**THE SMALL ENTERPRISE FOUNDATION**
**(An association incorporated under Section 21 of the Companies Act)**
**(Registration number: 1991/003485/08)**

**ANNUAL FINANCIAL STATEMENTS**
**30 June 2008**

# THE SMALL ENTERPRISE FOUNDATION

## MANAGEMENT REVIEW

## 30 JUNE 2008

*"SEF has empowered me and I have been able to not only provide for my family, but for my community too. I am a leader in my community, I teach other women how to sew clothes and also I serve as an advocate for the disabled in securing them housing".*
*Jane Mashego (SEF Client)*

## Summary of Performance

The Small Enterprise Foundation, SEF, is a non-profit, non-government organisation dedicated to ending poverty. The organisation was registered in July 1991 and disbursed its first loans in January 1992. The following is a summary of performance:

| Indicator | June 2008 | June 2007 | June 2006 |
|---|---|---|---|
| Number of active clients | 50 319 | 41 295 | 34 553 |
| % Women Clients | 99% | 99% | 99% |
| Value of Loans Outstanding | R 70.8million[1] | R 49.9 million | R 36.4 million |
| Current Average Loan Size Disbursed | R 1 715 | R 1 592 | R 1 547 |
| Number of Loans disbursed since inception | 468 705 | 364 827 | 284 626 |
| Amount disbursed since inception | R626 million | R467 million | R330 million |
| Bad Debts as % of annual disbursements | 0.3% | 0.2% | 0.3% |
| Bad Debts as % of average Principal Outstanding | 1.0% | 0.7% | 0.96% |
| Portfolio at risk > 30 days | 0.2% | 0.3% | 0.4% |
| Current Re-scheduled loans (due to illness) | R 320 422 | R 339 411 | R 196 484 |
| Death write-offs | R 337 159 | R 246 911 | R 184 122 |
| Total Savings held by clients | R 9.5 million | R 6.4 million | R 4.4 million |
| Total staff at year end | 255 | 250 | 177 |
| Total operations staff at year end | 214 | 211 | 146 |
| Clients per loan officer | 284 | 261 | 281 |
| Operational self-sufficiency[2] | 96% | 98% | 97% |
| Financial self-sufficiency[3] | 95% | 97% | 95% |

[1] At the close of the financial year the Rand/US$ exchange rate stood at R7.918 = US$1.00

[2] Operational self sufficiency = Financial Revenue (Total) /(Finance Expense + Loan Loss Provision + Operating Expense)

[3] Financial self sufficiency = Financial Revenue (Total) /(Finance Expense + Loan Loss Provision + Operating Expense + an adjustment which assumes all borrowings are at the prime lending rate)

**Introduction**

The Small Enterprise Foundation is a growing development organization.

**Values**

We believe in :

Respect for all

Having positive impact on the lives of our stakeholders

Striving for operational efficiency and self-sufficiency

**Mission**

To work aggressively towards the elimination of poverty by reaching the poor and *very poor* with a range of financial services to enable them to realise their potential.

**Vision**

A world free of poverty

## Highlights 2008

**SEF now serving 50 000 very poor entrepreneurs**

This financial year saw SEF growing to serve more than 50 000 poor people. This is the total number of active clients, each of whom is seen twice a month!

**Cumulative Disbursements exceed R500 million**

In October 2007 the organisation attained a milestone of over R500 million disbursed since inception. Thus, by that date the organisation had invested more than half-a-billion Rand in income generating activities of the very poor. By the end of the financial year this figure had reached R626 million.

**R20m support from Old Mutual for expansion into the Eastern Cape**

During the year we entered into a partnership with the Masisizane Fund of savings and investment group Old Mutual to create a R20 million microfinance fund. This fund is aimed at supporting the development of women enterprises in rural areas of the Eastern Cape, one of our country's poorest provinces.

Old Mutual must really be commended for their recognition of microcredit for self-employment as a powerful tool in the fight against poverty.

## BACKGROUND TO THE SMALL ENTERPRISE FOUNDATION

The Small Enterprise Foundation, SEF, was established with a mission to fight poverty in a sustainable manner. This is done by enabling the poor to increase their income through microcredit for self-employment and by assisting them in the accumulation of savings. SEF began operations in 1992 and since then has cumulatively disbursed 469 000 loans to the value of R 626 million to very poor women.

The organisation is now located in three of South Africa's provinces, namely, Limpopo Province, the most northerly province, Mpumalanga Province to the east of Johannesburg and the coastal Eastern Cape Province. The Limpopo and Eastern Cape provinces have the highest proportion of poor in the country with 77% and 72% of their populations living below the poverty income line, respectively.[4] The areas of Mpumalanga in which SEF works are characterised by similar poverty.

As the organisation's mission statement suggests, SEF works to reach the poor. In 1996, the organisation started a special program to target the *very poor* – those from households whose income is less than half the poverty line[5]. As a consequence the organisation now has two programs, MCP, which aims to work with poor people who have an existing micro-business and TCP which specifically targets women from households which are below half the poverty line. With 34 382 clients, TCP makes up 68% of active clients, with MCP serving the remaining 32%.

### Methodology

SEF starts working in a community by first identifying the poorest households through Participatory Wealth Ranking (PWR). Thereafter, field staff go to these households to motivate the women to start an income generating activity or in other cases where a previous micro-business had collapsed due to lack of funding then the women are encouraged to resume that enterprise. The motivation provided by the field staff, combined with access to a small loan is often all the *very poor* need to launch an income generating activity or micro-enterprise.

While the poor may be motivated to start a micro-business naturally one of their biggest hurdles is the lack of money to do so. It is here that SEF utilises the approach pioneered by the Grameen Bank of Bangladesh to provide microcredit for micro-enterprise.

A very poor person who wishes to access SEF's services is required to form a group with four others whom she knows very well and trusts. Each of the five must also be interested in obtaining a loan for their own individual business. The five group members are then required to guarantee each others' payments. No other collateral is required. SEF's loans are only for enterprise and a series of checks are in place to ensure that loans are not diverted for other purposes.

The graph of Business Value, on page 10 illustrates how successful clients are at starting and growing their businesses. This graph shows the average business assets of clients before each loan cycle. For example, before the first loan the average business value of clients is less than R100 (US$13) whereas by the beginning of the fourth loan cycle this has grown to an average of R1360 (US$172).

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[4] "*Fact Sheet, Poverty in South Africa*", Fact Sheet No.1, 26 July 2004, Human Sciences Research Council
[5] The "household subsistence level" is used as the poverty line. In 2001, this stood at R920 (US$121) per family of five per month.

## SAVINGS

In terms of South African law SEF may not take deposits so, instead of providing a direct savings service, the organisation strongly motivates its clients to save with a formal banking institution. This is done by providing training on how to open and operate a formal savings account and then motivating clients to save at each of their fortnightly meetings.

Due to its extensive outreach in rural areas, the majority of SEF's clients deposit their savings at the Post Bank while the remainder utilize Nedbank. As at the end of the financial year the cumulative sum of savings as held by clients in their Post Bank or Nedbank accounts amounted to R 9.5 million.

## OPERATIONAL PERFORMANCE REVIEW

### Growth

This year SEF continued its focus on expansion. Four new branches were opened, two in Limpopo and two in the Eastern Cape Province, and SEF now has 27 branches.

We passed yet another major milestone by serving more than 50 000 clients. By the end of the financial year the organisation was actively serving 50 319 clients. The graph below illustrates the growth since inception. On a compounded basis SEF has cumulatively grown by more than 25 % per annum for each of the past 6 years.

Figure 1 - Active Clients

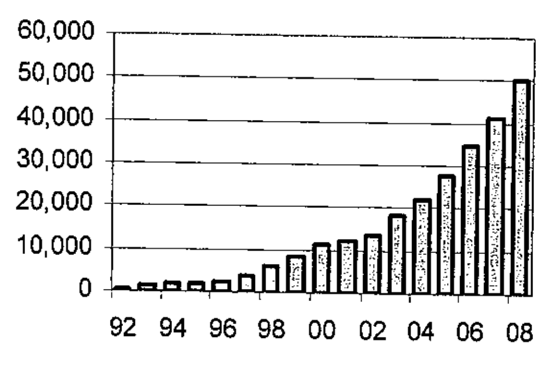
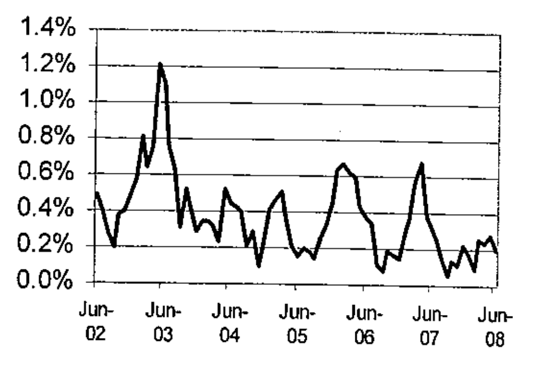
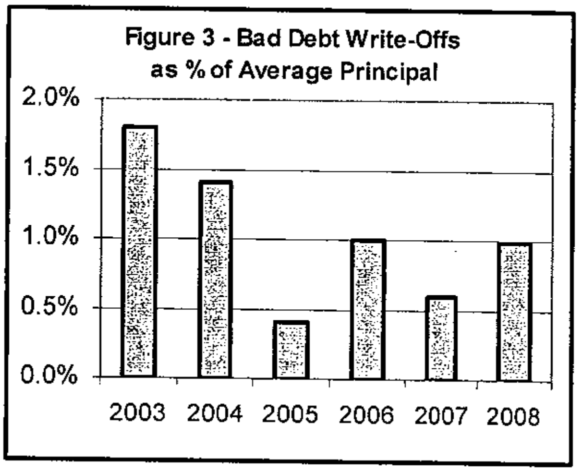


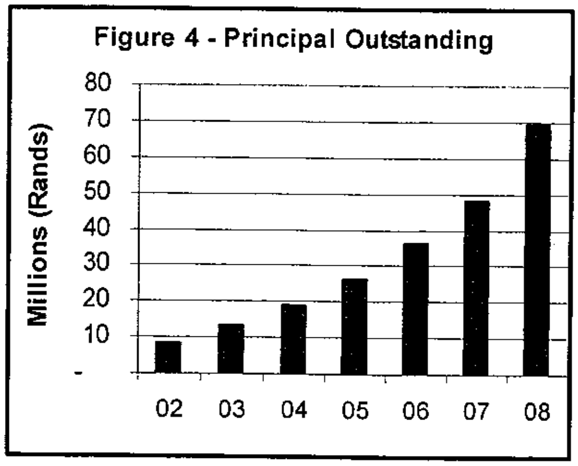

Figure 2 - Portfolio at Risk




### Portfolio at Risk

I am pleased to report that this was once again a strong year in terms of the arrears and portfolio at risk performance. The portfolio at risk over 30 days remained below 0.5% throughout the financial year. The portfolio at risk over 30 days is shown in Figure 2 above.




## Bad debt Performance

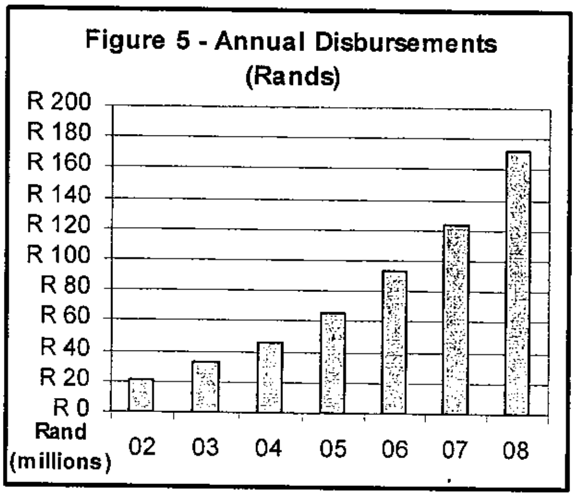
SEF has a very strict bad debt write-off policy with loans being declared not recoverable as soon as any part of any instalment is more than 84 days in arrears. Despite this tough approach Figure 3 illustrates how well the organisation has done in terms of bad debt performance. This year bad debts as a percentage of annual disbursements amounted to just 0.3%, or 0.98% when expressed as a percentage of the average principal outstanding for the year.

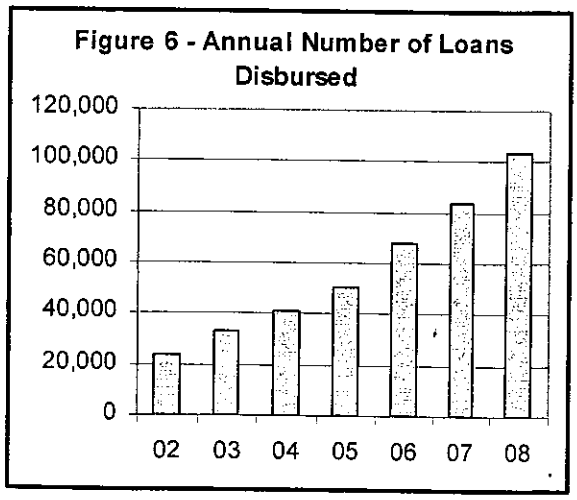
## Principal Outstanding

Over this financial year principal outstanding grew by 42% to R70 million. The strong growth in principal may be seen in Figure 4 above.

## Disbursement Activity

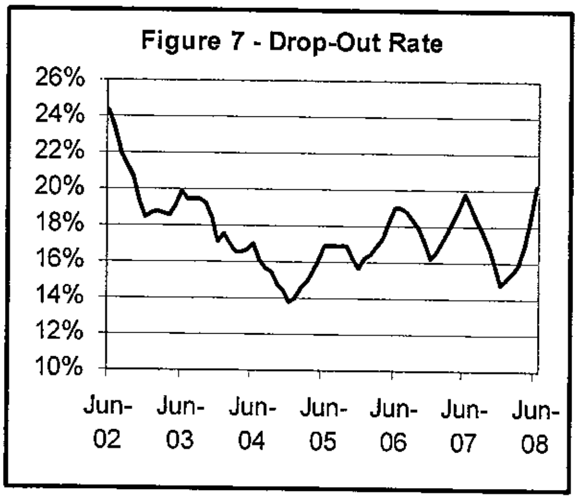
The vast majority of loans are repaid over six months thus when considering SEF's performance it is wise to look not only at the principal outstanding but also the disbursement activity. The following graphs, Figures 5 and 6, indicate how substantial this activity is, both in terms of the amount and number of loans disbursed.

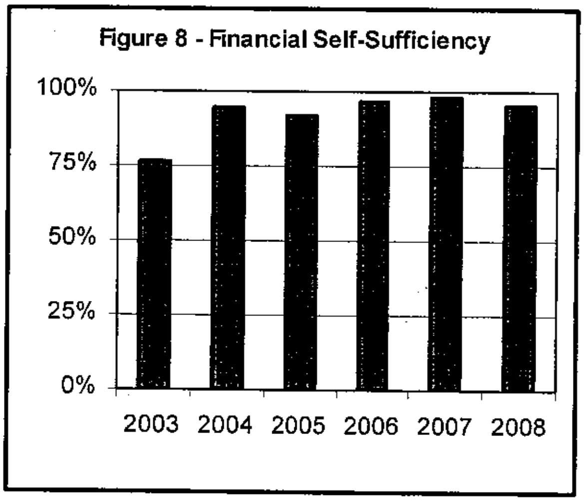


**Operational Challenge**

Figure 7 illustrates the client exit or drop-out rate. It will be seen that this has a cyclical nature with the highpoint coinciding with the financial year-end. The exit rate currently stands at 20%. The organisation is determined to improve its client retention.




**Operational Self-Sufficiency**

The organisation's financial performance in terms of operational self-sufficiency, the ratio of all operating income (loan plus investment income) to all operating expenses, including finance costs and loan loss provisions, stood at 96% for the year. Financial self-sufficiency[6] came to 95%.

As will be seen from Figure 8 above SEF has maintained its operational self-sufficiency above 90% since 2004. In fact, the organisation attained 100% operational self-sufficiency for the financial year to September 2004 but since then has continued a strategy of constant growth. Naturally growth implies additional investment, additional costs, before the income from the growth is seen. The organisation's chosen strategy is to balance growth and operational self-sufficiency.

**Eastern Cape**

SEF's expansion into the Eastern Cape deserves special mention. Until now the organisation has pursued an organic expansion strategy of always growing "to the next village". Quite literally new operations were always started in areas immediately adjacent to existing activities.

In 2007 Old Mutual approached SEF and encouraged it to launch operations in the Eastern Cape which is over a thousand kilometres from the current operational area. Through its Masisizane Fund Old Mutual then provided significant funding in the amount of R20 million to make this possible.

To date SEF has opened two branches in this area. The organisation's approach and product have been extremely well accepted and thus far there has been no need for any regional adaptation. After seven months of operations there has not been a single arrear over 30 days in this area.

[6] See definitions of these terms at the foot of page 1.

### Value Added Tax

In South Africa Valued Added Tax (VAT) is not applied to interest charged on loans but is charged on any fees, including financial transaction fees. In the past SEF only charged interest on its loans and, therefore, did not have to charge VAT to its clients.

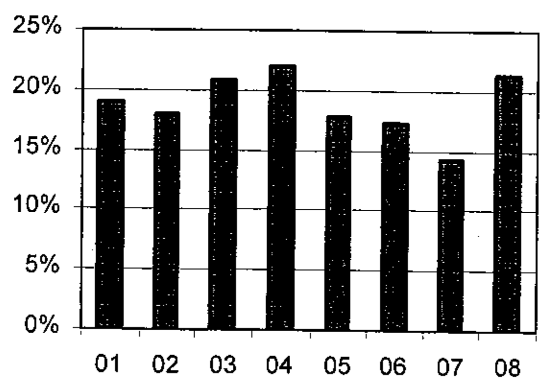
The main provisions of the new National Credit Act came into force on 1 June 2007. This act limits the level of interest that may be charged but allows institutions to also levy initiation fees and monthly service fees. In order to earn the same income from loans as it had previously done SEF was forced to break its income into interest plus initiation and service fees. As these fees attract VAT the organisation now has to charge and pay over VAT. In effect this has meant a most unfortunate increase in costs to the very poor. This came into effect in November 2007.

## HUMAN RESOURCES AND TRAINING

As at the end of June 2008 SEF employed a total of 255 staff, including 177 Development Facilitators[7] and 27 Branch Managers.

Figure 9 below demonstrates that the organisation has faced moderate to high staff turnover over the past years. While corrective performance management has been responsible for more than half of this turnover other factors have included government drives to recruit teachers (SEF had employed many unemployed teachers as Development Facilitators) and tough working conditions. The latter refers to staff working in isolated villages without many modern amenities and without the supportive environment of working daily with colleagues. During the past financial year staff turnover rose to 21%. The reduction of this has been identified as one of the organisations priorities.

Figure 9 - Staff Turnover




SEF provides the fundamental training for all of its staff itself. In particular this applies to Development Facilitators and Branch Managers. Use is also made of key external training interventions to further enhance the capacity of staff, especially managers.

[7] "Development Facilitator" is the SEF term for a field officer.

## RESEARCH AND DEVELOPMENT

The key themes in the R&D Department over the past two years have been improving SEF's poverty measurement tools, management systems and the incorporation of successful operational pilots into field operations.

With these themes in mind, some of the R&D Department's measurable results over the past year include:

- A Dropout Survey outlining some of the main causes of client exit.
- A pilot test comparing results of the Participatory Wealth Ranking (PWR) with the Progress out of Poverty Index (PPI), a statistically valid method of poverty asssessment.
- Completion of input into the MCRIL/EDA Rural Social Rating which will evaluate SEF's social performance.
- The formalisation of SEF's pre-paid repayment system and the integration of this into operations.

## ADMINISTRATION DEPARTMENT

Administration had a successful year with productivity remaining very high at above 4 000 clients per Loans Administrator. Our administrative systems have been fully adapted in line with the requirements of the National Credit Act.

## INFORMATION TECHNOLOGY SYSTEMS

SEF's information technology systems are currently undergoing transformation to better support the organisations mission and growth.

Several key areas are being addressed in parallel projects:

1. Upgrade of System Infrastructure:

   Network infrastructure and core systems are being migrated from a highly integrated Microsoft Small Business Server environment to a dynamic Enterprise Architecture that will reduce risk and provide many benefits while adhering to good governance.

2. Process Improvement (Workflow):

   Operational and internal processes will benefit from the structure and control offered by Workflow technologies. This simplifies the integration of disparate and legacy systems while providing a unified front-end to system users.

3. Loan Portfolio Management System (or MIS):

   A new MIS system will be acquired before the end of the 2008 calendar year. After compiling a short list of solution vendors, interviews and client site visits were carried out to determine product suitability and overall satisfaction levels. Vendors of note are Neptune Software (Orbit), Fern Software (Abacus One World), SEG Data (Workflow System) and IBM/C.A.R.E (Financial Matrix using Mifos). Sites visited were Finca

Uganda, Faulu (Uganda), Finance Trust (formally Uganda Women's Finance Trust) and Kuyasa Fund (South Africa). The selection phase of this project is nearing completion.

While these areas indicate some of the current highlights, SEF will continue to improve its systems and implement technology where possible to improve its ability to serve the poor.

## QUALITY ASSURANCE

The purpose of the department is to ensure that:

- All activities in the organisation are performed according to internal policies and procedures.
- Corrupt and/or fraudulent activities are prevented, identified and reported on.
- Special assignments as may be requested by senior managers are executed.
- Weaknesses/threats to the organization are identified and preventative measures are recommended.
- The overall service to our clients, the very poor, is of high quality.

By the end of June 2008, the Quality Assurance department had completed 48 routine audits and 12 special assignments as requested by senior managers.

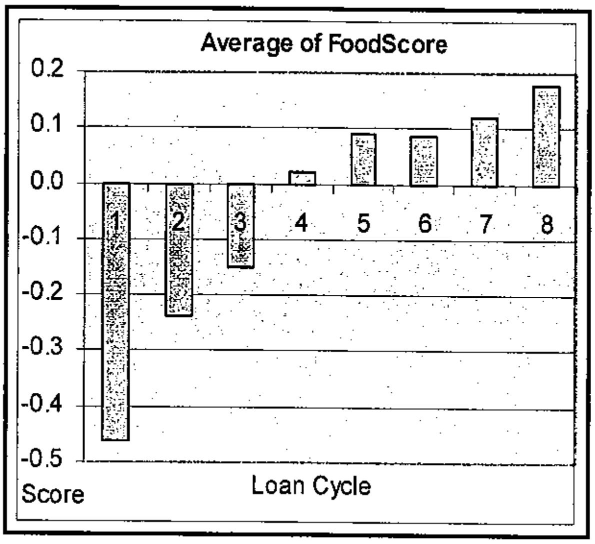
A branch rating system has now been introduced into our operations. This system will seek to evaluate and compare the compliance levels of branch activities against the internal policies and procedures, and in the long run help managers in dealing with quality issues. To further enhance portfolio quality, this system is built into the incentive scheme for Branch Managers. The rating system also ranks branches against each other on the basis of the quality score results.

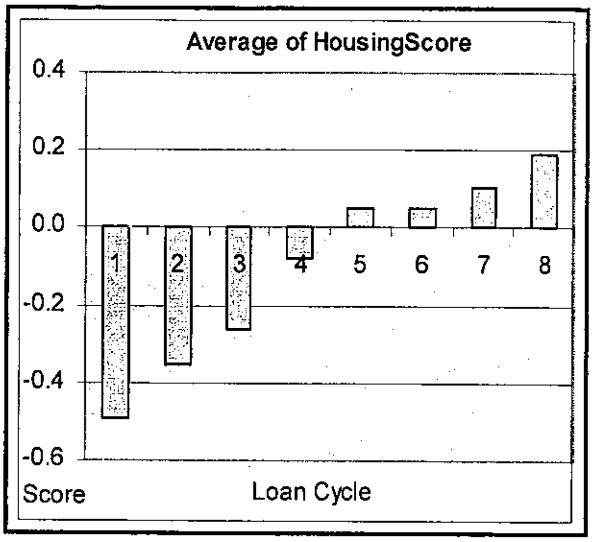
## IMPACT

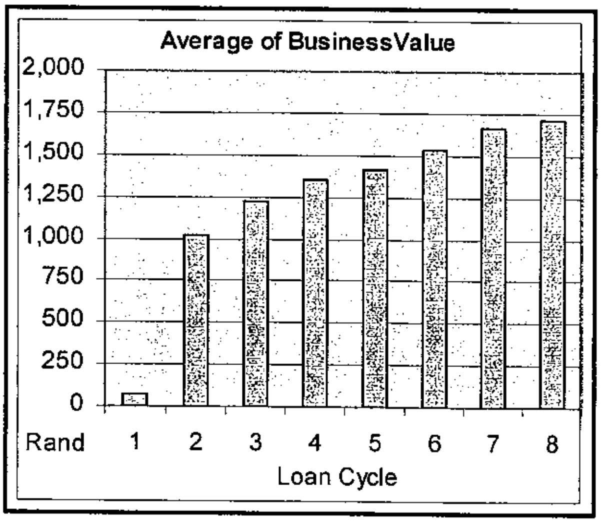
SEF does not just see microfinance as a simple process of people taking and repaying loans or using convenient, low cost savings instruments. For SEF microfinance is about whether people utilise such opportunities to improve the lives of their families and ultimately move out of poverty. Thus SEF is not only concerned about its own operational efficiency and sustainability but whether its work has a positive impact on the lives of those with whom it works.

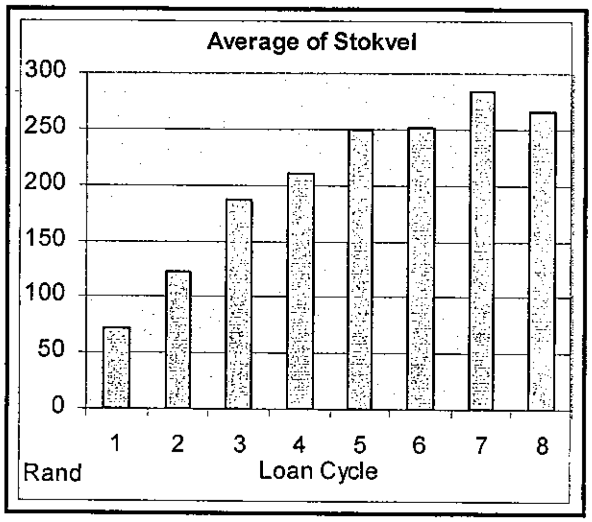
SEF uses an impact monitoring system to check, measure and understand the impact of the program on an ongoing basis. Using a participatory methodology, each client is interviewed on a number of key impact indicators before each loan cycle. This understanding not only informs SEF whether it is attaining its goal of positive impact but also provides information on how to improve performance to ensure better impact, and consequently improve operational and financial performance.

The following graphs illustrate outputs from the impact monitoring system for the quarter ending 30 June 2008. The first graphs were compiled from interviews with clients about their own perceptions of the quality and quantity of food consumption in their households and the quality of their housing. Their responses are allocated scores on a scale of -2 to +2 and the graphs display the aggregate responses at the start of successive loan cycles. The remaining graphs display the actual measured value of business assets and client savings, again measured prior to successive loan cycles.




## HIV/AIDS AND MICROFINANCE PILOT PROJECT

### IMAGE Project (Intervention with Microfinance for AIDS and Gender Equity)

IMAGE and SEF are now entering their eighth year of partnership. The IMAGE project combines SEF's microfinance work with a participatory training curriculum which focuses on gender empowerment and HIV/AIDS. The aim of the initiative is to address structural factors which fuel the HIV epidemic – particularly poverty and gender inequalities – with the aim of reducing vulnerability to the dual epidemics. Trained facilitators work in centres for 12 months providing structured training for the first six months followed by support for community mobilisation activities in the second six months.

Since undergoing a Pilot Phase between 2001 and 2004 and an initial upscale from 2004 to 2007, the IMAGE Project has been successful in reaching over 4,500 households in 83 villages in the Sekukhuneland region of Limpopo Province. During this establishment, the IMAGE Project has undergone a rigorous impact assessment by the University of the Witwatersrand and the London

School of Hygiene and Tropical Medicine. Over a two-year evaluation period, households of participants experienced substantial improvements in economic well-being, household status of women and, most promisingly, a reduction in intimate partner violence by 55%. The study also demonstrated that among young women who participated in the intervention, there were shifts in a number of key HIV-related risk behaviours – including higher rates of condom use. Key outcomes have been published in the Lancet medical journal, and the IMAGE Project has been heralded by the World Health Organization as a 'best-practice example' of a structural intervention to prevent and mitigate the effects of HIV infection in poor communities.

The project has received support from AngloPlatinum and operations are now being scaled up with an agreement to train 15,000 SEF clients over the next three years. To meet this target IMAGE is establishing field offices in the Mokopane and Fetakgomo areas of Limpopo Province and has recruited an additional nine members of staff.

Administration and management of the IMAGE project has moved from the University of the Witwatersrand to the Wits Health Consortium. An IMAGE Project office now resides within SEF's headquarters in Tzaneen.

**FUNDING**

I wish to use this opportunity to recognise our donors and to sincerely thank them on behalf of the organisation and our clients who have used the possibility provided by these donors to transform the lives of their families. The organisation wishes to humbly note that its work and significant achievements would not have been possible if it were not for the support of these donors. These funders share SEF's belief that microfinance can assist the poorest to improve their livelihood and through their financial support they contribute to the alleviation of poverty through microfinance.

During the past financial year the following donors provided operational grants:

- Old Mutual, through its Masisizane Fund
- Hivos.

The following donors provided capital grants:

- Old Mutual, through its Masisizane Fund
- The International Alliance for Women (TIAW)
- Threshold Foundation
- SIDA
- Vantage Capital.

Our appreciation is also due to private individuals, Dr Margaretha Vintges and Dr Gert Marincowitz, for their generous personal loans to SEF. These funds are being used as loans to *very poor women.* The support of these private individuals, who would otherwise have been able to earn more on their money by just depositing their funds into a conventional bank, not only provides low cost funding for SEF but their act of faith and belief in us inspires us.

SEF funds its loan book through loan facilities from the following organisations. While these loans are mainly provided on a commercial basis it must be recognised that, like SEF, all of these organisations also strive to attain a double bottom-line of social and investment return.

- ABSA, through a guarantee provided by Thembani International Guarantee Fund
- Genesis Steel
- Khula Enterprise Finance Limited
- Oikocredit
- Sentinel Steel
- Swedfund
- TEBA Bank, through a guarantee provided by Thembani International Guarantee Fund
- Tembeka Social Investment Ltd
- The Hivos-Triodos Fund
- Umsobomvu Youth Fund

The organisation wishes to thank these agencies for their excellent ongoing service and support. Without them the lives of 50 000 formerly very poor South Africans would not have been as hopeful as they are today.

## EXPANSION PLANS

The financial year saw SEF once again assess its strategic plans. Based on many factors including the fact that the organisation has grown by a cumulative 25% per annum for the past six years, the maintenance of excellent portfolio quality, strong social and financial performance and the ability to attract financial support, the decision was made to focus the organisation to roll-out the current methodology and products at a growth rate of at least 20% per annum until SEF is serving 350 000 active clients. This figure is based on a conservative estimate of the penetration that SEF currently experiences in the rural and peri-urban areas of its current operations. This expansion will take SEF into every rural and peri-urban corner of South Africa. The organisation is now fully focussed on this goal.

The following table illustrates the expected growth for the next five years:

| KEY STATISTICS | June 2009 | June 2010 | June 2011 | June 2012 | June 2013 |
|---|---|---|---|---|---|
| # Active Clients | 60,243 | 75,486 | 94,114 | 113,058 | 136,819 |
| Principal Outstanding | R 91 million | R130 million | R180 million | R238 million | R316 million |
| Financial Self Sufficiency | 92% | 97% | 106% | 115% | 125% |

## DIRECTORS

I would like to thank all board members, Matome Malatji (Chair), Sanjay Doshi, Marie Kirsten, Mutle Mogase, Modise Motloba, Olivia van Rooyen and Sizeka Rensburg for their continued guidance and support during the past year. This year saw an addition from our partnership with Old Mutual in the person of Charmaine Groves. I express my appreciation to you for joining the board of SEF. In addition I would like to thank Nkosana Mashiya for his advice and encouragement.

SEF's board conduct their work with the organisation on an entirely voluntary basis and yet are totally committed to ensuring that the organisation remains true to its mission and to achieving success in terms of that mission. I truly appreciate the time that they take from their own lives and from their families to assist us in our struggle to end poverty.

## THE CONTRIBUTION OF SEF's STAFF

In December of each year the organisation recognises the outstanding performances of staff. This year's best performers were:

| | | |
|---|---|---|
| Best Branch Manager: | Alfrida Ramoroka | |
| Best Branch Manager- 1st runner up: | Donald Mhangwana | |
| Best Development Facilitators: | Rinono Mushwana<br>Clarence Matshaba | |
| Best Development Facilitators- 1st runner ups | Cylia Roholane<br>Lazarus Maake<br>Grace Mudogwa<br>Euphilia Mbhalati | Rachel Maimela<br>Edna Tshikovha<br>Colbert Baloyi<br>Maria Malesa |
| Best Support Staff | Noko Mathatho | |
| Best Support Staff- 1st runner up | Gabaza Mushwana | |

On behalf of the Board of Directors and the organisation as a whole, I would like to congratulate all of these staff members for their excellent achievements and contributions to our work.

I wish to underline my gratitude to all of SEF's staff for their hard work, their determination to see the organisation succeed and their continued efforts to ensure that the poor overcome poverty.

John de Wit
Managing Director
06 November 2008

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**30 June 2008**

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## DIRECTORS' RESPONSIBILITY STATEMENT AND APPROVAL OF THE ANNUAL FINANCIAL STATEMENTS

The directors of the company are responsible for the maintenance of adequate accounting records and the preparation and integrity of the annual financial statements and related information. The annual financial statements have been compiled in terms of South African Statements of Generally Accepted Accounting Practice.

The directors are also responsible for the systems of internal control. These are designed to provide reasonable, but not absolute, assurance as to the reliability of the financial statements, and to adequately safeguard, verify and maintain accountability of assets, and to prevent and detect material misstatement and loss. The systems are implemented and monitored by suitably trained personnel with an appropriate segregation of authority and duties. Nothing has come to the attention of the directors to indicate that any material breakdown in the functioning of these controls, procedures and systems has occurred during the year under review.

The financial statements are prepared on a going concern basis. Nothing has come to the attention of the directors to indicate that the company will not remain a going concern for the foreseeable future.

The annual financial statements, set out on pages 5 to 31, were approved by the board of directors on 6 November 2008 and are signed on its behalf by:

Director

Director

**Deloitte.**

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## INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF THE SMALL ENTERPRISE FOUNDATION (AN ASSOCIATION INCORPORATED UNDER SECTION 21 OF THE COMPANIES ACT)

We have audited the annual financial statements of The Small Enterprise Foundation (An association incorporated under section 21 of the Companies Act), which comprise the directors' report, the balance sheet as at 30 June 2008, the income statement, the statement of changes in equity and cash flow statement for the year then ended, a summary of significant accounting policies and other explanatory notes, as set out on pages 5 to 31.

### *Directors' Responsibility for the Financial Statements*

The company's directors are responsible for the preparation and fair presentation of these financial statements in accordance with South African Statements of Generally Accepted Accounting Practice, and in the manner required by the Companies Act of South Africa. This responsibility includes: designing, implementing and maintaining internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

### *Auditor's Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal controls. An audit also includes evaluating the appropriateness of accounting principles used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall financial statement presentation.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

 

**INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF THE SMALL ENTERPRISE FOUNDATION (AN ASSOCIATION INCORPORATED UNDER SECTION 21 OF THE COMPANIES ACT) (continued)**

***Opinion***

In our opinion, these annual financial statements fairly present, in all material respects, the financial position of the company at 30 June 2008, and the results of its operations and cash flow information for the year then ended in accordance with South African Statements of Generally Accepted Accounting Practice, and in the manner required by the Companies Act in South Africa.

Deloitte & Touche

**Deloitte & Touche**

Per: Lito Nunes
Partner
6 November 2008

**THE SMALL ENTERPRISE FOUNDATION**
**(An association incorporated under Section 21 of the Companies Act)**
**REPORT OF THE DIRECTORS**
**30 June 2008**

The directors have pleasure in presenting their report on the organisation for the year ended 30 June 2008.

**Business review**

The principal business of the organisation is to motivate the poor to take up income generating activities and to extend credit to micro entrepreneurs to enable them to realise their potential and thereby generate income and employment. The company is registered with the National Credit Regulator.

The Small Enterprise Foundation has, since inception, granted 468 705 (2007: 364 827) loans to the value of R626 million (2007: R467 million). In the current year the organisation granted 103 878 (2007: 80 201) loans to the value of R159 million (2007: R137 million).

The Small Enterprise Foundation is incorporated in the Republic of South Africa as a non–profit company with the aim of providing micro finance to the poor and very poor. No holding company or parent company has any interest in the organisation and all its operations are conducted in the Limpopo, Mpumalanga and Eastern Cape provinces of South Africa. The head office is situated in Tzaneen in the Limpopo province.

**Operating results**

Results for the year ended 30 June 2008 are set out on pages 7 to 31 of the financial statements. The directors are pleased to report a 42% increase in loans and advances as well as a 35% increase in loan interest income. At the same time expenses, excluding finance costs and impairment of advances, increased by 31% due to five new branches being established.

**Loan loss reserves**

In cases where borrowers experience death amongst their members, the company will decrease the borrower's repayment and write-off the amount owed by the member. Such write-offs are classified as provisions for claims not yet incurred. During the year under review an amount of R 492 615 (2007: 337 368) was provided for.

A debt is declared irrecoverable once it is 84 days in arrears. An amount of R629 850 (2007: R371 707) was written off during the year under review.

We believe that this excellent performance will be maintained due to the nature of the lending procedures employed, the diligence of the field staff and the commitment of clients.

The only instance where the organisation allows the renegotiation of delinquent loans is where clients are able to provide medical evidence of long-term illness. Such amounts are not written off, and the respective clients are urged to continue with loan repayments when their condition improves. The accumulative amount renegotiated in this way since inception and still outstanding at year-end was R320 422 (2007: 339 411).

A loan loss reserve is created for all loans in arrears more than 1 day up to 84 days. The reserve is calculated based on historical information of outstanding loans for the previous 12 months and is calculated for the following categories:

**Loan loss reserves (continued)**

| | |
|---|---|
| 1 - 30 days in arrears | – MCP 9.62% and TCP 18.48% of the outstanding group loan amount is provided |
| 31 - 60 days in arrears | – MCP 50.04% and TCP 38.67% of the outstanding group loan amount is provided |
| 61 - 84 days in arrears | – MCP 51.61% and TCP 65.97% of the outstanding group loan amount is provided |
| 85 days and older | – The group loan is written off as a bad debt |

**Directors and secretary**

The directors of the company for the year under review, and at the date of this report were as follows:

Ms Marie Albertina Kirsten (Non-executive)
Mr Mutle Constantine Mogase (Non-executive)
Mr John Robert de Wit (Managing Director)
Mr Matome Patrick Malatji (Chairperson)
Mr Sanjay Doshi (Non-executive)
Ms Sizeka Monica Rensburg (Non-executive)
Ms Olivia Henwood (Non-executive)
Mr Modise Motloba (Non- executive)

Secretary and Public Officer - Nexia Levitt Kirson and John Robert de Wit

Auditors - Deloitte & Touche

**Business address and Domicile**
42 Boundary Street
Tzaneen
South Africa
0850

**Postal address**
P O Box 212
Tzaneen
South Africa
0850

| | |
|---|---|
| Web site: | www.sef.co.za |
| Email: | info@sef.co.za |
| Telephone: | +27 15 307 5837 |
| Fax: | +27 15 307 2977 |

**Post balance sheet events**

No events have occurred between the financial year-end and the date of this report that are expected to have a material adverse effect on either the operations of the company or its financial position.

THE SMALL ENTERPRISE FOUNDATION
(An association incorporated under Section 21 of the Companies Act)
BALANCE SHEET
at 30 June 2008

| | Notes | 2008<br>R | 2007<br>R |
|---|---|---|---|
| **ASSETS** | | | |
| **Non-current assets** | | | |
| Property and equipment | 2 | 2 204 387 | 1 976 981 |
| **Current assets** | | | |
| Loans and advances | 3 | 70 806 191 | 49 918 401 |
| Other receivables | 4 | 796 971 | 740 946 |
| Cash and short term funds | | 11 852 437 | 4 799 466 |
| **Total current assets** | | 83 455 599 | 55 458 813 |
| **TOTAL ASSETS** | | 85 659 986 | 57 435 794 |
| **FUNDS AND LIABILITIES** | | | |
| **Funds** | | | |
| General capital reserve | 5 | 8 367 670 | 6 246 429 |
| Development reserve | 6 | 6 654 459 | 7 085 882 |
| Educational reserve | 7 | 20 188 | 20 188 |
| Retained earnings | | 10 149 210 | 10 603 083 |
| **Total funds** | | 25 191 527 | 23 955 582 |
| **Non-current liabilities** | | | |
| Long term loans | 8 | 34 219 787 | 20 347 544 |
| **Current liabilities** | | | |
| Short term loans | 9 | 17 644 328 | 10 197 325 |
| Trade and other payables | | 1 846 616 | 930 105 |
| Accruals | 10 | 3 075 039 | 2 005 238 |
| Unutilised grants | 15 | 3 682 689 | - |
| **Total current liabilities** | | 26 248 672 | 13 132 668 |
| **TOTAL FUNDS AND LIABILITIES** | | 85 659 986 | 57 435 794 |

**THE SMALL ENTERPRISE FOUNDATION**
**(An association incorporated under Section 21 of the Companies Act)**
**INCOME STATEMENT**
**for the year ended 30 June 2008**

| | Notes | 2008<br>R | 2007<br>R |
|---|---|---|---|
| Revenue | 11 | 38 409 765 | 28 842 764 |
| Finance costs | 12 | (5 258 490) | (3 102 256) |
| Impairment of advances | 13 | (891 253) | (512 945) |
| Provision for impairment of advances | 3 | (153 082) | (316 075) |
| **Margin on lending activities** | | 32 106 940 | 24 911 488 |
| Operating expenses | | (22 795 897) | (15 793 632) |
| **Operating income** | | 9 311 043 | 9 117 856 |
| Sundry income | | 66 887 | 53 620 |
| Loss on disposal of property and equipment | | 1 077 | (5 132) |
| **Income before head office expenses** | | 9 379 007 | 9 166 344 |
| Head office expenses | 20 | (11 163 661) | (10 078 275) |
| **Loss before grants** | 14 | (1 784 654) | (795 399) |
| Operational grants utilised to cover expenses | 15 | 1 330 780 | 1 707 330 |
| Capital grants received | 15 | 2 121 241 | 4 670 881 |
| Other grants (refunded) / received | | (431 422) | 35 176 |
| **Net income for the year** | | 1 235 945 | 5 501 456 |
| Capital grants received* | 15 | (1 689 819) | (4 670 881) |
| (Loss)/income for the period available for operations | | (453 874) | 830 575 |

*All capital grants were received with the express condition that the funds be used for lending to customers and are therefore considered being capital in nature. The capital grants are therefore not available in the day to day operations of the entity.

**THE SMALL ENTERPRISE FOUNDATION**
**(An association incorporated under Section 21 of the Companies Act)**
**STATEMENT OF CHANGES IN EQUITY**
**For the year ended 30 June 2008**

| | General capital reserve R | Development reserve R | Educational reserve R | Retained earnings R | Total R |
|---|---|---|---|---|---|
| **Balance as at 01 Jul 2007** | **1 575 548** | **7 050 706** | **20 188** | **9 807 684** | **18 454 126** |
| Net income for the year | - | - | - | 5 501 456 | 5 501 456 |
| Grants transferred from accumulated income* | 4 670 881 | 35 176 | - | (4 706 057) | - |
| **Balance as at 30 June 2007** | **6 246 429** | **7 085 882** | **20 188** | **10 603 083** | **23 955 582** |
| Net income for the year | | | | 1 235 945 | 1 235 945 |
| Grants transferred from accumulated income* | 2 121 241 | (431 423) | - | (1 689 818) | - |
| **Balance as at 30 June 2008** | **8 367 670** | **6 654 459** | **20 188** | **10 149 210** | **25 191 527** |

*During the current year all capital grants received were recognised as income. The capital grants were then transferred to the General capital reserve as these grants were specifically received from donors to be used as loan capital. Prior year comparatives have been adjusted accordingly.

**THE SMALL ENTERPRISE FOUNDATION**
**(An association incorporated under Section 21 of the Companies Act)**
**CASH FLOW STATEMENT**
**for the year ended 30 June 2008**

| | Notes | 2008<br>R | 2007<br>R |
|---|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | | |
| Cash utilised by operations | A | (53 426 186) | (35 508 604) |
| Other interest and fees received | | 38 409 765 | 26 742 545 |
| Interest paid | | (5 258 490) | (3 102 256) |
| Net cash used in operating activities | | (20 274 911) | (11 868 315) |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | | |
| Additions to property and equipment | | (709 641) | (481 700) |
| Proceeds on disposal of property and equipment | | 15 300 | 5 351 |
| Net cash used in investing activities | | (694 341) | (476 349) |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | | |
| Increase in long term loans | | 13 872 243 | 1 674 551 |
| Increase in short terms loans | | 7 447 003 | 2 173 043 |
| Grants received | | 7 134 399 | 6 413 387 |
| Grants refunded | | (431 422) | - |
| Net cash generated by financing activities | | 28 022 223 | 10 260 981 |
| **NET (DECREASE)/INCREASE IN CASH AND CASH EQUIVALENTS** | | 7 052 971 | (2 083 683) |
| Cash and cash equivalents at beginning of the financial year | | 4 799 466 | 6 883 149 |
| **CASH AND CASH EQUIVALENTS AT END OF FINANCIAL YEAR** | B | 11 852 437 | 4 799 466 |

**THE SMALL ENTERPRISE FOUNDATION**
**(An association incorporated under Section 21 of the Companies Act)**
**NOTES TO THE CASH FLOW STATEMENT**
**for the year ended 30 June 2008**

| | 2008 R | 2007 R |
|---|---|---|
| **A. CASH UTILISED BY OPERATIONS** | | |
| Loss before grants | (1 784 654) | (911 931) |
| Adjusted for: | | |
| - Other interest and fees received | (38 409 765) | (26 742 545) |
| - Finance costs | 5 258 490 | 3 102 256 |
| - Depreciation | 468 323 | 346 761 |
| - Loss on disposal of property and equipment | (1 077) | 5 132 |
| - Provision for impairment on loans and advances | 153 082 | 316 084 |
| Operating loss / (profit) before working capital changes | (34 315 601) | (23 884 243) |
| - Adjusted for changes in working capital: | | |
| - Increase in other receivables | (56 025) | (154 676) |
| - Increase in trade and other payables | 916 511 | 483 090 |
| - Increase in other accruals | 1 069 801 | 346 570 |
| - Increase in loans and advances | (21 040 872) | (12 299 345) |
| Cash utilised by operations | (53 426 186) | (35 508 604) |

**B. CASH AND CASH EQUIVALENTS**

Cash and cash equivalents consist of

| | 2008 R | 2007 R |
|---|---|---|
| Balances with banks | 11 852 437 | 4 799 465 |

**1. Accounting policies**

The annual financial statements have been prepared in accordance with South African Statements of Generally Accepted Accounting Practice. The annual financial statements are prepared on the accrual basis, except for certain financial instruments which are fair valued. The following principal accounting policies have been incorporated, and are consistent with prior years in all material respects:

**1.1 Interest earned on advances**

Interest earned on advances is recognised using the effective interest rate method over the term of the loans. No interest rate risk exists on advances as interest is not linked to market changes but remains constant even when Repo rate changes are made.

**1.2 Other interest received**

Other interest received is accrued on a daily basis using the effective interest rate method.

**1.3 Initiation and service fees**

Initiation fees are recognised as income on the date that loans and advances are disbursed.
Service fees are recognised as income on a monthly basis as they are received.

**1.4 Grants received**

***Operational grants received***

These are grants which are specifically designated to be utilised for operational expenses, where the expenses to which they relate have actually been incurred and charged to income in the same period, and where all the contractual conditions for payment of the grant amount have been met.

***Grants for loan capital***

Grants designated for loan capital are recognised in the income statement when received. These grants are then transferred to the General capital reserve.

**1.5 Property and equipment**

Property and equipment are stated at historical cost and are depreciated using the straight-line method over the estimated useful lives of the assets. The following rates of depreciation have been used:

| | |
|---|---|
| Furniture and fittings | 5 years |
| Office equipment | 5 years |
| Computer equipment | 3 years |
| Motor vehicles | 4 years |
| Buildings | 40 years |

Land is not depreciated.

The carrying amounts of property and equipment are written down to their estimated recoverable amounts, where the estimated recoverable amount is lower than the carrying value.

## 1. Accounting policies (continued)

### 1.6 Financial assets and financial liabilities

Financial assets and financial liabilities are recognised on balance sheet when the company becomes a party to the contractual provisions of the instrument.

All financial instruments are initially measured at cost, which is the fair value of the consideration given or received in exchange for these instruments, less any impairment.

At 30 June 2008, the company's principal financial assets included cash and short term funds, advances and accrued interest, and trade and other receivables. Advances and accrued interest are measured at amortised cost. Cash, short term funds and trade and other receivables are stated at their nominal values which approximate fair values. All financial assets are reduced by appropriate allowances for estimated irrecoverable amounts where applicable.

At 30 June 2008, the company's principal financial liabilities included trade and other payables, short and long term loans. Short and long term loans are measured at amortised cost. Trade and other payables are stated at their nominal value which approximates fair value.

### 1.7 Retirement benefits

Contributions to retirement benefit funds are charged to the income statement when they are incurred.

### 1.8 Provisions

Provisions for staff related expenses such as outstanding leave days not taken at year end and 13$^{th}$ cheques are made at total cost to the organisation as at 30 June 2008.

A provision for incentive bonus based on the performance of the organisation as well as on individual basis was created as at 30 June 2008.

Provision for audit fees and workmen's compensation are based on estimates as at 30 June 2008.

### 1.9 Adoption of new and revised South African Statements of General Accepted Accounting Practice and interpretations effective in the current period

In the current year, the Company has adopted AC 144 Financial Instruments: Disclosure, which is effective for annual reporting periods beginning on or after 1 January 2007, and the consequential amendments to AC 101 Presentation of Financial Statements.

The impact of the adoption of AC 144 and the changes to AC 101 has been to expand the disclosures provided in these financial statements regarding the Company's financial instruments in such a manner that it provides useful information to the users of the financial statements.

The adoption of these Interpretations has not led to any changes in the Company's accounting policies.

## 2. Property and equipment

| | Land & buildings<br>R | Furniture & fittings<br>R | Office equipment<br>R | Computer equipment<br>R | Motor vehicles<br>R | Total<br>R |
|---|---|---|---|---|---|---|
| **2008** | | | | | | |
| **Cost** | | | | | | |
| At beginning of year | 1 072 320 | 530 620 | 818 968 | 809 195 | 13 611 | 3 244 714 |
| Additions | 15 838 | 133 252 | 216 046 | 344 505 | - | 709 641 |
| Disposals and scrapings | - | - | (37 996) | (10 049) | | (48 045) |
| At end of year | 1 088 158 | 663 872 | 997 018 | 1 143 651 | 13 611 | 3 906 310 |
| **Accumulated depreciation** | | | | | | |
| At beginning of year | 65 413 | 279 044 | 341 907 | 576 086 | 5 282 | 1 267 732 |
| Depreciation | 23 791 | 81 143 | 160 510 | 199 476 | 3 403 | 468 323 |
| Disposals and scrapings | - | - | (26 597) | (7 535) | - | (34 132) |
| At end of year | 89 204 | 360 187 | 475 820 | 768 026 | 8 685 | 1 701 923 |
| **Carrying value** | 998 954 | 303 685 | 521 198 | 375 625 | 4 926 | 2 204 387 |

## 2. Property and equipment

| | Land & buildings R | Furniture & fittings R | Office equipment R | Computer equipment R | Motor vehicles R | Total R |
|---|---|---|---|---|---|---|
| **2007** | | | | | | |
| **Cost** | | | | | | |
| At beginning of year | 1 072 320 | 382 556 | 622 535 | 693 463 | 65 543 | 2 836 417 |
| Additions | - | 148 464 | 196 433 | 130 135 | 6 668 | 481 700 |
| Disposals and scrapings | - | (400) | - | (14 403) | (58 600) | (73 403) |
| At end of year | 1 072 320 | 530 620 | 818 968 | 809 195 | 13 611 | 3 244 714 |
| **Accumulated depreciation** | | | | | | |
| At beginning of year | 41 856 | 226 065 | 227 574 | 438 789 | 49 608 | 983 892 |
| Depreciation | 23 558 | 53 379 | 114 333 | 151 109 | 4 382 | 346 761 |
| Disposals and scrapings | - | (400) | | (13 812) | (48 708) | (62 920) |
| At end of year | 65 414 | 279 044 | 341 907 | 576 086 | 5 282 | 1 267 733 |
| **Carrying value** | 1 006 906 | 251 576 | 477 061 | 233 109 | 8 329 | 1 976 981 |

| | 2008<br>R | 2007<br>R |
|---|---|---|
| **3. Loans and advances** | | |
| Gross advances | 70 032 124 | 49 108 054 |
| Accrued interest on advances | 1 699 978 | 1 583 176 |
| Provision for bad debts | (433 296) | (435 461) |
| IBNR provision (death write offs) | (492 615) | (337 368) |
| | 70 806 191 | 49 918 401 |
| Movement in impairment provision: | | |
| Balance at beginning of year | 772 829 | 456 754 |
| Current year movement in provision | 153 082 | 316 075 |
| Balance at end of year | 925 911 | 772 829 |

Advances that have been funded out of loans received from the following institutions; Hivos Triodos Bank, Khula Enterprise Finance, Umsobomvu Youth Fund, Tembeka Social Investment Co, Teba Bank ABSA bank and Oiko Credit, have been ceded to them as security. See note 8.

The entity is operational with its Head office in Tzaneen and operational in the surrounding areas in the Limpopo Province, Mpumalanga Province and the Eastern Cape Province, South Africa. Individual loans do not exceed R12 000.

Effective interest rates, based on a declining balance, are charged at a rate of 40.9% and an initiation and service fee are also charged. Rates do not fluctuate with changes to Repo rate changes and no provision is calculated for rate changes.

Due to the fact that the interest rate on advances does not fluctuate with changes in the Repo rate and due to the fact that the advances have a short time to maturity, the carrying amounts approximate fair value.

Amounts written off during the year were expensed directly to the income statement.

| | 2008 R | 2007 R |
|---|---|---|

## 3. Loans and advances (continued)

A total amount of R515 459 (2007: R435 461) of advances was in arrears at the financial year end. An analysis of the arrears for the current year is presented below.

| | 2008 R | 2007 R |
|---|---|---|
| Rescheduled loans | 320 422 | 339 411 |
| 1 – 30 days | 89 619 | 23 777 |
| 31 – 60 days | 30 802 | 40 671 |
| 61 – 84 days | 74 617 | 31 602 |
| | 515 460 | 435 461 |

## 4. Other receivables

Included in accounts receivable is an amount for staff debtors of R55 424 (2007: R56 428). This constitutes small loans generally available to all first time vehicle users, salary advances given to staff, as well as study loans. These loans carry a market related interest rate. There were no arrears in respect of staff loans (2007: R nil) at the financial year end. Loans are normally repaid over a period of two years.

Due to the fact that the other receivables have a short time to maturity, the carrying amount approximates fair value.

| | 2008 R | 2007 R |
|---|---|---|
| Other receivables and staff debtors | 796 971 | 740 946 |

| | 2008<br>R | 2007<br>R |
|---|---|---|

## 5. General capital reserve

The general capital reserve consists of grants received from donors other than USAID (see note 6). Such grants are, for most part, non-recurring grants from a variety of organisations wanting to express their interest in, and support of, the work performed by The Small Enterprise Foundation. During the year grants were received from the Swedish International Development Agency (SIDA), the Thusano Trust, Old Mutual, The Threshold Foundation and The International Alliance of Women. All grants have been designated by the donors concerned as loan capital to be utilised for future disbursements of loans to clients.

| | 2008 R | 2007 R |
|---|---|---|
| Balance at beginning of year | 6 246 429 | 1 575 548 |
| Movement in general capital reserve | 2 121 241 | 4 670 881 |
| Balance at end of year | 8 367 670 | 6 246 429 |

## 6. Development reserve

The development reserve comprises mainly of grants received from USAID.

| | 2008 R | 2007 R |
|---|---|---|
| Balance at beginning of year | 7 085 882 | 7 050 706 |
| Movement in development reserve | - | 35 176 |
| Unutilised portion of Ford grant refunded | (431 423) | - |
| Balance at end of year | 6 654 459 | 7 085 882 |

## 7. Educational reserve

The educational reserve consists of small individual grants. The donors have requested the funds be used to disburse educational loans to existing members of the organisation under an educational loan programme introduced in 1998. As from July 2007 these loans were discontinued.

| | 2008 R | 2007 R |
|---|---|---|
| Balance at end of year | 20 188 | 20 188 |

| | **2008** | **2007** |
|---|---|---|
| | **R** | **R** |

## 8. Long term loans

**Hivos Triodos Bank**

Hivos Triodos Bank of the Netherlands has approved three loan facilities totalling R14.25 million.

The first facility of R7 million is redeemable in South African Rand in one instalment on 1 July 2009. No grace period is specified in the contract. Interest is paid at the prime rate with a minimum of 12% and a maximum of 18% per annum, and is payable six monthly in arrears. Loan capital of R7 million is outstanding at year end.

The agreement for the second facility of R4 million was signed in 2007 and the first R2 million was received in June 2007. The loan is redeemable in South African Rand in one installment of R2 million on 1 July 2010 and a final installment of R2 million on 1 July 2011. Interest payable on this loan facility is paid at prime with a minimum of 12% and a maximum of 18% per annum and is payable 6 monthly in arrears. Loan capital of R4 million is outstanding at year end.

The agreement for the third facility of R3.25 million was signed in 2008 and the amount of R3.25 million was received in June 2008. The loan is redeemable in South African Rand in one instalment of R3.25 million on 1 July 2012. Interest payable on this loan facility is paid at prime with a minimum of 12% and a maximum of 18% per annum and is payable 6 monthly in arrears. Loan capital of R3.25 million is outstanding at year end.

The purpose of the Hivos Triodos loans is to increase the working capital for the purposes of on lending to micro entrepreneurs. The loans are secured by a first cession of the advances book to micro entrepreneurs financed by this loan facility.

| | 2008 R | 2007 R |
|---|---|---|
| Balance at beginning of year | 9 000 000 | 6 000 000 |
| Movement | 6 051 402 | 5 011 397 |
| Short term portion transferred to current liabilities | (726 402) | (2 011 397) |
| Balance at end of the year | 14 325 000 | 9 000 000 |

| | 2008<br>R | 2007<br>R |
|---|---|---|

## 8. Long term loans (continued)

**Khula Enterprise Finance Limited**

In the 2004 year, the company entered into two additional business loan agreements with Khula Enterprise Finance Limited. The maximum loan facilities under these agreements are R2.1 million and R9.6 million. Interest on loan drawdowns is calculated at prime minus 3%.

Drawdowns in respect of the R2.1 million facility are repayable over 60 months from the date of the specific drawdown. Loan capital of R825 503 is still outstanding at year end.

The repayment period in respect of the R9.6 million facility is set at a maximum of 60 months from initial drawdown. Loan capital of R6 054 467 is still outstanding at year end.

These loans are secured by a cession of the Khula end user loans.

| | 2008<br>R | 2007<br>R |
|---|---|---|
| Balance at beginning of year | 6 060 110 | 7 205 999 |
| Movement | 819 811 | 1 996 033 |
| Short term portion transferred to current liabilities | (3 131 563) | (3 141 922) |
| Balance at end of year | 3 748 358 | 6 060 110 |

## 8. Long term loans (continued)

**Tembeka Social Investment Company Limited**

In November 2003, the company entered into a loan agreement with Tembeka Social Investment Company Limited. The loan facility under this agreement is R1 million. Interest is calculated at 13% and is payable quarterly in arrears. Loan capital of R250 000 is still outstanding at year end.

An additional loan of R2 million was entered into in April 2007. The loan is repayable in 8 instalments of R250 000 starting in month 18 and thereinafter every 6 months with a final payment in April 2010. Interest is payable at a flat rate of 13% per annum and is payable quarterly in arrears. Loan capital of R 1 million is still outstanding at year end.

| | 2008<br>R | 2007<br>R |
|---|---|---|
| Balance at beginning of year | 1 499 997 | 1 000 000 |
| Movement | 801 559 | 784 723 |
| Short term portion transferred to current liabilities | (1 051 556) | (284 726) |
| Balance at end of year | 1 250 000 | 1 499 997 |

| | 2008 R | 2007 R |
|---|---|---|

## 8. Long term loans (continued)

**Teba Bank and Tembani International Guarantee Fund**

In February 2004, the company entered into a loan agreement with Tembani International Guarantee Fund and Teba Bank. The maximum loan facility under this agreement is R3 000 000. Interest is calculated at prime less 1% and is payable monthly. The loan is repayable on a monthly basis. Maturity date is 25 February 2009. An addendum was signed in February 2006 to increase the facility with R2 million to R5 million. The facility operates on a revolving fund basis.

This loan is secured by a cession of a fixed deposit of R500 000 held at Standard Bank and a letter of credit for R3.5 million by City Bank New York on behalf of Tembani International Guarantee Fund.

The loan is further secured by a cession of end user loans.

| | 2008 R | 2007 R |
|---|---|---|
| Balance at beginning of year | - | 1 927 018 |
| Movement | 5 031 487 | 1 546 660 |
| Short term portion transferred to current liabilities | (5 031 487) | (380 358) |
| Balance at end of year | - | - |

| | 2008 R | 2007 R |
|---|---|---|

**8. Long term loans (continued)**

**Umsobomvu Youth Fund**

In December 2005 the company entered into a loan agreement with Umsobomvu Youth Fund. The maximum loan facility under this agreement is R5.4 million. The interest is calculated at prime less 4% and is payable in 10 equal quarterly payments starting 90 days after the last drawdown. Final payment of the loan facility will be in September 2008.

| | 2008 R | 2007 R |
|---|---|---|
| Balance at beginning of year | 971 380 | 2 539 977 |
| Movement | 202 200 | 873 736 |
| Short term portion transferred to current liabilities | (1 173 580) | (2 442 333) |
| | - | 971 380 |

**Oiko credit**

In March 2007 the company entered into a loan agreement with Oiko credit. The maximum loan facility under this loan is R10.1 million. The interest is calculated at repo rate +3.75% with a minimum interest rate of 10.75% and is payable in 3 monthly instalments. The loan capital is payable in 16 equal half yearly payments starting 6 months after the initial drawdown and a final payment in March 2015. The loan is repayable in South African Rand.

| | 2008 R | 2007 R |
|---|---|---|
| Balance at beginning of year | 2 816 057 | - |
| Movement | 6 089 899 | 4 123 758 |
| Short term portion transferred to current liabilities | (1 330 956) | (1 307 702) |
| | 7 575 000 | 2 816 057 |

**Swedfund**

In October 2007 the company entered into a loan agreement with Swedfund. The maximum loan facility under this loan is R10 million. The interest is calculated at JIBAR (Johannesburg Inter-bank Acceptance Rate) plus 3.8% for a six month period calculated two banking days prior to the first day of the relevant interest period. The JIBAR rate for the period April 2008 to 31 August 2008 was 11.713%. The loan capital is payable in 7 equal half yearly payments starting 18 months after the initial drawdown and a final payment in March 2012. R8 million was drawn up to the end of June 2008. The loan is repayable in South African Rand.

| | 2008 R | 2007 R |
|---|---|---|

**8. Long term loans (continued)**

**Swedfund (continued)**

| | 2008 R | 2007 R |
|---|---|---|
| Balance at beginning of year | - | - |
| Movement | 8 262 501 | - |
| Short term portion transferred to current liabilities | (1 691 072) | - |
| Balance at Year end | 6 571 429 | - |

**Genesis steel**

In February 2008 the company received a loan from Genesis steel to the value of R465 000. There are no repayment terms and no interest is payable.

| | 2008 R | 2007 R |
|---|---|---|
| Balance at beginning of year | - | - |
| Movement | 465 000 | - |
| Short term portion transferred to current liabilities | - | - |
| Balance at Year end | 465 000 | - |

**Sentinel steel**

In February 2008 the company received a loan from Sentinel steel to the value of R285 000. There are no repayment terms and no interest is payable.

| | 2008 R | 2007 R |
|---|---|---|
| Balance at beginning of year | - | - |
| Movement | 285 000 | - |
| Short term portion transferred to current liabilities | - | - |
| Balance at Year end | 285 000 | - |
| Total long term loans | 34 219 787 | 20 347 544 |

Long term loans are carried at amortised cost. Due to the fact that the loans materially have a variable interest rate that fluctuates with changes in the Repo rate, the carrying amount approximates fair value.

| | 2008 R | 2007 R |
|---|---|---|
| **9. Short term loans** | | |
| In the 2006 financial year the company entered into a loan agreement with Margaretha Vintges. The loan amount advanced was R100 000. Interest is calculated at prime less 4%. The full amount outstanding is repayable on short-term notice by the lender. | | |
| Loan from Margaretha Vintages | 132 056 | 119 296 |
| In the previous year the company entered into a loan agreement with GJ O Marincowitz. The loan amount advanced was R500 000. Interest is calculated at 5%. The full amount outstanding is repayable on short-term notice by the lender. | | |
| Loan from GJ O Marincowitz | 535 707 | 509 592 |
| Current portion of Hivos Triodos Bank loan | 726 402 | 2 011 397 |
| Current portion of Khula Enterprise Finance Limited Business loan | 3 131 563 | 3 141 922 |
| Current portion of Tembeka Social Investment Company loan | 1 051 556 | 284 726 |
| Current portion of Teba Bank loan and Tembani International Guarantee Fund | 5 031 487 | 380 358 |
| Current portion of Umsobomvu Youth Fund Loan | 1 173 580 | 2 442 333 |
| Current portion of Oiko Credit | 1 330 956 | 1 307 701 |
| Current portion Swedfund | 1 691 072 | - |
| In April 2008, the company entered into a loan agreement with Tembani International Guarantee Fund and Absa Bank. The maximum loan facility under this agreement is R5 000 000. Interest is calculated at prime less 1.5% and is payable monthly. Maturity date is November 2012. The facility operates on a revolving fund basis. This loan is secured by a cession of a fixed deposit of R500 000 held at ABSA Bank and a letter of credit for R3.5 million by City Bank New York on behalf of Tembani International Guarantee Fund. | | |
| The loan is further secured by a cession of end user loans. ABSA Bank and Tembani International Guarantee Fund revolving facility | 2 839 949 | - |
| | 17 644 328 | 10 197 325 |

| | 2008 R | 2007 R |
|---|---|---|
| **10. Accruals** | | |
| Accrual for accumulated leave | 969 076 | 621 514 |
| Accrual for annual bonus | 700 053 | 540 765 |
| Accrual for incentive bonus | 665 295 | 300 000 |
| Accrual for audit fee | 448 990 | 425 000 |
| Accrual other | 291 625 | 117 959 |
| | 3 075 039 | 2 005 238 |
| **11. Revenue** | | |
| Interest received on advances | 19 416 982 | 26 156 610 |
| Interest received on cash balances | 944 685 | 585 935 |
| Initiation fees | 17 586 741 | 2 100 160 |
| Service fees | 461 357 | 59 |
| | 38 409 765 | 28 842 764 |
| **12. Finance costs** | | |
| Finance costs in respect of loans | 5 182 680 | 3 039 837 |
| Administration cost on borrowings | 75 810 | 62 419 |
| | 5 258 490 | 3 102 256 |
| **13. Impairment of advances** | | |
| Bad debts written off | 629 850 | 371 707 |
| Bad debts recovered | (75 756) | (105 674) |
| Death write-offs | 337 159 | 246 912 |
| | 891 253 | 512 945 |

## 14. Loss before grants

The loss before grants is arrived at after taking the following into account.

| | 2008 R | 2007 R |
|---|---|---|
| Staff costs | 22 551 361 | 17 809 039 |
| Auditor's remuneration | | |
| - Statutory audit – current year | 383 990 | 370 000 |
| - Statutory audit – prior year under provision | 26 880 | 30 926 |
| - Audit expenses | 65 000 | 55 000 |
| | 475 870 | 455 926 |
| Depreciation | 468 323 | 346 761 |
| Operating leases | | |
| - Rentals motor vehicles | 803 483 | 663 475 |
| - Buildings | 422 686 | 231 601 |
| | 1 226 169 | 895 076 |
| Death write offs | 337 159 | 246 912 |
| Legal fees | 15 492 | 93 329 |
| Directors' emoluments | | |
| - For managerial duties (paid by the company) | 751 576 | 741 512 |
| - Expenses relating to managerial duties | 73 170 | 39 090 |
| | 824 746 | 780 602 |

| | 2008 | 2007 |
|---|---|---|
| | R | R |
| **15. Grants received** | | |
| **Operational grants received – gross amount** | | |
| H.S.D.U | - | 151 217 |
| Ford Foundation for a micro-insurance product pilot | - | 666 939 |
| Old Mutual Masisizane Fund | 2 900 000 | - |
| Hivos Triodos | 445 618 | 924 350 |
| Transfer of un-utilised grants to development reserve | | |
| - Ford Foundation | - | (35 176) |
| Total operational grants received | 3 345 618 | 1 707 330 |
| Unitilised portion of operational grants received | | |
| - Old Mutual Masisizane fund | (1 884 755) | - |
| - Hivos | (130 083) | - |
| | 1 330 780 | 1 707 330 |
| **Capital grants received – gross amount** | | |
| Sida | 1 017 059 | 3 920 881 |
| Thusano Trust | 210 000 | 750 000 |
| Old Mutual Masisizane Fund | 500 000 | - |
| Hivos | 1 782 474 | - |
| Threshold foundation | 216 660 | - |
| The International Alliance of Women | 62 588 | - |
| Total capital grants received | 3 788 781 | 4 670 881 |
| Unitilised portion of capital grants received | | |
| - Hivos | (1 667 540) | - |
| | 2 121 241 | 4 670 881 |
| Total grants received | 3 452 021 | 4 670 881 |

All capital grants were received with the express condition that the funds be used for lending to customers and are therefore considered being capital in nature. The capital portion of the HIVOS grant is intended for the purchase of a new computerised loan administration management system. This is considered to be an intangible asset.

No donations or subsidies in kind were received during the year under review (2007: R Nil).

| | 2008 R | 2007 R |
|---|---|---|

## 16. Operating leases

The company has various operating leases entered into with Stannic for the rental of motor vehicles. The minimum lease payments are detailed below:

| | 2008 R | 2007 R |
|---|---|---|
| Amounts payable within 1 year | 830 887 | 623 318 |
| Amounts payable within 2 – 5 years | 1 297 589 | 945 813 |
| Amounts payable greater the 5 years | - | - |
| Total | 2 128 476 | 1 569 131 |

## 17. Taxation

No provision has been made for taxation as the organisation is incorporated under Section 21 of the Companies Act and is therefore exempt from taxation.

## 18. Retirement benefits

All permanent employees of the company are members of the Old Mutual Orion Provident Fund. The provident fund is in the nature of a defined contribution plan, where the retirement benefits are determined with reference to the employer and employees' contributions to the fund. In 2008, the employer contributed R2 453 722 (2007: 1 971 411) towards the provident fund and group life premiums. Current contributions to the provident fund are charged against income as incurred.

**19. Risk management**

**Credit risk**

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation, and cause the other party to incur a financial loss. The company mitigates this risk by employing a comprehensive framework of polices, procedures and limits to ensure a process of risk assessment, quantification and monitoring.

**Liquidity risk**

Liquidity risk, also referred to as funding risk, is the risk that an enterprise will encounter difficulty in raising funds to meet future financial commitments. As the company is still dependant on grants in order to continue as a going concern, the management of this risk is critical to the company's survival. The company does however have loan facilities available should funds be required to meet commitments.

**Cash flow risk**

Cash flow risk is the risk that future cash flows associated with a monetary financial instrument will fluctuate in amount. The company mitigates this risk by setting fixed repayment terms for all loans and advances.

**Interest rate risk**

Interest rate risk is the risk that interest rates will fluctuate in future. The company adopts a policy of ensuring that its borrowings are at market related rates to address its interest rate risk. Interest earned on advances , at an effective rate of 40.9%, is fixed.

**Capital risk**

The company manages its capital to ensure that it will be able to continue as a going concern while maximising its social returns through the optimisation of the debt and equity balance. The Company's strategy remains unchanged from 2007.

The capital structure of the company consists of debt, which includes borrowings, cash and cash equivalents, reserves and retained earnings respectively.

## 20. Total head office cost

The total cost for head office activities amounted to R11 163 661.
This includes the following activities or departments:

| | 2008 R | 2007 R |
|---|---|---|
| Training department | 1 405 835 | 1 563 370 |
| Human Resources department | 1 532 319 | 920 208 |
| Quality Assurance department | 872 875 | 851 883 |
| Loans administration | 1 050 897 | 876 849 |
| Research and development including micro-insurance trial | 385 240 | 924 117 |
| Senior Management Finance and secretarial | 5 916 495 | 4 941 848 |
| | 11 163 661 | 10 078 275 |

## 21. Encumbered assets and contingent liabilities

The following securities have been ceded by the company:

The Standard Bank fixed deposit account has been ceded as security to Teba Bank for the loan held with Teba Bank to the value of R500 000.

The Standard Bank money market account has been ceded to Stannic as collateral of the leased vehicles to the value of R475 319.

The Standard Bank Bond Account has a second mortgage registered with Standard Bank to the value of R1 700 000.

ABSA bank fixed deposit account has been ceded as security to Absa bank for the loan held with Absa bank to the value of R500 000.