needs in the community identified in the raison d'être for establishing the co-operative. We have found that aligning the co-operative to the basic needs of products and services brings a strong motivational drive to the co-operative, strengthening the bond between co-operative members.

The third pillar is about **the support and development of small business**. Social structures in the co-operative form around common bonds – in most cases, similar business activities.

In a consumer co-operative created in Mount Ayliff in the Eastern Cape as part of the Department of Social Development's exit strategy programmes, ten groups were formed around business activities such as gardening, bakery, and handcraft. This step allowed members to create a support group that was used for a number of capacity-building interventions (as discussed in Part 5). One significant observation from this experience is that members start to build confidence in their skills and abilities, and offer these to other members in the group.

Investment and development does not stop with the support of basic goods and services, but aims to facilitate initiatives that flow from **community communication**. In this fourth pillar of the eco-community concept, market demand and market supply are optimised between different communities in the first and the second economy. This is critical to sustainability, since a co-operative can benefit from the existing business climate where the South African government focuses on the fostering and favouring of small businesses.

c. Collaboration

Our model is founded on collaboration (Levine, 1997), addressing the principles of **being community driven**, **being co-operative-based**, **member interdependence**, and **freedom of choice**.

In our economic development model, all economic and social activities need to flow from those needs identified by the community during the mobilisation phase. In this phase, a co-operative structure is introduced to support ownership and effective collaboration between the members of the community – formalised by registration under the Co-operatives Act. By joining the co-operative, the member receives the benefits prescribed by the statutes and bylaws of the co-operative.

As governed by the Co-operatives Act, all members have equal voting status in co-operative matters. This gives the poor a strategic advantage: members can use their equal and collective bargaining power as a strategic asset to manage and grow the co-operative, irrespective of their financial status (Van Rensburg, 2006a).

The final principle in collaboration deals with the freedom of choice. Members in the co-operative have the choice whether or not to participate in co-operative activities to their benefit. To have the freedom of choice, it is crucial for the co-operative to act as a business in offering its members benefit. If real benefits are not realised, membership will diminish over time.

4.2 Implementation cycle

Models are only good in theory: they must be implemented and tested in practice. To understand the successful implementation of the economic development model in a community, the philosophy of the model needs to be understood.

The essential philosophy is to enable the community to aspire to their own structured economic framework that sustains a number of commercial and value-added industries, enterprises, and services in the community. Once the community achieves success with at least one trading storehouse, it attracts more members, and draws nearby communities into the same economic benefits. This eventually moves members from being consumers to being investors in the co-operative (Khandker and Shahidur, 1998).

We address a number of areas in the implementation cycle. The first, as already mentioned, is the 'basic need' of the community. Different communities have different needs. Closely following this is the infrastructure development required to support the co-operative and the basic products and services offered to the members (De Gregorio, 1996). Past and present experience shows us that it can include, but is not limited to, infrastructure such as running water, electricity, office space, equipment, and telecommunication facilities.

The next area of implementation is to facilitate business initiatives in the co-operative. We do this through training interventions as well as establishing linkages with first economy businesses. Once we have secured important revenue streams for the co-operative, education and health are the next business activities we address. Depending on these interventions, we establish capacity for growth in the co-operative and its membership. If this is successful, we introduce wealth creation by mobilising member savings, to enhance growth in co-operative assets.

The micro-finance developmental sector in South Africa has been targeted by many interventions in various forms, in an effort to mobilise assets in poor communities. Most of them have failed dismally, for various reasons – just one being the difficulty of aligning the economic development intervention with the cultural fit of the community. Two issues in 'cultural fit' need to be addressed: ownership and demographics.

Ownership, as mentioned earlier, must be established through aligning all co-operative activities to meeting community needs. The second issue in cultural fit, demographics, requires that the economic development model's intervention be appropriate to the socio-demographic profile of the co-operative. For example, if a business relationship requires the co-operative to produce and deliver certain services that are not oriented towards the specific competencies of the members, it will fail – and reduce the likelihood of the co-operative being sustainable in the long run.

5. Building Capacity for Poverty Reduction

We have learnt, through implementing and running the economic development model at grassroots level, that building the capacity of the co-operative must come before successful grassroots economic development is achieved. The reality is that poverty robs its victims of their ability to access economic opportunities in their own country, and therefore of their right to exercise full citizenship. This prevents poor people from participating fully in the formal economy. Capacity-building therefore starts where people are, and brings them to the point where they participate as full members of the co-operative.

As discussed in the previous part of this article, successful implementation requires economic development that fits the particular socio-demographic profile of the community. Similarly, capacity-building needs to support the co-operative so that it can be adapted, managed and grown along with the co-operative's capacity. We achieve this by targeting the development of **social capital**, **market creation**, and the **governance framework** in the co-operative.

5.1 Social capital development

The core focus of social capital is to have the co-operative functioning at a sustainable level to ensure that participating members can enjoy the benefits of the co-operative. To achieve this goal, we take a series of steps to ensure that members embrace the values and principles of the model. These include marketing and organising the community into a co-operative, followed by establishing ownership through group formation, savings mobilisation, leadership, and infrastructure deployment activities.

a. Community organising and marketing

Marketing the model in the community is the first step in developing social capital. Marketing initiatives are followed by organising the community around local leadership, community members, and community-based structures. This helps to popularise the concept and principles, establishing the base of the model in the community. It is critical to this part of the process that we start to identify 'champions' who will drive the process further in the community.

b. Community ownership

As the community's awareness grows and it shows interest in the concept, the first wave of membership acquisition for the co-operative develops commitment. In this membership base, which will be around 200-300 members, a core group is formed as champions of the process. In order to strengthen the core group, we focus on the concept, philosophy and principles of the economic model and its co-operative vehicle.

c. Co-operating group formation
Upon reaching the critical mass of 200-300 members, we form groups to facilitate various aspects of the implementation, supervision, and regulation of the co-operative. Groups form around common interests (bonds) such as geographical areas or business activities. If the co-operative can leverage existing groups, the community can rapidly develop momentum in support of the co-operative. By coupling training, mentoring and support in the group with peer pressure and competition, the members more readily accept the moral and organisational culture requirements of the model, ensuring that the values and principles are implemented on an individual level.

d. Savings mobilisation
Savings contributions by members in the co-operative give meaning to the social development process. It entrenches members' commitment to the co-operative. More importantly, in the medium term savings mobilisations provide the seed capital for the co-operative to invest in business activities, or in any other opportunity which may grow the assets of the co-operative. In one example, the Motswedi Village Bank has accumulated over 3 million ZAR from 2,000 members in its ten years of existence, which is a substantial amount for a poor community to accumulate (Van de Ruit, et al, 2001).

Savings mobilisation builds group cohesiveness and ownership of the co-operative, laying the foundation for growing further commitment (McKinnon, 1973). This commitment is expressed in local dependency on the co-operative, as opposed to external grant-funded dependency.

e. Leader identification and targeting
As these social capital capacity-building interventions are deployed in the community, the facilitators become conversant with the needs and aspirations of the community. Using this knowledge, the appropriate image and brand building for the co-operative starts with the identification and development of leadership. This is important, since the appropriate leaders in a particular community will help to create the necessary values and principles that the co-operative requires to succeed in its economic development mission.

The co-operative members elect their leadership democratically according to the statutes and by-laws of the co-operative. It follows the process of creating organisational and reporting structures in a bottom-up approach. This means that a group will elect a group leader; and from among the group leaders, they will elect directors, managers and employees for the co-operative. This process firmly establishes buy-in and commitment from all members, since it follows an open, democratic route for management and leadership in the co-operative.

f. Build / identify physical structure
The final step in the social capital development process deals with physical infrastructure for the co-operative. It brings permanency to the initiative as physical assets are created, helping to establish the brand and image of the co-operative through offices and equipment. As the co-operative extends its operations, it builds credibility with outside entities that deal with the co-operative and its membership.

5.2 Market Creation
In any economic situation, markets need either to exist or to be created to identify business investments and business activities. The main problem disadvantaged, poor communities face in this regard is a lack of capital, skills, business relationships, and markets. In building this competency area – **market creation** – we must address these critical issues to ensure that the co-operative pursues sustainable economic activities. This process places the focus on equipping the community with the required competencies to manage the business, to act responsibly with business credit, and to manage business relationships between the first and second economy.

a. Financial literacy and business development
The financial literacy and business development section of this process aims to establish the required competencies for managing the business. Its base is a philosophy that propagates **asset-based community development**. This places wealth and wealth-creation within a broad developmental strategy, as opposed to **need-based community development** (Van Rensburg, 2006b). The process starts with members in the co-operative acknowledging their existing position, and then gradually takes them through a process of education and training interventions, until the

philosophy of asset-based wealth creation is firmly established in the co-operative.

We teach groups the basic principles and methods in wealth-building for asset-based community development. The purpose here is to achieve mindset changes about being poor, and using those assets that are available to the poor to create wealth in their own communities (Van Rensburg, 2006a). We deploy and teach this to the individual member in the co-operative through the group structures — the most effective way of building financial literacy capacity. Table 1 shows the set of values and principles for financial literacy training.

As individuals and groups grow in their financial literacy, we introduce more practical business planning methods to motivate members to move from 'survivalist-needs' thinking to 'investment-assets' thinking. As this happens, it creates a platform from which the co-operative can conduct sustainable business.

b. Building business credit capacity

Credit is a vital component of business creation and business expansion. In the targeted market for our economic development model, the poor lack access to capital for very small and micro enterprises. In most implementations of the model, we require a primary trading storehouse to inject business credit into the community. However, business credit creates a challenge for the co-operative facilitating the credit. In financing very small and small businesses, we have found that defaulters on a credit loan book can quickly reach 40% of all new businesses, making it extremely risky to lend into this market.

A large part of the capacity-building process revolves around operational training on credit management for the staff of the co-operative. This covers the full cycle of credit vetting, credit operations, collections, and general administration, financial management and product policies. Upon completion of the training, the co-operative's staff run its operations in an efficient and effective manner for all the products and services that the co-operative may offer its membership base.

In some of the co-operatives, the board, management team and staff have managed to increase their product offerings by 100 per cent – less than a year after becoming skilled in their operations (Van Rensburg, 2006b).

c. Creation of markets

Communities in the second economy face serious constraints when accessing markets to buy their products or services. Although this is not a unique situation for small businesses, it is made worse by the fact that business relationships and networks between second economy businesses and first economy businesses in the developmental micro-finance sector are virtually non-existent. Building the co-operative's capacity in this area requires a focus on establishing the appropriate products, attitudes, morality and market potential within the co-operative and its membership.

The first step in this process is to identify and support business opportunities in the community that have potential. The co-operative needs to acquire the ability to do this through practice. Subsequently, through the development and presentation of a business plan and budget to the co-operative board members, requesting financial support from the co-operative or from third party funders, they demonstrate confidence and member commitment.

Alongside this, we help the co-operative to develop product knowledge and packaging in the most appropriate way for its target markets. The co-operative supports this by forming partnerships for institutional support, investments and sourcing opportunities to create critical organisational capacity. This action exposes a critical level of competency in the co-operative – being able to link to the first economy and offer its products and services in exchange for revenue flows.

5.3 Governance

The third element, governance, focuses on the creation of governance systems within the co-operative, its management structures, and

Assets, not liabilities, create wealth.
Increase assets and get out of debt.
Role of good credit versus that of bad credit.
Generate wealth through savings mobilisations and business growth.
Pool savings and target big business investing.

Table 1. Capacity-building principles

members (Holden & Prokopenko, 2001). In a number of cases in the intervention, members did not act responsibly towards the co-operative, and in the process destroyed its business. These cases included bad investment decisions, no cash flow planning, non-payment of regulatory taxes, or allowing too much bad debt in loan books. To ensure sustainability of the organisation, our economic development model requires that the co-operative implement good governance practices (Bencivenga and B Smith 1991). These practices can include, but are not limited to, governance issues such as good corporate governance, legal juristic entities, management and staff appointments, deployment of operational and regulatory systems, and general governance training.

a. Corporate governance

The second King report (King, 2002) provides good corporate governance practice guidelines for a business. For a co-operative, this includes having a Board of Directors elected from the membership base to oversee the strategic direction of the co-operative. Other duties of the Board include the consolidation and integration of all members' aspirations and needs to fulfil this oversight role and responsibility. This requires policies and procedures that support corporate governance practices, as well as allowing the management team to manage and control all functions and operations in the co-operative.

b. Register legal entity

In the broader context of linking first economy and second economy business, legal juristic business entities are important. In most instances, business entities wanting to do business with the South African government or any large business have to be a registered legal entity under the applicable companies or co-operative laws. In forming the co-operative, the directors will register and incorporate it with the Registrar of Companies in accordance with the applicable laws.

c. Appointment of management and staff

The Board of Directors appoints operational staff on their good business judgement. The capacity-building process helps them to ensure that they follow correct policies, procedures and processes in all human resource related activities. It aims to address the risks of dealing with staff – having the basic capabilities to deal with appointments, management and exit of staff in the organisation.

d. Deployment of operational and regulatory systems

Deploying operational systems, policies, procedures and processes in the co-operative ensures the basic delivery of services by the co-operative to its market. It also reduces the risk of organisational failure due to bad service, poorly design operational processes, and a lack of operational capability in the organisation (Levine, 1991).

Within these systems, we include operational compliance, business performance and key performance indicators as management practices, to make the business of the co-operative transparent to all related stakeholders.

e. Governance training

The main idea behind governance training is to ensure that good governance principles shape the value system of the co-operative and its membership. We do this through various forms of governance training for board members, staff members and the membership itself.

To end our discussion of the capacity-building process, we must say that implementing it is not a simple and straight forward process. Capacity-building requires a delicate balance between achieving business sustainability and contributing to the socio-economic development of its members. As stated in the introduction, capacity-building is a prerequisite for sustainability, although not a guarantee for success. It reduces the risk of failure by addressing those competency areas that, in many cases, are taken for granted in formal businesses.

6. Measuring the Impact of the Model

If the old saying, "To measure is to know", is true for our economic development model, than it also holds true for any private or public organisation. Different stakeholders in the process want to see the impact of the intervention through quantitative data, rather than through subjective measurements and discussions. In a recent study I did to obtain quantitative data to research and test credit vetting models in the South African micro-finance industry, I obtained very little usable data, even from those institutions that have been in operation for more than five years.

In measuring the model, we need to ask and answer two types of questions:

(1) Is the model *sustainable*?

(2) What impact does its implementation have on a community — the *outreach* perspective?

6.1 Sustainability

We measure sustainability through a **sustainability profile**. This includes important socio-economic information in order to profile the economic activities in the co-operative against group formations. Typical attributes include, but are not limited to, financial statements such as balance sheets, income statements, cash flow statements, group formations, business activities per group formation, co-operative product portfolio reports, typical CGAP (Consultative Group to Assist the Poorest, 2000) indicators, and credit risk profiles. A trained analyst will quickly gain accurate insight into the level of sustainability of the co-operative through these reports.

6.2 Outreach Profiles

The *outreach profile* aims to provide sensible demographic information on the co-operative and its membership base. This is specifically aimed at reporting on the outreach that the co-operative achieves in its community, using particular measurable attributes of the membership base. Table 2 presents a number of examples of these measurable attributes.

7. Implementation Lessons

Since we completed the original design in the course of 2002, we have implemented various versions of the model in different communities to test its feasibility and impact. During its development we formulated the hypothesis that financial service activities are important in economic growth and poverty reduction (DFID, 2004). This was also the common denominator in all implementations of the model, although we followed different approaches through the use of primary and secondary co-operative groups.

At the primary level, the co-operative organisation, Sakhubukumkani Co-operative Ltd, included very small micro-enterprises in direct project pilots. (Sakhu Co-op Ltd is the implementation vehicle of Wezi Ximiya, founder of the economic model.) This co-operative has grown from its original two founding members to over 1,000 very small and micro enterprises members.

At the same time that Sakhu Co-op Ltd supported and developed primary groups through privately funded initiatives, it partnered with various governmental and corporate stakeholders to reach secondary groups of co-operatives. Whereas Sakhu Co-op Ltd engaged directly with the primary groups, the secondary groups were exposed to the model as a reference point or best practice model with which they could align themselves. This was made possible through corporate sponsorship of the economic development model.

In Table 3 we provide an estimated summary of the impacted population, combining the primary and secondary groups into one. Through this, we show that different organisational types have been tested, with micro credit outlets being the only group not part of the co-operative movement.

In the development, implementation and refinement of the model, we have learnt a number of important lessons. Interestingly enough, we can arrange these lessons according to a typical operations management taxonomy that I use to analyse operations in first economy businesses – showing that fundamental business principles are common to first economy and second economy businesses (Van Rensburg, 2005). We used four areas for analysis purposes: strategy and positioning, credit management, markets, and operations management.

Base Information	Specific Information
National identification number	Income levels
Date of birth	Disabilities
Marital status	Ethnic grouping
Communication access (fixed line, cellular line)	Type of residence area
Physical address	Formal banking relationships
Duration of occupation	Number of dependants
Type of ownership	Type of dwelling
	Level of education

Table 2. Outreach attributes

Organisation Type	Core focus/main activities	Number of organisations	Estimated customer base per organisation
Micro Credit Outlet	Micro credit services its customer base.	20	1,000
Financial Services Co-operatives	Providing micro-finance services to their membership base.	75	1,000
Savings and Credit Union	Savings and credit services to its membership base.	1	1,000
Consumer co-operatives	Micro credit lending to its membership base	20	1,000

Table 3. Sample population

a. Strategy and positioning

In covering the micro-finance developmental sector in South Africa, my qualitative investigation has led to the hypothesis that most of these institutions do not operate on a sustainable basis, and can only meet cash flow requirements thanks to donor funding.[1] Within these organisations, the level of managerial and operational capacity for dealing with numerous important business issues is generally low, although in a number of cases extensive academic knowledge was accumulated in the field of micro-finance. General governance is virtually non-existent in the smaller organisations, and severely limited in the bigger organisations. In combining these factors, I found that most of the organisations were limited in their capacity to devise strategy, or to position themselves effectively in their markets to operate a sustainable business.

I could identify virtually no external linkages with the first economy, apart from those organisations that focus on obtaining grant funding for their operations. In relation to building capacity to create linkages with first economy opportunities, such as the provision of services through public tenders, discovered that these second economy businesses were not good corporate citizens, and lacked the capacity to deal with the first economy. This meant that in most cases they could not meet procurement policies and procedures insofar as tax and legal issues were concerned.

The majority of co-operatives involved in this project deal in one way or another with fast-moving consumer goods. As a direct result of the segregation and exclusion policies of the apartheid regime, FMCG supply chains were not formally developed into peri-urban and rural areas over the years, and informal trading satisfied the needs of people. Because of the low barrier to entry into this business, FMCG forms a major source of business in the second economy. As a result, customers will pay between 30% and 60% more for FMCG goods in these informal supply chains than those in the formal economy. However, in this monopolistic structure lie opportunities for the co-operatives to create a strategy for wholesale co-operative retailing as found in countries such as the United Kingdom (the Co-operative Group, 2006).

Co-operatives, and the communities they operate within, differ from region to region, as well as from urban areas to rural areas. This requires different strategies and implementation methods for the economic development model – especially concerning social capital and its capacity-building process.

b. Credit Management

Providing credit for small businesses, especially small businesses without any collateral, is a challenge; in funding start-up businesses for co-operative members, every one of these loans defaulted (Stiglitz & Weiss, 1981). In extending credit to co-operative members running existing businesses, we found that in the disbursement of over 20,000 small business loans that, on average 20% to 30% of small businesses are good repayers of credit with very little or no default.

Analysing bad debt and non-repayment of loans for these businesses revealed a number of common internal and external factors. Internal factors are those over which the business owner has control, and they typically include factors such as business expansion and stock purchasing without adequate cash flow planning. External factors are those over which a business owner has no control, and include theft, accidents, illness, and the like.

A vital component of credit management is managing risk through credit vetting methods, tools and techniques (DFID, 2004). In the South African micro-finance industry, meaningful quantitative data does not exist, and so proper credit vetting models for unsecured loans are difficult to construct. In most of the organisations, there is very little capacity to perform effective credit vetting in order to protect the co-operative against bad debt. Organisations such as the Small Enterprise Foundation (SEF) use various methods and tools to asses the profile of the market to target poor families; but from the economic development model viewpoint, it is questionable whether these are sustainable business practices (Van de Ruit, et al, 2001).

c. Marketing

From a marketing perspective, the institutions involved did not see themselves as commercially oriented businesses, but rather as social developmental instruments. As in any business, the growth of the business is very dependent on marketing the appropriate products and services to customers in a particular market segment. We have to correct this shortfall in capacity in order to achieve the co-operative's sustainability.

d. Operations Management

In running the operations of the co-operative, it is critical that affordable operational systems are in place to support the business and to allow the business to expand and grow without being hampered by exorbitant expenses. Although the business of the co-operative is simple, the scope of products it offers can create a microcosm of banking and financial transactions. It is a major challenge to manage a co-operative in the way that a financial institution **should** manage administrative and financial transactions, as a broad set of skills and knowledge is required.

As part of the economic development model, the co-operative normally employs local community members to perform administrative, financial and managerial activities.

In a few cases employees will have the appropriate level of skills and knowledge, but in most instances co-operative employees require human resource capacity-building. The challenge here is that capacity-building interventions need to be relevant, practical, and focused in order to mobilise and equip staff to the appropriate level of operational proficiency. This level of proficiency must support the organisation in meeting its operational objectives of cost, quality, speed, dependability, and flexibility.

The above lessons show that running an institution in the developmental micro-finance sector does not require different skills and competencies from those needed to run a formal business in the first economy. The shareholders, management, and staff of the co-operative must still ensure that they adhere to the basic principles of a business: having a good product or service offering, customers that buy from the business, and well-run operations to make sure that the co-operative can be sustained.

8. Conclusion

The majority black population in South Africa lives in extreme poverty, and simply seeks to meet basic needs to survive (Landman, 2003). Amidst existing programmes and interventions to reduce poverty and stimulate economic growth, concerns are growing that earlier expectations of significant first economy growth and job creation may not be realised at grassroots level. Currently poverty, unemployment, and underemployment are still increasing in this group of people; and this translates into a growing social welfare burden for South Africa.

I believe that the cornerstone of addressing poverty reduction and economic growth is a focus on the consumer and small business owner in communities through co-operative structures. Co-operative structures are a fitting juristic entity for members to create a social enterprise, in which they can do business, but also grow the social awareness and social responsibility of the members in the co-operative. Key to this process is the establishment of ownership and behaviours that strengthen the co-operative into a sustainable organisation for its members.

In this article I have presented an economic development model that enables co-operatives to create wealth in the community through micro-finance activities. The core of this wealth creation lies in mobilising savings through the co-operative structure for asset acquisition, with the long-term effect of changing the social standing of its members.

In conclusion, using a co-operative structure to implement the economic development model aims to help poor communities to build assets that will enable them better to access basic services such as health, education, food security, and — eventually — wealth.

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Notes

[1] This hypothesis does need to be proved quantitatively through a scientific research project.