Exploring Microenterprise Programs: Self-Employment in Disadvantaged Communities

By Marius Ioan Dancea

Poverty continues to plague America's urban communities. Many proposals have sought to address the issues related to poverty. Microenterprise programs are one such approach. Microenterprise programs design training programs that educate urban poor on how to establish and operate small businesses and structure microcredit activities that provide minimal loans to prospective or small business owners. By focusing on particular sites, such as ACCION Chicago, this article analyzes two aspects of microenterprise programs to argue that if such programs are to benefit those truly in need, they must simultaneously provide training and microcredit activities to the urban poor.

Microenterprise programs seek to increase self-sufficiency and self-employment among the poor, those on welfare, and the unemployed. However, not all microenterprise programs use similar strategies. Some programs focus on training activities designed to educate individuals on how to establish and operate small businesses. Alternatively, other microenterprise programs, such as those provided by ACCION Chicago, focus only on microcredit activities. Microcredit provides small loans to existing businesses or to individuals who seek to establish and operate new small businesses. This article analyzes the activities of one microenterprise agency, ACCION Chicago, using that paradigm as a means to better understand microenterprise and microcredit programs generally. The current study will also use this focus to discuss the social problems that microcredit programs attempt to address, the targeted solutions proposed, and the challenges that microenterprise initiatives confront.

Microenterprise and Microcredit Programs

Microenterprise programs depend on the formulation of strong relationships between lenders and borrowers; those relationships also help to ensure low default rates. Virtually all microenterprise programs provide training to low-income individuals, and once they have been trained, some are then referred to partner microcredit programs. However, some individuals do not benefit from microcredit programs because their credit history or income makes them ineligible to borrow (Servon, 1999). Lisa Servon argues that, in order to be most effective in the fight against poverty, programs should increase human capital while simultaneously increasing the ability of disadvantaged groups to access financial capital. There are two types of microenterprise programs. Some microenterprise programs focus only on microcredit activities, while other programs focus on both microcredit activities and training practices. ACCION Chicago, for example, focuses on microcredit activities to increase financial capital (i.e., money). Alternatively, the Institute for Social and Economic Development focuses on microcredit activities as well as training to increase human capital (i.e., skills). Both of these strategies are important in aiding disadvantaged individuals to become more self-sufficient.

Some researchers argue that lack of access to credit is a problem that cannot be cured with training activities alone, but must be solved by improving individuals' credit (e.g., Raheim, 1997). Microcredit programs partially address this problem by providing loans to small business owners who have been previously unable to access traditional forms of credit. Servon (1999) finds that funding for microenterprise programs is usually a result of relationships with banks, private-sector corporations, churches, community colleges, other microenterprise programs, community-based organizations, and government agencies at the local, state, and federal levels. In particular, ACCION Chicago provides loans of up to $35,000 to businesses that have been in operation for more than 1 year. Loans of approximately $15,000 are made to businesses in operation less than a year. The terms of these loans are typically from 2 months to 4 years. Loans are typically covered by collateral or guaranteed by a qualified cosigner. In other words, microenterprise lenders do not furnish these sorts of loan guarantees as part of their services. Notably, ACCION Chicago does not furnish these sorts of loan guarantees as part of their services.

In order to obtain loans through ACCION Chicago, applicants must have income sufficient to honor payments on the new debt, must live and operate the business within Illinois, must use the loan to engage in legal business activity, and must be at least 18 years old. The interest rate on these loans depends on credit risk and history of the business. Rates can range between 10.6 percent and 16 percent for a fixed-rate loan. The turnaround time to receive a loan varies, depending on qualifications, but a pre-qualification determination can be made within one week. Loan approval and the loan-closing schedule depend on the timely submission of requested documents. The effectiveness of ACCION Chicago's microcredit program can be seen in its success rate. Over 90 percent of ACCION Chicago's loans have been repaid (ACCION Chicago 2002; Jonathan Brereton, chief operating officer, and Peter Redovich, associate, ACCION Chicago, personal communication, November 21, 2003).

WHAT'S THE PROBLEM?

In 1997, one billion people around the world lived in poverty (Woodworth, 2000). Concentrated pockets of poverty also continue to plague the United States. This is particularly the case in urban areas (Tinker, 2000). Very few community strategies have been effective at alleviating the economic barriers faced by residents of these low-income pockets (Raheim, 1997). Warner Woodworth argues that the underlying cause of poverty is lack of wealth, asserting that the individual, not government, is responsible for creating wealth. This argument is problematic, however, because it does not take into consideration the availability of employment. Furthermore, regardless of the willingness of welfare recipients to work, there is no way to reduce the number of people in poverty until increases in employment enable those in need to build wealth or until other means of acquiring wealth are provided (Pfleger and Bennett, 1995).

Employment opportunities allow individuals to build assets. Effective strategies to increase self-sufficiency (as outlined in such policies as Temporary Assistance for Needy Families) must focus on increasing individuals' assets. This focus on building assets, in turn, increases national levels of wealth (Pfleger and Bennett, 1995; Raheim, 1997). But assets alone are not sufficient to address persistent economic barriers. One strategy of overcoming economic barriers is community development. Ronald Ferguson and William Dickens (1999) point out that in order to facilitate growth of community development (that most argue cannot be separated from economic development), "neighborhood-based organizations could be instruments of political and economic empowerment, with a heavy emphasis on internal production and self-sufficiency as an economic development strategy" (p. 18). The individual benefits from strong neighborhood organizations because they not only create networking and support opportunities for low-income individuals, but these organizations also assist individuals by teaching how to build assets. Thus, the most effective way of increasing individuals' wealth, and thus national wealth, is to provide programs that pave the way of wealth creation and maintenance.

For poor women (especially poor single mothers), barriers, such as lack of child care, decreased access to transportation, low education, and low job skills, further limit employment opportunities (Tinker, 2000). In addition, juggling parenthood with employment intensifies economic isolation, and such demands further impede individual economic growth (Tinker, 2000). For recent immigrants (especially undocumented immigrants) and refugees, a number of factors, including language and cultural differences, may make mainstream employment inaccessible (Raheim, 1997). The factors are further complicated by the flight of entry-level jobs to other countries, where cheaper labor and more lenient labor laws only serve to further deepen the poverty in American urban areas. Economic isolation also results from the pressures that many companies place on entry-level employees to discourage them from organizing. Such pressures can include elimination of health care benefits in order to increase profits and threats to shut down the company if employees attempt to exercise rights to organize (Virginia Parks, personal communication, November 20, 2003).

For members of oppressed or marginalized groups, self-employment (such as starting a new business) can provide a level of flexibility and freedom. Self-employment may also result in a living wage and enable individuals to earn a higher wage than the one that could be earned in the mainstream labor market (Raheim, 1997). In fact, for some families, self-employment activities may be the sole means of survival. According to Salome Raheim (1997), a study finds that approximately 500,000 former welfare recipients were supporting themselves through self-employment activities. However, there are also significant barriers to self-employment as well, in particular, to those people receiving public aid. Over 100,000 women were supporting their families through a combination of self-employment and welfare benefits (Raheim, 1997).

According to Raheim (1997), the primary barriers to self-employment include lack of business knowledge and skills (human capital), as well as lack of access to various types of capital (such as financial). In terms of human capital, low-income people from disadvantaged groups are less likely to have access to the information resources that would make such knowledge and skills reachable (Raheim, 1997).

Interestingly, the basic forms that define community development (human capital, physical capital, and social capital) are the same types of capital missing from those who need them most, and the absence of this capital impedes their growth. Notably, theorists such as Alejandro Portes (1998) and James DeFilippis (2001) argue that social capital is essentially created at the individual level; networks are made of individuals, but can be aggregated and measured at the community level. In particular, Portes writes, "the greatest theoretical promise of social capital lies at the individual level—exemplified by Bourdieu and Coleman—there is nothing intrinsically wrong with redefining it as a structural property of large aggregates" (Portes, 1998, p. 15). DeFilippis concludes that social capital should not be "divorced from capital (in the literal economic sense), stripped of *power* relations, and imbued with the assumption that social networks are win-win relationships and that individual gains, interests, and profits are synonymous with group gains, interests and profits" (2001, p. 800). DeFilippis (2001) points to community-controlled capital and argues that the root of the problem lies in the lack of economic capital. He argues that the absence of available economic capital should receive primary focus, and he eschews the strategy of building economic capital through social capital. Therefore, Portes and DeFilippis shed light on how the complexities of the various types of capital have great relevance for microenterprise programs; these programs constantly try to seek out the best methods to negotiate capital.

Raheim (1997) argues that lack of access to physical capital might be the biggest barrier to people receiving public assistance, because it limits opportunities for business success. Banks are reluctant to finance the business ventures of low-income people because of poor credit history or lack of collateral. Moreover, the loans needed to finance many self-employment activities are seen as too small to be profitable for many banks. Lack of capital also limits the types of businesses that can be created. Woodworth (2000) argues that even a small loan could make a big difference in low-income communities, particularly in third-world nations. Servon (1999) finds that microenterprise programs depart from traditional attempts to address the problem of persistent poverty through economic development. As compared to either traditional economic development or poverty alleviation strategies, microenterprise programs are more flexible, more creative, and more oriented to the context in which they operate. Indeed, the microenterprise strategy offers hope that there is room to operate within the confines of the policies now in place.

ACCION CHICAGO'S SOLUTION TO THE PROBLEM

There is much evidence to suggest that microenterprise programs provide a trickle-up approach to the battle of poverty (Fairley, 1998; Pfleger and Bennett, 1995; Raheim, 1997), but not all microenterprise programs have the same strategy. Some microenterprise programs provide services that focus on training and interaction with the clients. Other programs, such as those of ACCION Chicago, focus on microcredit activities. In order to understand how ACCION Chicago assists the impoverished with its programs, two

ACCION Chicago associates were interviewed together. One was a current chief operations officer and the other was a former employee. Both noted that by providing training and financial services, ACCION Chicago is giving low-income individuals the tools (i.e., business skills and financial capital) to compete in the mainstream economy. This focus on providing both training and services contradicts ACCION Chicago's mission because according to its mission, ACCION only provides microcredit activities. Thus, they argue that capital and training should go hand in hand. That is, if programs are to be most effective in helping the poor and unemployed overcome the barrier of economic isolation, they should focus on training services while simultaneously providing access to capital (Jonathan Brereton, chief operating officer, and Peter Redovich, associate, ACCION Chicago, personal communication, November 21, 2003). Their views are in agreement and coincide with research showing that although training activities provided by microenterprise programs should be combined with credit assistance, lack of access to financial capital is a major barrier to individual economic prosperity. Limitations on access to credit deserve a closer examination to determine their role in the training-credit relationship (Raheim, 1997).

Often, microenterprise programs like those of ACCION Chicago have similarities with microenterprise programs in third-world countries. For example, Woodworth (2000) finds that to empower the third-world poor, small businesses are created through village banking. In this process, no collateral or credit history is required. When a group borrows money, each member of the group is individually liable for the entire amount of the loan. Woodworth noted that social pressure and trust create powerful incentives (such as group responsibility, accountability, and shame from the community) for the group to pay back the loan; members do not want to be the sole individual responsible for repayment. The structure of these microenterprise programs in third-world countries does not necessarily mirror those in the U.S. If the practices and programs at ACCION Chicago are analyzed, differences become apparent. ACCION Chicago requires collateral or a cosigner in order to prequalify for the loan. The microenterprise lenders in third-world countries definitely do not require such steps. In the U.S., such requirements create a creaming effect, such that the system favors those able to find cosigners and collateral. As a result, the poorest and least skilled are cut off by this strategy.

ACCURACY OF GOAL-STRATEGY MATCH

ACCION Chicago's proposed solution to the problem of poverty is to provide "credit and other business services to small business owners who do not have access to traditional sources of financing" (ACCION Chicago, 2002, p. 2). However, ACCION Chicago does not target individuals who are not business owners. Rather, they provide loans for existing and prospective owners but do not provide services to any other type of clients. Microenterprise programs serve two types of clients: the larger, more advantaged pool that is ready to borrow, and the smaller, less-advantaged pool that needs more training. For both of these groups, there is pressure to control loan losses and to keep the cost of training down. Such pressures reinforce the tendency to lend to better-educated, more affluent clients (Bates and Servon, 1996). ACCION Chicago falls into the same trap as most microenterprise programs: "[they] do more to help those who exist at the margins of the mainstream economy than those who are completely cut off from the economic mainstream" (Servon, 1997, p. 166). As a result, microcredit makes only a small impact on the poorest communities.

CHALLENGES TO THE INITIATIVE

There are a variety of factors that impede the success of microcredit programs like those at ACCION Chicago. In her review of the research, Joanne Fairley (1998) points out six specific factors that complicate the success of microcredit programs. First, "microcredit institutions work with a safe target group—not the poorest—because of funding accountability concerns" (Fairley, 1998, p. 2). Second, because the poor are stigmatized, many microcredit lenders distrust the poorest of the poor. Third, there is a huge time commitment when trying to assist the poor. Fourth, policies such as licensing requirements and a fluctuating economy harm the growth of small businesses and savings. Fifth, the poorest of the poor become uninterested and uninvolved because of the many risks. Sixth, policies that would provide alternative forms to inflexible microcredit criteria for the poorest of the poor are absent. In addition to these six factors, Raheim (1997) notes that small amounts of loans will facilitate more small businesses than demand will support. Also, he contends that lack of adequate health insurance (e.g., major medical expenses) can easily bankrupt uninsured small business owners because small businesses often do not generate enough income to assume health insurance costs.

SOLUTIONS TO CHALLENGES

Joanne Fairley (1998), Solome Raheim (1997), and Lisa Servon (1999) provide us with important lessons on how microcredit programs can facilitate economic growth and success of small businesses that belong to low-income individuals and communities. First, at the individual level, microcredit programs should target those who are marginalized and excluded from economic opportunities by attracting and providing more training classes. Second, at the institutional level, microenterprise programs should be funded in such a way so as to grant waivers to participants for at least 2 years in order to eliminate such barriers as health insurance that have the potential to bankrupt a small business. Because self-employers often lack financial stability, giving microloans to them is not enough. The state should provide special care to these newly developing microenterprise programs in order to aid in the potential success of the small business. This is especially the case during the first 2 to 3 developing months of small businesses. This would shield fragile small businesses against undercapitalization effects, such as unanticipated medical emergencies.

Third, at the national level, the U.S. government should consider increasing funds to self-employment development programs (e.g., microcredit and training programs) and provide more self-employment options at job placement sites. Also, Raheim (1997) concludes that self-selected participation appears to be more effective and empowering when it attempts to target individuals based on beliefs about their potential for success. It is also important to note that the Community Reinvestment Act (CRA; 12 U.S.C. § 2901) requires banks to work with microenterprise programs, such as those of ACCION Chicago, in order to meet the requirements set by the government (Brereton and Redovich, personal communication, November 21, 2003). Thus, evidence suggests that investing in the poorest communities is highly selective, but has great potential to increase both the self-sufficiency of individuals and the basic forms of community development, such as physical capital, human capital, and social capital.

There have been few evaluations of the effectiveness of microenterprise programs. One exception involves the only experimental test of the impact of microenterprise programs conducted by the Unemployment Insurance Self-Employment Demonstration (UISED). UISED analyzed data from microenterprise programs in Washington and Massachusetts (Schreiner, 1999). The UISED did not reveal the best design for microenterprise, nor for programs regarding social investment. However, Mary Schreiner (1999) concludes that while UISED did shorten unemployment spells, other changes had small impacts and the most disadvantaged individuals did not choose to participate.

CONCLUDING REMARKS

Research suggests that microcredit programs can help to alleviate poverty when they are closely connected with training programs. However, microenterprise programs are not the only answer to the problem of poverty. This is particularly true of the problems facing those most in need. Nevertheless, evidence clearly shows that effective strategies to reduce welfare dependency must focus on increasing wealth through self-employment (Raheim, 1997; Servon, 1999). The government's involvement in the welfare state need not increase in order to curb poverty. Rather, more strategies are needed that use microenterprise programs effectively to target the poorest of the poor. ■

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