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Title

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Permalink

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Journal

Berkeley Planning Journal, 7(1)

Author

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Publication Date

1992

DOI

10.5070/BP37113109

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MICROCREDIT IN THE U.S.: AN ALTERNATIVE ECONOMIC SURVIVAL STRATEGY

Lisa J. Servon

Introduction

Since the introduction of the first U.S. microenterprise¹ program in 1983, more than 100 have been started. They exist in both rural and urban settings, target diverse populations, and maintain different criteria for lending. Their single common denominator is that they all serve as "lenders of last resort" (McLenighan and Pogge 1991), providing credit to people who want to be self-employed but who cannot obtain credit through traditional channels.

This paper locates microcredit programs in the cultural climate of the U.S. by looking at one example, the Chicago-based Women's Self-Employment Project (WSEP), and examining how it has responded to its political and economic environment. The first two sections, entitled "The Women's Self-Employment Project" and "The Full Circle Fund," describe the program's agenda and operational structure. The next three sections discuss why private non-profits, rather than the public or for-profit private sector, fund U.S. microcredit programs. The "Challenges and Strategies" section looks at recent attempts to collectivize programs and to lobby for change. A section entitled "The Gender Question" provides a rationale for targeting microcredit programs specifically to women. The paper ends with a discussion of what microcredit programs in the U.S. have accomplished thus far and what they might hope to accomplish, given the proper support, in the future.

Micro lenders make it their mission to take risks that fall outside of the standards of traditional banks (McLenighan and Pogge 1991). These programs combat the myth that the poor are poor because they are lazy or otherwise deserving of their economic status; they recognize, as Karen File says, "that poor people work, very hard, to survive; that many do operate small businesses to do so; . . . and that the poor are 'bankable'" (File 1991). Microcredit programs often operate with the goals of poverty alleviation, community development, and individual empowerment; this causes them to do much more than business development.

Interestingly, less developed countries (LDCs) began to use microcredit as an economic development tool several years before the idea caught on in the U.S. While microenterprises share many similarities across cultures – little startup capital, easy entry into the market, rapid return on investment, and management by one person or one family – important differences also exist. A greater proportion of microentrepreneurs in LDCs work in the informal economy, where governments tacitly accept such activity. In the U.S., the informal economy is less acknowledged but often plays an important role in the life cycle of microbusinesses by providing a proving ground in which microentrepreneurs can experiment before moving to the more complex atmosphere of the formal economy.

The majority of microenterprise programs, both in developed and developing countries, focus on women.² Perhaps the most significant factor leading to this gender specificity is a dramatic increase in female-headed households over

the last 20 years. Over a third of all households worldwide are headed by women; in urban areas, female-headed households approach 40 percent.³ These arresting statistics have forced recognition of women's essential economic role as family earners. Self-employment works better than formal wage labor for many women because self-employment (which is generally home-based) adapts with relative ease to women's other choices and responsibilities, which include reproduction, childcare, and housework.⁴

The Women's Self-Employment Project

Women's and community organizations in Chicago, united by a common concern for the plight of low-income women, arrived at the idea for WSEP in 1985. At that time, women and children made up 78 percent of the nation's poor. In Chicago, women headed 60 percent of poor family households. Additionally, two-thirds of all working women earned less than \$15,000 per year; many of these women were welfare recipients, unable to obtain jobs paying enough to allow them to make the transition from welfare to work (Gellatly 1991: 3).⁵ Targeting poor women for self-employment meant creating a source of credit as well as providing education.

WSEP incorporated as a non-profit organization in 1986 to promote self-employment as a strategy for developing economic self-sufficiency for low- and moderate-income women; it provides training, technical assistance, and business loans. Since the program's inception, over 2,500 women have attended orientations, and over 450 have completed the program; 235 businesses are currently open. As of March 1991, the loan fund had disbursed 117 loans totaling over \$165,000, with only four defaults occurring in the early development of the fund, and a 97 percent repayment rate.

The Full Circle Fund

WSEP's Full Circle Fund (FCF) program uses peer lending, a practice initiated in 1979 by the Grameen Bank in Bangladesh. The Full Circle Fund operates as follows: five women who desire to, or currently, operate their own business and come from the same community form a "circle" and present their ideas to WSEP. Each group attends a four-week orientation program that enables it to become certified as an official WSEP group. The orientation teaches the groups the rules of the Fund, the procedures of borrowing and repayment, and basic business and management skills, and provides case studies on loan decisions and the business plans of sister members.

Full Circle Fund participants possess a great deal of autonomy over decisions governing the group. Upon WSEP certification, members choose two women to receive the first loans. The trust of fellow members serves as collateral. According to Susan Matteucci, Senior Enterprise Agent at WSEP, "this loan is a reality just like other borrowing, only peer pressure and peer support replace traditional collateral" (Gellatly 1991). Only after these two women have made three consecutive payments can the next two members become eligible for loans. Upon completion of three more punctual payments, the fifth member receives her loan. The loan ceiling is \$10,000, with a first-time maximum of \$1,500. Members achieve eligibility for additional loans only as long as all members maintain current payments.⁶ Mandatory individual savings accounts and a group Emergency Fund complete the structure of the program. As of March 31, 1991, women from the communities of Rogers Park, West Town,

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and Englewood had started 16 circles; 42 loans totaling \$38,804 have been disbursed. The repayment rate is 100 percent.

The peer group structure of the Full Circle Fund contributes greatly to its success. From a practical perspective, the combination of peer support and peer pressure operates more effectively than collateral to ensure payback. Because screening and loan approval are functions of the borrowing group, the women learn about and become responsible for underwriting and risk management. Finally, group lending helps to cut administrative costs by making members responsible for tasks that institutional staff would otherwise perform.⁷

Spillover Effects

While U.S. programs like WSEP have a much less clear agenda of social reform and self-improvement than do LDC programs,⁸ most clearly state program goals of helping women to take a proactive stance in terms of themselves and their communities. Beverly Smith, Director of WSEP, believes that the gap between poverty/dependency and self-sufficiency must be filled with a process of self-assessment, self-esteem, and self-empowerment. "If more women can go through these levels," she asserts, "then they will be better equipped to handle responsibility and move toward self-sufficiency" (Gellatly 1991).

Full Circle Fund borrowing groups, together with participation in the larger structure of WSEP, foster information networks and personal empowerment (Tinker 1989). WSEP women acknowledge that the opportunity to talk about ideas is as important as the more formalized meeting purposes; the structured meeting time sparks discussion of other issues, such as housing and childcare. Enterprise agents at WSEP say that women often become interested in WSEP primarily because they see spillover effects of networks in their neighborhoods and want to become a part of them.⁹

Why Not the Private Sector?

Interestingly, non-governmental organizations (NGOs) provide all of the microcredit programs in the U.S., filling a need that neither the government nor the for-profit private sector has met. These sectors have overlooked this population both for economic and for less tangible, more cultural reasons. First, the administrative costs of these loans remain too high relative to initial loan size to provide banks with sufficient profit incentive to provide them. In addition, most of the prospective borrowers need training as well as credit. Banks do not possess the resources to provide this training.

Risk, the other primary reason cited by the financial industry, is largely a myth that these programs have begun to debunk. The women targeted by WSEP are often perceived as lacking both marketable skills and hard-edged economic competitiveness, making them undesirable loan candidates. Many of the WSEP participants start businesses based on skills that have been categorized as women's work: child care, sewing, and cooking, for example. In fact, WSEP requires women to draw upon abilities they currently possess; the training focuses on business management skills. One of the reasons why women encounter difficulty when they try to obtain loans through traditional channels is that "women's work" has a shorter history of receiving the kind of recognition (such as pay) that "men's work" of a similar skill level has received. Patriarchal assumptions and valuations resulting from these histories have

relegated "women's work" to a lesser status than "men's work," and this is reflected in these women's difficulties in obtaining bank loans.

The second concern, regarding women's lack of competitive edge, arises from misperceptions about men's and women's value systems. Women's businesses are often discredited for not growing in the same way or at the same rate as men's. In many cultures, women have little or no control over their earnings; they are used either for basic immediate needs such as food or become part of a family pool to which the women often have no access (Noponen 1977). Under these circumstances, women cannot reinvest their earnings into their businesses. When women do control the surplus, they often invest it in their families rather than using it to grow the business.¹⁰ Irene Tinker asserts that:

For economists who consider profit-making and growth the very essence of entrepreneurship, alternative behavior is dismissed as pre-entrepreneurial; [women's] enterprises are not deemed worthy of inclusion in credit and other support programs designed to assist micro and small scale enterprises . . . the problem lies with the dominant economic value system, not the micro-entrepreneurs; the solution is for a paradigm shift to a more human economy (Tinker, forthcoming).

The concept of human economy acknowledges the legitimacy of valuing people and community welfare over individual avarice. It builds on data that show women continuing to "invest in their children's food or education despite accusations that this is not rational economic behavior" (Tinker, forthcoming).

Why Not the Public Sector?

The public sector's specific reasons for not recognizing and filling the need for microcredit programs are somewhat more difficult to discern, although the factors discussed above certainly operate in government as well. The U.S. policy environment, like the financial industry, "discriminates in favor of large-scale enterprise, and policies such as artificially low interest rate ceilings, overvalued exchange rates, and extensive regulation of business tend to make it harder to assist microenterprises" (Carr 1988). Interestingly, U.S. foreign aid has supported microcredit programs in LDCs for nearly thirty years and has only recently begun to promote domestic programs. This governmental lack of interest is particularly perplexing given the tradition of entrepreneurship that resides in U.S. culture. Governmental hesitancy probably stems from misperceptions similar to those of the for-profit private sector.

Why Private Non-Profits?

NGOs like WSEP have begun to fill a need that the public and for-profit private sectors have neglected both for economic reasons and because of pervasive stereotypes about gender, race, and the poor. One result is that small, unconnected organizations currently provide microcredit in the U.S. Some theorists argue that private organizations are actually best suited to deliver these programs. NGOs play the role of coordinator well in poor communities as a result of their basic commitment to and understanding of these communities. In addition, private non-profits (unlike governments) must behave like firms (in terms of efficiency, for example) in order to survive.

They must also respond more quickly and accurately to the needs and desires of their constituents. The provision of unique programs devised to assist different interest groups makes sense given the context of the market system in the U.S. The diversity of programs may even be necessary, considering the heterogeneous population of the poor in this country. The lack of governmental support that has given rise to this diversity, however, also causes these programs to have a very tenuous existence, dependent upon the changing interests of foundations and philanthropists.

While the current system of private delivery allows for the necessary flexibility that presently characterizes U.S. microcredit programs, the accompanying lack of sustained financial support makes significant expansion unlikely. A best-case future scenario for U.S. microcredit programs would involve a public-private partnership, with government providing decentralized support, in order not to squelch the entrepreneurial management style that has made these programs successful in the first place. Microcredit could grow by developing creative linkages with banks for loan support and with community colleges for training support.

Challenges and Strategies

Even though these programs operate outside of government, the policy environment shapes their structure and reach. For the most part, policymakers have failed to encourage self-employment as a route to self-sufficiency. Some policies hinder what these programs attempt to accomplish, operating as disincentives to self-employment. Federal welfare regulations constitute one of these barriers, placing a \$1,000 ceiling on the assets an AFDC recipient can accumulate without risking loss of her benefits. According to Gail Christopher (1986), "a business that is worth less than \$1,000 does not represent any potential for financial security, gainful self-employment, or economic self-sufficiency".

In 1986, WSEP conducted research on these barriers and presented a report to the Illinois Department of Public Aid. This report led to the Independent Business Women Demonstration Program, which allowed participants to receive loans, establish bank accounts, and operate businesses for 12 months without the loss of any welfare benefits (Cellatly 1991). The Illinois Department of Public Aid subsequently funded WSEP to conduct a pilot program in order to discern whether self-employment allowed women to make the transition from welfare to self-sufficiency. Fourteen of the 20 welfare recipients went off welfare and no longer receive money from AFDC; 16 are either off welfare completely or receive greatly reduced levels of aid. None has returned to a complete reliance on welfare.

Since then, microcredit programs have begun to organize in order to advocate on behalf of their constituencies; the Corporation for Enterprise Development (CfED) and the Association for Enterprise Opportunity (AEO) are two related organizations resulting from these efforts to lobby from a united position. CfED has mounted the Self-Employment Investment Demonstration (SEID) in order to obtain special federal project funding, waivers, and cost-sharing. AEO formed as a result of a June 1991 organizing meeting of representatives of microcredit programs. This organization also lobbies for more regular funding from the government.

These organizations have attempted to overcome barriers to government participation in microcredit programs. While SEID attempts to bring federal

funding into these projects, the amount of paperwork and bureaucracy makes it neither an efficient nor an effective method of government participation in microenterprise. In addition, the one-year waiver of asset limits currently provided fails to provide sufficient time for a business to prove its viability. Oftentimes, a period of instability following the commencement of business occurs before the generation of a steady flow of earnings.¹¹ Concern over the prospect of achieving such immediate success operates as a disincentive for many AFDC recipients to join SEID. While AEO has targeted government agencies and policies that can lend support to microenterprise initiatives, both organizations have worked together to relax welfare stipulations.¹²

The Gender Question

While the empowerment aspect of each of these microcredit programs constitutes an important ingredient towards helping women to achieve economic self-sufficiency, much more work needs to be done in order to help change the gender-based power structure of social relationships. Alleviation of the threat that will inevitably accompany such change, because it brings with it alterations in patterns of resource allocation, requires that programs like WSEP market themselves as part of a family/community strategy of economic development. Even when coupled with the critical empowerment strategies that many programs incorporate, there is a limit to what credit programs can do. While these programs can improve individual self-esteem and spur women to mobilize collectively, more powerful structures of subordination remain. Credit programs may then constitute an intermediate stage, contributing to women's economic security and self-confidence, both necessary steps toward breaking dependence and challenging entrenched gender relations in a constructive way.

The Case for Expansion of the Microcredit Model

One argument against microenterprise states that keeping marginal activities afloat by investing in microenterprise initiatives falls short as an economic development strategy because it keeps women on the fringe of the economy rather than integrating them into the mainstream. Because it assists women in understanding and evaluating economic options, self-employment may, however, constitute the important transition step leading to more active participation in the mainstream economy. Full Circle Fund members have begun to generate a pattern of obtaining training, spreading the word about the program, and helping to pull other community members in and up. Some have moved from self-employment to formal wage positions that they would not have been able to obtain without the WSEP experience.

One argument in favor of incorporating microcredit programs into a larger economic development program concerns the inner-city economy. Over the past three decades, providers of goods and services to these areas have largely fled, leaving communities gravely underserved.¹³ Some proponents of these programs argue that loanees will help to fill this void, providing these communities with much needed goods and services, such as daycare, repair shops, and small retail. In addition, the entrepreneurs become customers for other businesses, thus generating further employment. This economic revitalization can foster social and political betterment as well, functioning to increase household income, provide role models, and strengthen democratic institutions (Caravajal, 3).

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The statistics regarding default and repayment rates for microenterprise programs indicate that poor women, when provided with some technical and social assistance, are credit-worthy. Clearly, low income does not mean low creativity, low energy, and low responsibility. The high repayment rates on these loans, coupled with the increasing importance of women's role as family earners, make these programs an effective use of development funds (Noponen 1977).

Most of the women who participate in WSEP remain in the community to do business; the investment in training therefore stays local, with the potential to spread to others in the community as the businesses grow and as the women become role models. According to WSEP philosophy, "to create self-sufficiency for a woman is to help an entire family rise out of poverty and create new community role models" (Wolter 1991). Beverly Smith, Director of WSEP, further asserts that "women are the ones who spur economic growth. The woman goes into the community to buy shoes and food for her family" (Wolter 1990).

Definition and measurement of success are difficult for microcredit programs. Microentrepreneurs often delay working completely within the formal sector because it entails understanding and operating within a complex regulatory environment. Even after beginning to pay taxes on their businesses, these people often continue to keep some employees, such as independent contractors, off the books, and to participate in trading and bartering. Evaluations of these programs must attempt to measure the activity generated by microenterprises in the informal sector.

The non-economic results of these programs are more difficult to quantify. According to Bob Friedman of AEO, "Marked change in tangible economic indicators – employment, income, assets – are likely to be accompanied by and preceded by other, less tangible but no less important psychological, behavioral and social changes" (Friedman 1991). These include increased self-esteem, participation in community organizations, and investment in education.

The self-employment solution follows logically from the gendered focus because its flexibility allows women to maintain other, family-oriented responsibilities. The peer group structure works because it feeds individual self-worth at the same time that it fuels networking and community development. The prevalence of poor, women-headed households continues to be a problem warranting creative strategies. Microcredit programs, like WSEP, which include heavy emphasis on training and empowerment, effectively combat this problem by offering an alternative to formal wage labor and creating support networks that have positive spillover effects in the communities in which the women live and do business.¹⁴

U.S. microcredit programs, therefore, have begun to compile a history that warrants greater support. Currently, however, the fragmented nature of program delivery, combined with low and irregular funding, makes expansion difficult and slow. If U.S. microcredit continues to be funded largely through foundation and grant monies, substantial growth is unlikely. While repayment rates match those of programs in LDCs, U.S. programs do not approach those of the LDCs in terms of scale. The need to achieve scale is one reason why the recent creation of CfED and AEO is critical.

Existing policies that operate as disincentives will continue to make many women wary of taking such a big leap. Especially in a developed country like the U.S., participation in programs like WSEP must be measured against other alternatives to which low-income women have access (Ramdas 1991). Any alternative to welfare must virtually guarantee a long-range standard of living equal to or above that provided by welfare.

At this point, political factors combine with the lack of a significant history of success to keep microcredit from growing to a substantial scale in the U.S.; current U.S. federal policy remains largely unfriendly to private non-profit efforts to supply alternative sources of credit. The policy environment has relaxed somewhat in the last few years, largely as a result of lobbying efforts by CfED and AEO. It remains to be seen whether these recently organized coalitions will obtain further cooperation from government and/or whether government may take on a larger role in the provision of microcredit.

ACKNOWLEDGEMENT

Sincere thanks to Alec Gershberg for insightful commentary throughout the evolution of this piece.

NOTES

- ¹Microenterprises are very small businesses employing from one to four persons.
- ²WSEP, as its name suggests, serves only women, while Grameen Bank loanees include 90 percent women.
- ³UN 1991; cited in Tinker, forthcoming.
- ⁴Recent scholarship has documented and rendered visible women's heretofore largely "invisible" roles, such as serving as providers of water, fuel, and processed food. See Tinker, forthcoming.
- ⁵One of the most significant factors behind these data is the relatively recent "feminization of poverty," which has affected the nation as a whole and urban areas in particular. See Feinberg and Knox 1990.
- ⁶The interest rate is 15 percent, and borrowers make payments every two weeks.
- ⁷One largely unexplored factor that likely contributes to the women's amenability to working with the peer group structure is the already entrenched system of matrilineal kin support networks that operate as survival strategies in impoverished urban areas. Members of these networks approach a cooperative lifestyle, sharing responsibility for child-rearing and child care, food preparation, and other needs of the community. Some immigrant populations also devise informal credit schemes amongst themselves.
- ⁸One component of the Grameen Bank is a set of rules of conduct called the Sixteen Principles, to which all members must adhere. These principles focus on actions of daily life, and include resolutions to boil water, rotate crops, clean houses, and refuse to participate in the economically crippling dowry system still prevalent in Bangladesh (File, n.p.).
- ⁹Women participating in LDC credit groups such as the Grameen Bank have used peer groups as a jumping-off point to organize around other issues, such as health care, and have even lobbied for policy that supports self-employment. Kavita Ramdas, program officer of the Community Initiatives Program at the MacArthur Foundation, believes that "these political empowerment aspects could play a similar role in poverty alleviation and community development here" (Ramdas 1991: 28).
- ¹⁰Bob Friedman (1991) of Association for Enterprise Opportunity (AEO) also discusses the important distinction between income generation and asset creation, claiming that evaluation of microcredit programs must look not only at profitability and business starts but also at education and community involvement.

- ¹¹The Office of Family Assistance currently is considering the issue of waiver length.
- ¹²Two of these are the 1977 Community Reinvestment Act (CRA) and the Small Business Administration (SBA). Current lobbying is geared toward formalizing CRA credit for banks that form partnerships with microcredit programs, viewing these agreements as a legitimate way for banks to meet part of their reinvestment responsibility. In 1991, the Bush Administration authorized a pilot program in five states that will incorporate self-employment training with lending. It is the first SBA program designed to help the poor to become business owners.
- ¹³Alpert asserts that "inner cities have become small pockets of socialism in the American capitalist economy The public sector – federal, state, and city agencies – became the dominant force in the ghetto economy" (Alpert 1991: 167).
- ¹⁴Other economic questions which might be considered for further research include the extent to which small service and retail businesses, which form the bulk of these microenterprises, actually help the local economies that they serve.

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