Microenterprise:
Human Reconstruction in America's Inner Cities*

Lewis D. Solomon

June 1991

Introduction

Gloria Davis has traveled what seems like a very long road -- from welfare mother to successful entrepreneur in only two years. Davis now operates a designer dress shop called Neo Emporium on North Clark Street in Chicago. The store houses designer clothing on consignment and offers custom designed clothing. Davis, who sewed bridesmaids dresses at home when she was not going to trade school or raising her children, got her first loan from the Women's Self-Employment Project -- for a grand total of $175.

Davis is an early success story in a promising new approach to the seemingly intractable poverty of America's urban underclass. The approach is usually referred to as microenterprise, a development model in which small loans and peer support are made available to those interested in starting "small" small businesses. In contrast to the traditional approach to poverty -- in which a wide range of government sponsored welfare programs only seems to contribute to underclass dependency and despair -- self-employment, supported by modest amounts of credit, rather than wage employment, may enable enterprising individuals to break the seemingly inexorable trap of poverty.

This paper explores the potential of creating a pervasive urban entrepreneurial culture through self- employment, access to credit and peer support. Yet microenterprise cannot, by itself, transform the bleak urban landscape. A successful strategy for human reconstruction in the inner cities must rest on three principles.

First, new policies should be based on old- fashioned, but often neglected values --responsibility for one's self and one's community, pride, hope for the future, and the work ethic.[1] Second, society must discard or modify institutions and legal rules and regulations which restrict individual initiative. Money, particularly public sector credit and investment, should be steered to productive people. Third, self-help and the development of communities from within rests on involving people in the process. By keying policies to the values of responsibility, empowerment, control over one's life and human growth, the resurgence of America's inner cities can occur. To achieve these goals, public and private ventures must launch a holistic effort to deal with a broad range of urban ills.

What Is Microenterprise Development?

The microenterprise development model stems from the concept of entrepreneurship and the notion of "small" small business. Microenterprises are especially important in areas such as inner cities where there are few formal job opportunities. A microenterprise usually employs less than five persons. These small businesses are usually capitalized with under $5,000 and tend to gravitate to retail or service activities. Many are home-based.

Recent microenterprise development focuses on loan funds. A revolving microenterprise loan fund, usually organized as a nonprofit organization,[2] makes very small, short-term working capital loans to people who wish to start or expand a small business. This type of lending requires neither collateral from borrowers nor a job history or credit rating.

Lower paid workers, unemployed individuals, and those who are disadvantaged in the labor market (because of a language barrier or a handicap) are more likely than others to turn to self-employment. In other words, confronted with limited options in formal labor markets, inner city residents may increasingly look to self-employment initiatives as an alternative to traditional ways to earn money. However, the ability to achieve economic self-sufficiency is hampered by lack of access to capital. Microenterprise loans are unattractive to commercial banks. The loan transaction costs are high relative to the interest and fees received from a small loan. The costs to originate and service a $1,000 loan approximate those associated with a $100,000 loan. Similar paperwork is required to originate and service a loan, regardless of its amount. The microenterprise borrower has few assets that can serve as collateral. Many of the owners have no credit history and are not personally known to the bank lending officers.

Government programs have not figured prominently in microenterprise financing. They tend to be oriented to larger, more sophisticated, small businesses. As one economic development organization concluded, "[d]espite the lack of hard evidence, there appear to be capital needs in the microenterprise sector which are not met by the banking community and existing governmental programs."[3]

A promising model for microenterprise lending in the U.S. is the Grameen Bank in Bangladesh. The Bank has been successful in helping people in a desperately poor Third World country work their way out of the most abject poverty. This paper examines how the Grameen Bank works, and assesses the efforts of micro bankers in the U.S. to stimulate self-employment among the inner city poor. Although this inexpensive, market- oriented, entrepreneurial solution can help alleviate poverty and promote economic development, various governmental and social obstacles currently hinder the potential of microenterprise development. This paper proposes various means to overcome these barriers and considers the potential contributions from the private, nonprofit, and government sectors. It concludes that these contributions, combined with a broader role for the micro banker, are necessary for microenterprises to flourish.

The Informal Sector in the Third World

The informal economic sector, chronicled in Peru by Hernando de Soto,[4] consists of microenterprises in sprawling urban centers and rural villages. Entry- level microenterprises include vendors peddling their wares on street corners, farmers and traders who sell locally grown and produced foodstuffs, and entrepreneurs who engage in a variety of service and repair functions.[5]

Informal sector enterprises comprise 80-90 percent of the business activities in a typical poor Third World urban neighborhood or village. Such activities employ from 30-70 percent of a developing nation's labor force.[6] Informal businesses are found not only in urban areas but also among rural households and consist of off-farm enterprises, clothing, construction, and delivery of items such as sanitation supplies. They typically are family businesses which rely on members for capital, investment and labor. In short, microenterprises generally are owned by the landless urban and rural poor. The informal sector is relatively easy to enter, unregulated, small scale, competitive, labor intensive, and permits adaptability of resources from one use to another.[7]

Women play a significant role in the Third World's informal economic sector. For example, in Peru, excluding domestics, 40 percent of the informal sector labor force and 61 percent of self-employed are women.[8] Since Third World women often lack access to formal employment, home-based activities are their only means of earning a livelihood. The informal sector also provides the flexibility of balancing child care and the need for income.[9]

In developing nations, from Bangladesh to Peru, entrepreneurs struggle to escape constant indebtedness to loansharks, relatives, informal moneylenders and traders. They want to exit poverty by receiving the full value of their labor. All too often, however, an informal financial intermediary takes away a significant part of an income stream due an individual.[10] Hence the need for a new credit source that will help poor people build their asset base and keep a higher share of the proceeds of their work.[11]

The Grameen Bank

The Grameen Bank in Bangladesh has pioneered microenterprise uncollateralized lending. Founded in 1983, the Bank's borrowers number in the hundreds of thousands.[12] It tests the hypothesis that the poor can generate productive self-employment if they are supplied with capital. The Bank is a borrowers' cooperative with borrowers owning 75 percent of its shares. (The government owns the remaining 25 percent.) A private entity, the Bank sets its own policy and has its own branches and staff. Except for foreign exchange transactions, it is empowered to conduct the full range of banking functions, including technical and extension services to clients.

Because its intended beneficiaries are often illiterate and timid about approaching banks, the Grameen Bank puts branches in small communities and sends employees into villages to spread information about its activities, promote the formation of borrower groups, and collect repayments. Village banking benefits from economies of scale. Many of the loans are similar, enabling one bank representative to monitor thousands of loans on a weekly basis.[13] The average loan is for $67.[14] With an annual interest rate of 16 percent,[15] the Bank's loans have enabled thousands of poor borrowers to escape the clutches of the dreaded village moneylender, who typically charges interest rates of 120 to 200 percent per year.[16]

Between two-thirds and three-quarters of the Bank's borrowers are landless women.[17] The Bank concentrates on female borrowers, whom it regards as having a greater interest in family stability than males.[18] As Mohammed Yunus, the founder of the Grameen Bank notes,

> Given an opportunity to fight against hunger and poverty, a poor woman turns out to be a natural and better fighter than a poor man. Poor women have the intense drive to move up, they are hard working, concerned about their human dignity, concerned about their children's present and future, willing to make personal sacrifices for the well-being of their children.[19]

Female and male borrowers form separate groups. Between 80 and 90 percent of the money loaned to women is used for one of two purposes: 1) livestock and fisheries; or, 2) processing and manufacturing. Loans for women-owned trading and shopkeeping enterprises have also risen substantially.[20] The Bank's financial assistance to landless women has enhanced their social and political status. Female borrowers are less home-bound and command greater respect from their husbands and neighbors as a result of their increased access to capital.[21]

For male borrowers, trading and shopkeeping are the major activities, accounting for about 50 percent of the total loaned to men. Other enterprises for which males borrow include, in descending order of importance, processing and manufacturing, livestock and fisheries, and transport services.[22]

The Bank initially offered larger loans to collective enterprises, so that groups of poor borrowers could pool their resources, achieve economies of scale, and compete with people in higher income groups. However, these collective enterprises failed to expand as rapidly as individual ones, and the number of people participating in them has dropped significantly since the mid-1980s.[23]

Performance Data and Social Impact

From the perspective of the Grameen Bank, the key measure of success or failure is the loan repayment rate. From the standpoint of the landless poor who borrow from the Bank, success is measured in terms of increases in incomes, savings and assets.

Loan Repayments

The Bank enjoys an enviable loan repayment rate of 98 percent.[24] Bank officials say its success is attributable to the use of solidarity groups as well as its policies of short-term loans and incremental lending.[25]

In order to qualify for uncollateralized loans from the Bank, potential borrowers must form groups of five.[26] Before any one group member obtains a loan, the entire group must undergo a training session, spanning one to two weeks, to learn the Bank's strictly enforced rules and procedures and help members develop their business skills. After the initial training period, each group member attends weekly group meetings with an officer of the Bank.[27]

Up to 10 groups of borrowers in one area federate into a "center" and elect a center chief and deputy center chief. Several centers in turn form a branch. Each group formulates and considers loan requests which are reviewed and approved by the center chief, a Bank worker, program officer, and finally the Bank's branch and zone manager.

The advantages of establishing solidarity groups include: (1) providing a group member the reassurance to take business risks he/she might not have undertaken; (2) laying a foundation for larger business ventures (collective or joint enterprises) which individuals find too risky to undertake alone; and, (3) creating peer pressure to fulfill loan repayment schedules and other obligations to the Bank and the group.

All loan requests are discussed candidly at group meetings; transactions between the Bank and individual members of each group are not confidential. The group scrutinizes each member's prospective enterprise and business proposals, ensuring that they "are more likely to be well thought out and are likely to make a profit from which they can repay the loan."[28] Group members strive to keep business ideas that are not feasible from being approved and to share ideas to make businesses more profitable. Moreover, in forming their groups, members screen out prospective borrowers deemed unlikely to repay a loan.

Once the Bank approves a loan, group members monitor how the money is used. This ensures that borrowers "are more apt to operate their business properly since they will be examined by others frequently."[29]

Peer pressure is also sustained by the sequence of loans. Say, for example, that one member of a newly- formed group receives a loan. The other four members are ineligible for loans until the borrower demonstrates regular payment of the weekly installment.[30] The group thus has an incentive to encourage a delinquent member to make her payments, or it may resort to making the missed payments. Second loans are not approved for any one member until the accounts of all members are settled. In other words, the group ensures mutual accountability and serves as a form of moral collateral.

By relying on the borrowers themselves to monitor loans and guarantee repayment, the Bank is able to forego close analysis of each loan application, thereby lowering the high transaction costs that discourage loans to small businesses. And by grouping borrowers, the Bank staff can service more loans with fewer contacts.

Two other factors contribute to loan repayment success. First, most loans are short-term. A one-year term is typical, with principal repaid in fifty weekly equal installments and the interest repaid in the fifty-first and fifty-second installments.[31] Second, the Bank practices incremental lending. Borrowers initially receive a small loan, so as not to overwhelm them with cash. Once the borrower repays the first loan, subsequent loans can be larger and have a longer repayment period. The incremental lending technique provides incentives to the borrower and minimizes the risk to the Bank.

Impact on Income and Savings

Of course, peer pressure will be unavailing if borrowers do not generate enough income from their loans to pay them back. Studies of Grameen Bank lending show that increases in borrowers' incomes have been striking. For example, over a two-and-a-half year period in the mid-1980s, household incomes among Bank borrowers rose about 70 percent in nominal terms.[32] This income gain is particularly notable in comparison to the average annual income increase of 2.6 percent for the landless and rural poor in Bangladesh.[33]

Borrowers' savings rates also rise. Higher savings come from two main sources. Each group member participates in a group savings program that requires weekly deposits into a savings account. Each borrower also pays a group "tax" of 5 percent of any loan amount received.[34] Group members can borrow from the group funds for investment and consumption purposes with the consent of the group members. The group funds serve two purposes. First, they give the borrower a greater stake in the venture as well as a resource for other investments. Also, members who leave the group may withdraw the personal weekly savings, but not the 5 percent deduction. Second, the savings requirement provides additional capital for the Bank.[35] The group members also must contribute to an emergency fund equal to 25 percent of the interest charged by the Bank on its loans. These funds are used for the development of health, life, and property insurance for the group members.[36] In short, over time, the borrowers earn and save enough to increase their investment capacity.

The Human Impact

Beyond these generalizations with respect to how loans are being used and the aggregate direct benefits resulting from the extension of credit, how has the Bank changed peoples' lives? Two examples help to bring the human dimension of microenterprise to life.

In Bathoimuri, a village 40 miles north of Dhaka, the capital of Bangladesh, the Bank had as of 1987 lent money to 575 people, two thirds of them women. Rabea, a landless Bangladeshi, lived in a dirt-floored house. She was so poor she could not offer a visitor a chair or protect her children from rain leaking through her thatched roof. In 1986, Rabea borrowed enough to start a small business and slowly advance her family's standard of living. She borrowed $90, bought a cow and started selling milk. Her earnings made possible a $85 family investment in a bicycle rickshaw, which enables her two grown sons to make a living.[37]

Rezia Begum, the leader of Center No. 1 in Jamurki, had repaid her sixth Bank loan and was waiting approval of her seventh to expand her rice-husking business. She recounted that when she applied for her first loan, the Bank was still an experiment, "'I was living under banana leaves. I had no home.'"[38] Her husband, a wage laborer without steady income, warned her that the Bank's offer of a loan was a "hoax." However, Rezia viewed the situation as desperate. She felt, "'I must try.'"[39] At that time she worked as a housemaid. She was "paid" in table scraps, not money. Rezia recalled, "'I had no food for breakfasts. Our meals were uncertain. If I worked, I would share whatever leftovers I got. Everyday we didn't know if we would eat or not.'" Now, her typical diet, although meager by Western standards, is vastly improved: leftover rice, a small fish and jackfruit nuts for breakfast; rice, lentils, jute stalk, squash, and fish for lunch and dinner. Thanks to her earnings, she had a modest homestead and two wells for drinking water.

A major function of the Bank is social improvement, specifically, family planning, health, sanitation, and nutrition. According to Bank officials, 90 percent of the borrowers in the village of Jamurki adopted temporary or permanent birth-control measures; Rezia and several others in her center have had tubal ligations.

Rezia's husband borrowed money from the Bank to trade firewood but he misused the funds. Rezia stated smugly, as other group members giggled (covering their mouths with Muslim modesty), "'I persuaded the bank not to loan to him again, and because I had assets by that time, he couldn't leave me.'"[40]

Although she made strides economically and personally, Rezia remains impoverished. Rezia readily acknowledged, "'Another bank still won't consider us loanworthy.'"[41] However, that did not diminish her pride and wonder at how far she had come. When she was a maid, she never imagined a bank might take a chance on her. She reflected, "I never even dreamed of it. It was beyond our comprehension.'"[42]

Financing the Grameen Bank

The Bank provides loans that conventional banks would regard as too risky and costly. While some of the Bank's practices -- such as shifting loan tracking responsibilities to the group -- conserve operating costs, other aspects of the Bank's unconventional techniques, such as training members and weekly collection, result in higher costs than the typical rural credit program.[43] The major sources of funds for the Bank are loans from domestic and foreign banks, grants, and deposits contributed by members to the emergency and weekly savings funds.[44] While the Bank operated at a profit of 2.8 percent of its loan volume in 1984, the following two years yielded no profits.[45] Thus, studies indicate that the Bank may need a subsidy for its operations.[46]

Lessons

The Grameen Bank experiment demonstrates the possibility of providing credit to the poor in spite of a lack of collateral. The Bank's success suggests that the extremely poor can improve their socio-economic status through microenterprises if given an opportunity. This opportunity is unlike the traditional welfare hand-out; rather, the Bank has succeeded because it empowers solidarity groups to manage their own funds and monitor the group. Thus, instead of an outside authority dictating constraints on the borrower, the borrower's peers provide pressure as well as support. The Bank's experience demonstrates a link between economic revitalization and an improved social structure,[47] and thus provides a valuable guide to other countries. The concept of generating self-employment through credit monitored by micro borrowers groups may work elsewhere provided that the program accounts for varying social and economic structures.

Micro-Entrepreneurship Among the U.S. Poor

In the United States, microenterprise lenders have sought to enable poor people to generate a livelihood through self-employment. These lenders recognize that entrepreneurs require access to capital for startup financing. Microenterprise lending involves more than merely providing funds to the disadvantaged; it promotes entrepreneurial development as a strategy for greater self-sufficiency, self-esteem, and autonomy. Loans are made on the premise that inner city residents are people with considerable potential. To tap this potential, microenterprise lenders have developed a variety of programs.

Women's Self-Employment Project: The Grameen Bank Model

One of the leaders in the area of community economic development48 is the Women's Self-Employment Project (WSEP) in Chicago. Incorporated in 1986, the project provides training and credit for low-income women to start their own microenterprises. WSEP promotes self-employment as a transition from welfare to work or as a supplement or alternative to low-wage jobs.

WSEP runs two complementary programs: (1) its original self-employment training program and loan fund for individual women and (2) the Full Circle Fund (Fund) started in the Fall of 1988, a peer group microenterprise revolving credit program modeled on the approach pioneered by the Grameen Bank. In the original program, women participate in a 12-week training program and make business plans, then apply for individual loans. The training concentrates on both business skills and self-development. In order to receive a WSEP loan, the borrower must provide collateral of 50 percent of the loan's value.[49]

The Full Circle Fund, WSEP's second program, does not impose such a collateral requirement. As in Bangladesh, women organize themselves into groups of borrowers. The Fund's primary objective is to provide credit which will improve the income-generating capacities of the microenterprises. As of early 1991, the Fund had a loan fund of $190,000 and 17 groups of borrowers were created under the Fund's sponsorship.[50]

The Fund's focus on poor women who are, by traditional banking standards, the least credit-worthy requires considerable community outreach. A Fund staff member, called an enterprise agent, seeks prospective borrowers in low-income neighborhoods through a variety of methods, including referrals from community organizations, community publications, and word of mouth.[51] The enterprise agent meets prospective borrowers on their own turf -- in the home, in religious organizations, on the streets -- not in a downtown office. The agent helps to put together a Circle, or group of five borrowers, and monitors each loan. [52]

The Fund provides short-term (one year) loans to women in order to start or expand a self-employment business.[53] The initial loan is limited to $1,500; the maximum loan cannot exceed $10,000. The Fund does not make working capital loans; instead loans are provided for equipment and machinery, inventory, supplies, and marketing.[54]

To foster trust and group cohesion, Circles are composed of women who live in the same community. Family members or business partners cannot belong to the same group, but may participate by joining a separate group.[55]

The Circle members go through an orientation that culminates in its certification as an official borrowing group.[56] An orientation season, spread over six weeks, familiarizes the Circle with the Fund's rules and regulations; the general rules for borrowing and repayment; basic business skills, such as the need for maintaining budgets and separating business and personal funds; and, devising a business plan and marketing strategy. Vocational training and technical assistance is minimal, as the Fund seeks to capitalize on the prospective borrowers' existing skills and self-employment activities.

Once a Circle is certified, its members meet every two weeks to discuss and analyze their business and expansion plans, make decisions regarding individual borrowing requests, and receive and make loan repayments.[57] The group lends the necessary moral support for members whose business is in the transition stage from an idea to reality.

In effect, the Circle serves as the Fund's "loan committee." It reviews loan proposals and selects the members who will receive the first loans. In some instances, an enterprise agent and the WSEP loan committee evaluate the loan and raise questions for the Circle to address.

The interest rate on the Fund's one-year loans is 15 percent. Borrowers start making payments two weeks after receiving a loan, and continue paying every two weeks for the rest of the year. The Circle requires borrowers to begin using their loans within one month and produce receipts for business purchases.[58]

Group members are eligible for future loans only if all borrowers in a circle are current on their loan repayments. If one member of a group defaults, the others lose their access to the Fund's credit. After the first two members make their loan repayments at meetings over a two-month period, the third and fourth members become eligible for loans. If all four members keep up their payments for another two months, the fifth group member becomes eligible for a loan.[59]

The Circle also collects deposits for each member's savings account, called an Enterprise Account.[60] In addition, each borrower contributes five percent of her loan amount to the Circle's collective savings account.[61] Circle members decide how to use this emergency fund account. In theory, they may use the savings fund for any purpose, but it is intended for business-related expenses, such as group insurance, an emergency loan to a group member, or as a source of additional funds for a member's business.

The Fund's Record

With a track record of less than three years, it is premature to assess the success of the Fund. Remarkably, however, no borrower has defaulted as of 1991.[62] Borrowing from the Grameen Bank model, the Fund's strategy is to replace bank collateral with peer pressure and group support. The peer groups further enable participants to network with other business owners, thereby lessening the isolation of self- employment.[63]

For what purposes are these microenterprise loans used? Here are the main categories and the number of Fund participants in each: graphic design, 1; product promotion, 1; seamstress, 11; clothing/accessories sales, 11; beauty, 5; household services, 5; day care, 8; bookkeeping, 2; food, 4; arts/crafts, 6; entertainment, 1; general merchandise sales, 7; phone answering service, 1; travel/business service, 3; car wash, 1.[64]

Success Stories

Gloria Davis, referred to in the introduction, now operates a designer dress shop. Davis emphasizes that the Fund provides the opportunity to exchange ideas with other aspiring entrepreneurs as the loan proceeds. Davis, one of the Fund's early success stories, explains, "'You have to crawl before you can walk, and [the Fund] is perfect for people starting out. I think it's a good networking system, but I have to laugh when people ask how [the Fund] helped me because now we're helping them.'"[65]

For Monica Sargent, Davis's cousin and business partner and formerly a low-level secretary who put together gift baskets and sold them to workers at her office, the Fund's process was long but well worth it. The Neo Emporium boutique has given a new look to the neighborhood. The back room of the store needed painting (as of the summer of 1990), but it's where all the sewing will take place. According to Sargent, a chance at financial freedom is worth a little spilled paint. While Sargent has fulfilled her loan obligations to the Fund, she remains committed to helping other women achieve their dream. "'They have helped me," she notes. "I would also like to see designing women succeed also, to see them through.'"[66]

The Neo Emporium shop has entered into consignment arrangements with other Fund participants. Norma Quintana, who sews children's clothing, had not received her loan (as of the end of 1990) to buy a sewing machine, but Davis had commissioned her to sell her clothing at the Neo Emporium.[67]

Sherry Box was in the process (as of the summer of 1990) of developing a temporary service for seamstresses. She wants to use her Circle of seamstresses and designers, aptly named "Designing Women," and her 20 years of sewing knowledge, to become the Kelly Girl of the rag trade. Although barely past the flier stage, with the help of her Circle and a consignment contract with the Neo Emporium, she is doing what it takes to make it. Ms. Box looked forward to the assistance and communication with other women entrepreneurs. Ms. Box related, "'I've been sewing for years, you know, things like prom dresses and wedding dresses and things, and I have always wanted to work for myself.'"[68]

Nelida Medina used her first Fund loan in May 1989 to buy a small freezer and a machine to puree vegetables. Medina, who dreams of owning her own restaurant, was just starting out. Although getting the business started was difficult, Medina noted, "`The best benefit [of the Fund] has been being able to come here, let yourself be known and meet other people and their projects.'"[69]

Rural Microenterprise Projects

In addition to the Full Circle Fund, there are other peer group lending programs that focus on rural communities. These include the Good Faith Fund in Arkansas, created by the Southern Development Bankcorporation,[70] and three North Carolina-based funds, Mountain Micro Enterprise Fund, NEED Micro Loan Fund, and WICA Micro Enterprise Loan Fund[71]. Microenterprise projects in native American communities include the Lakota Fund in South Dakota[72] and the First People's Fund in Canada, a private sector initiative of The Calmeadow Foundation.[73]

Microenterprise in the Ghetto

This paper focuses on microenterprise's potential to stimulate self-employment and economic independence in America's blighted inner city communities. Can the Grameen Bank model work in ghettoes marked by pervasive crime and drug abuse, social disintegration and welfare dependency? This section examines some of the main obstacles to fostering microenterprise development in underclass communities.

The "Skimming" Argument

First, skeptics argue that only a small percentage of inner city residents are risk-oriented. These critics contend that because the microenterprise model is inappropriate for vast numbers of persons, it does not provide a viable, long-term approach to overcoming dependency and poverty. Small-scale enterprises will not achieve the impact on income and savings that has been achieved in the Third World context.

Clearly, microenterprise alone cannot untangle the web of problems that bedevil America's inner cities. Until we try, we do not know how many people may benefit from access to credit and peer support. We do know, however, that the spirit of enterprise currently is alive and well in the inner-city. The urban working poor have a long-standing culture of self- employment.[74] People barred from the mainstream economy for lack of academic credentials are especially apt to turn to self-employment. The challenge now is to broaden the base of the entrepreneurial culture that already exists in poor communities.

If even a small percentage of inner city residents form microenterprises, the social utility of these ventures will be multifold. Self-employment provides economic and social benefits for individuals, families and communities. It leads to the development of such personal assets as leadership ability, self- confidence, and economic literacy. The availability of loan funds and accompanying training opens borrowers' lives to choices and options they otherwise would not have had. As inner city individuals move into new activities, they have the opportunity to take risks society has assumed are beyond their grasp. The children of micro entrepreneurs are exposed to models of self-sufficiency and ownership, rather than to the social worker or government bureaucrat. Income generated by self-employment enables people to take more control over their lives. For example, some inner city parents find they can send children to parochial schools.[75]

Micro entrepreneurs also help to generate legal economic activity in low-income neighborhoods, fostering community pride and cohesion and a general spirit of betterment.[76] In short, creating an entrepreneurial culture in America's inner cities can empower individuals and begin to change perceptions about the choices and options available to them.

Lack of Demand for Goods and Services

Critics of microenterprise argue that most U.S. cities have inadequate informal markets for goods and services.[77] Specifically, these skeptics argue that home-based businesses in U.S. cities face competition from larger entities and businesses with storefront locations. They view the U.S. economy as dominated by technology and subject to low-wage foreign competition.

Despite the presence of established, large-scale firms, one can discern the existence of marketing niches for microenterprises in urban areas that will permit the development of a secure customer base. An unmet demand exists for goods and services in a variety of areas, such as home and auto repair (from simple repairs and painting to electrical, plumbing, and carpentry work as well as television, video, and appliances); child and elder day care; health and environmental services; computers and information services (word processing); clothing (tailors and dressmakers); and, crafts and food (for example, catering, specialty foods,).[78] Many inner city residents have the ability to organize a successful sales network among friends, relatives, neighbors, and members of religious institutions. In addition, microenterprise lenders can assist new ventures in developing marketing strategies, linking complementary businesses, and implementing collective work arrangements.[79] Although marketing in the U.S. generally requires a high level of sophistication, inner city dwellers should be able to develop a wide array of goods and services to substitute for those imported into urban areas as well as for export outside the inner city.

Are Small Ventures Viable?

Even if small ventures get off the ground and develop market niches, will micro-entrepreneurs be able to generate a sustained and sufficiently high income level?[80] Studies indicate that even relatively small amounts of capital can enable enterprising poor people to overcome a significant barrier to starting or expanding a business. For example, in a statewide survey of female business owners in Maine, 29 percent of the respondents started their businesses with less than $1,000 and another 26 percent started with between $1,000 and $5,000.[81]

Micro-entrepreneurs with the highest prospects for success are those who have "an ear to the ground," who can sell, and who can be flexible and change with the market. Microenterprise development should focus on cultivating and translating individual talents and skills into goods and services that can sell in urban communities. What sells? Small, low priced, less fancy items (for example, jewelry in the $3 to $5 price range), general merchandise, items which will be purchased over and over again. Highly detailed and expensive handcrafted items simply will not make it.[82]

In addition to yielding economic self-sufficiency for some, others will use self-employment income to supplement wages from jobs.[83] Access to credit, even if it does not lead to long-term self-employment, often provides a stepping stone to economic advancement. The experience of starting a microenterprise and repaying a loan improves an individual's readiness for salaried employment. Similarly, participation in a borrowing group enables members to establish or improve their credit history by demonstrating the ability to manage business and repay debt.

Legal Barriers

Federal, state, and local laws and regulations pose a serious obstacle to microenterprise development. Barriers to self-employment include: 1) welfare regulations; 2) public housing rules and regulations for housing subsidies to low-income individuals; and, 3) municipal limitations or prohibitions on home-based businesses.

In 1935, the Aid to Families with Dependent Children (AFDC) program was adopted as part of the Social Security Act to enable single parents to remain out of the work force so they could fulfill their domestic responsibilities.[84] AFDC regulations, namely, asset levels as well as health insurance and child care provisions, make difficult the transition from welfare dependency to economic self-sufficiency.

AFDC's rigid asset and income limits make it almost impossible for a recipient to become independent through self-employment. Those receiving AFDC generally cannot accumulate more than $1,000 in personal assets or they will lose their eligibility.[85] Because it does not distinguish between personal and business property, the $1,000 asset limit also discourages business start-ups.

To encourage entrepreneurship among the welfare poor, the assets limit should be raised.[86] The cap precluding borrowing working capital or buying equipment and inventory for a microenterprise should likewise be raised. States should also emulate the Internal Revenue Code and permit a depreciation allowance for equipment in determining the value of a small business.[87] Self-employed people may also require an automobile for business purposes. The $1,500 cap does not allow an AFDC recipient to own or buy a car suitable for regular use in business activities.

AFDC rules also include stringent income eligibility levels. In determining an AFDC recipient's income level, federal law requires welfare officials to disregard a flat monthly amount (a so-called standard disregard) of $90 to cover all work-related and business expenses (for example, transportation, clothing, travel, and parking).[88] However, a self-employed person needs a higher disregard amount for transportation, auto repairs, and clothing.

AFDC recipients also face the threat of losing Medicaid (health) and child care benefits. Termination of AFDC often results in termination of Medicaid even if a family does not have private insurance. Microenterprises generally do not generate an immediate, sufficient income for an entrepreneur to purchase private health insurance to replace Medicaid. To meet this gap, the Family Support Act of 1988 provides transitional Medicaid coverage for twelve months after AFDC payments cease because of employment.[89] The Act also requires a state to "guarantee" child care for 12 months after a family loses AFDC eligibility because of employment or increased income, subject to a fee requirement, provided the child care is needed for the parent's continued employment.[90]

Affordable health insurance remains a problem for people continuing self-employment as their primary source of income. In a self-employment demonstration project for welfare recipients in Illinois, none of the recipients relying on self-employment as their primary means of support could obtain affordable health insurance.[91] Microenterprise lenders should explore the possibility of using the group savings account as an emergency fund and as a mechanism to fund group health insurance coverage.

Public housing regulations and federally subsidized housing also contain stringent income eligibility rules. For example, the Housing Act of 1937 provides housing assistance (subsidy) payments to participating owners on behalf of eligible tenants for very low-income families at rents they can afford.[92] Very low-income families are defined as those families whose income does not exceed 50 percent of the medium income for the area as determined by the Housing and Urban Development Agency (HUD) with adjustments for smaller and larger families.[93] The Housing Act also offers public housing for lower-income families,[94] defined as those families whose income does not exceed 80 percent of the HUD determined median income for the area.[95] A family that exceeds the income limits loses the subsidy or the ability to occupy a public housing unit.

Program administrators, as well as local housing authorities, need to develop transitional eligibility standards to enable people to make the progression from dependency to economic self-sufficiency.

Municipalities often limit or prohibit home-based businesses. Home occupation ordinances seek to regulate potential abuses such as long hours, poor working conditions, child labor, wage exploitation, and lack of benefits. They also seek to balance the worker's needs with those of the residential community. Such ordinances typically permit only customary or traditional home businesses.[96] They also confine the home business to a limited percentage of the residential space, limit the number of nonresident employees, and restrict the type and size of equipment used.[97] Local governments justify these restrictions as reasonable, the standard governing use of zoning power.[98]

Such restrictions, however, impede microenterprises. Low-income persons necessarily must rely on their homes to curb start-up costs. Restricting equipment may frustrate microentrepreneurs in the mechanical or food industries. Although a fear of "sweatshop" home-based industry may be valid, particularly in the needle trades, local governments must reconsider and remove obstacles that impede home- based small business development.

Fostering microenterprises requires acknowledgment and modification of federal, state, and local barriers and disincentives. If self-employment is to be a viable route to self-sufficiency and decreased dependence on government budgets, policy makers must create regulatory conditions favorable to generating a livelihood through self-employment.

Cultural Differences

Different geographical and cultural realities also complicate the task of emulating the Grameen Bank model in America's inner cities. High population density and a relatively homogeneous pool of borrowers may underpin the Grameen Bank's successes. Communities in Bangladesh are very stable and the borrowers share a common cultural and social background.[99] In U.S. cities, borrowers may be spread out geographically. This lack of concentration undercuts the high borrower-to-staff ratio that results in lower transaction costs for the Grameen Bank. This suggests a need to cluster borrower groups in specific inner city neighborhoods.

A considerable degree of cultural diversity characterizes many U.S. inner cities. In areas with public housing, single women with children have relocated from different parts of the city and maintain networks of relatives and friends in their old neighborhoods. These factors may make it difficult to establish stable, geographically-proximate borrower groups, consisting of individuals who know and trust each other. To overcome these cultural and geographical barriers, as well as the anonymity which characterizes modern urban America, enterprise agents/outreach workers must devote additional time and energy to organizing stable borrowers groups.

The multicultural nature of U.S. urban neighborhoods may also complicate the organization of Grameen-style centers or clusters of groups. The centers comprise a key aspect of the Grameen approach because they facilitate cost-effective lending by reducing administrative costs and may also provide the "structural basis for efficient grassroots banking and for community development activities."[100]

In addition to the difficulty of finding a location for center meetings, U.S. borrower groups may resist the idea of meeting at a center with other groups. Borrowers may prefer the smaller, close-knit support groups. Furthermore, mixing groups with different ethnic compositions from diverse neighborhoods encounters resistance.[101]

If the key aim of the center concept is to reduce administrative costs while operating within the multicultural context of urban America, alternatives to bi-weekly center meetings should be explored. They might include: (1) alternating between bi-weekly group meetings and center meetings; (2) permitting a borrower group to conduct bi-weekly meetings on its own to establish a good working relationship between group members before the group joins a center; (3) replacing the bi-weekly center meetings with regular meetings of group chairs and giving them additional powers; (4) replacing the bi-weekly center meetings with quarterly or semi-annual general meetings (being aware of ethnic and community factors) to provide networking opportunities. In the last three alternatives, the circle chair would collect funds and bring them to a central repayment location.[102] Another possibility is to gather various groups in a central location (within ethnic and community constraints) to promote ease of loan repayment, but give groups the option of meeting separately.

Micro-Entrepreneurship: The Broader Issues

Even if the obstacles outlined above are surmounted, in order for microenterprises to blossom in the inner cities, various structural, capital, and urban problems must be addressed.

Microenterprise won't just happen by scattering small amounts of credit around inner city communities. Lenders must be prepared to offer prospective borrowers training and counseling before they offer money. For example, at the

Micro Enterprise Capital Corporation in Washington, D.C., the first for-profit micro bank in North America, prospective borrowers must complete a three-month series of courses in budgeting, finance, and marketing.[103] The Workshop for Business Opportunities in New York provides not only technical instruction, but also self-enhancement training for minority self-employed entrepreneurs.[104] The public sector could offer assistance in this area. For example, publicly-supported educational institutions could offer free entrepreneurship classes. Publicly- sponsored programs could furnish technical assistance for both the borrower and the counsellor.[105]

Microenterprise lenders also should join hands with nonprofit and public sector community organizations and networks to achieve the volume of borrowers necessary for cost-effectiveness, and to provide borrowers with access to training, educational and social services that enhance the likelihood of success. For example, access to microenterprise loans could be linked to a public or nonprofit literacy program.

Public sector organizations such as the U.S. Small Business Administration could create their own microenterprise lending programs[106] or provide funds to nonprofit (or profit-oriented) lenders. Commercial banks should be involved in loan programs as participants in providing funds or loan guarantees. This will expand access to credit and make banks more familiar with the capabilities and needs of microenterprises. It will allow micro-entrepreneurs to develop a business relationship with a commercial bank. To encourage commercial banks to get involved, government can reduce their risks by creating microenterprise loan guarantee funds.

Microenterprise lenders should also consider three further goals. First, micro bankers should consider a social development program similar to the Grameen Bank's "Sixteen Decisions," designed to motivate group members with discipline, unity, hard work, courage, and improved living standards.[107] Second, micro bankers should consider building discussion of and counseling for drug and alcohol problems into group sessions. Third, micro bankers should give special consideration to allocating credit to teenagers and individuals in their early twenties.

If the social aim of microenterprise development is to liberate the human potential trapped in America's inner cities, it seems unlikely that merely relying on the market will turn the tide. Although the credit supplied by micro bankers provides the possibility of self-employment, microenterprise loans deal with only one aspect of an interrelated web of decay and despair. Entrepreneurs will help propel a renaissance of the inner city, but entrepreneurship by itself likely will not replace a pervasive welfare culture.

Overcoming the legacy of dependency and the isolation of poor people in ghettos requires a renewed emphasis on quality of life factors, such public safety, infrastructure, schools, and housing. Many inner cities are undesirable areas for businesses. To summarize the obvious, businesses (as well as residents) face a number of significant problems ranging from crime and fear for personal safety, deteriorating infrastructure, a populace lacking job skills and work experience, and a welfare system that often makes work a losing proposition.

The private financial sector can make a significant contribution to the concept of microenterprise development. Privately owned banks, such as Shorebank Corporation in Chicago and the Southern Development Bancorporation in Arkansas, foster community enterprise and stability, and offer a model of the job-creating potential of bank holding companies.[108] This type of bank extends credit to locally owned and operated businesses and bolsters a low-income community through housing loans. For example, Shorebank has succeeded in stemming the decline of Chicago's South Shore neighborhood through a program of loans to increase home ownership and rehabilitate apartment buildings occupied by low- and middle-income families. Estimates are that Shorebank's loans led to the rehabilitation of approximately one- third of the South Shore's buildings.[109] Furthermore, in the South Shore neighborhood crime is down; the black middle class is staying. Entrepreneurs who renovated the apartment buildings financed by Southbank serve as "gatekeepers" for the community.

Other functions performed by a bank holding company include managing a technical assistance arm to provide business services (such as, accounting, marketing, and planning) to borrower companies.[110] Through a real estate development corporation, a holding company also functions as a real estate developer to assemble land and develop properties for use as business incubators, as well as low and moderate-income housing.[111] A venture capital arm provides equity investments in larger locally-owned firms and a seed capital fund for loans to new and expanding businesses.[112]

As one observer notes, "Shorebank demonstrates the power of combining the investment methods of the private sector with the social goals of the public sector."[113] Critical to a private bank's growth is its ability to attract deposits from institutions and wealthy investors who support community renewal programs. Obstacles, however, remain.

Shorebank has not proven sufficiently profitable to convince others to imitate its successes. Government can help by becoming an equity investor in private development banks and by steering public deposits to them.

Innovative public sector policies are needed to break the cycle of dependency. As writer David Osborne points out, "[t]o create a healthy market, [the] entire constellation of social pathologies, unskilled labor, and inadequate services must be altered. And if that is to happen, government must play a central role."[114] Osborne calls for "reinventing" government's role in assuring opportunities for citizens:

> [t]he necessary elements include investment capital; management assistance for local businesses; infrastructure investments; improved services, such as crime control, housing, and education; significant job training and adult education; and efforts to help people on welfare get training and jobs. And it is essential that community members benefit not just as employees but as owners - - through tenant co-ops, community organizations, and old-fashioned home and business ownership.[115]

Many public sector reforms are on the horizon. Two are especially noteworthy. First, despite the fierce opposition from an entrenched educational establishment, school choice is coming.[116] This will enable parents to choose the schools their children attend, thereby creating competition for the tax dollars that go with those children. Second, Congress recently has given public housing tenants greater power in managing public housing facilities.[117] Some tenants may also purchase public housing if they participate in a resident management program.[118] Conversion of public housing units to cooperative ownership provides low-income families with the opportunity to experience the benefits of ownership, and can expand the asset base in inner city communities.[119]

The public and nonprofit sectors also should continue to provide and expand remedial education, occupational skill training, youth apprenticeships, job-readiness training, and job placement services. These activities are essential to help improve the job prospects of the distressingly large proportion of ghetto residents who lack the requisite skills, work habits, and educational credentials to obtain gainful employment.

National Legislation

Finally, the federal government should foster the spread of microenterprise development programs. Ironically, Washington spends more on microenterprise activities in foreign countries than in the United States.

Rep. Tony P. Hall (D-OH), chairman of the House Select Committee on Hunger, has introduced an omnibus anti-hunger bill (H.R. 2258) that promotes microenterprise both as a way to help low-income people leave public assistance and as a tool for state and local economic development.

The bill would set up community-based, public- private programs to provide access to credit, business and marketing assistance, and general support for borrowers, including child care and transportation. It would be financed by diverting one percent of federal economic development funds -- from Community Development Block Grants, the Rural Development Administration, and the Small Business Administration -- to microenterprise.

The Hall bill also modifies AFDC rules that penalize self-sufficiency. It changes net worth and income rules and enables participants to keep their welfare, food and health benefits while developing a microenterprise. And, in order to promote economic development, the proposal authorizes the Secretary of Labor to set up $1 million competitive grants to 10 states to develop microenterprise programs for the poor over the next five years.

Conclusion

The rise of an urban underclass over the past 20 years presents a seemingly intractable form of poverty. The problem extends beyond the grim statistics of unemployment and underemployment to even more dismal accounts of violent crime, drug addiction, teenage pregnancy, broken families and an abysmal public school system.

What hope exists for reversing the isolation and demoralization of America's inner city poor? Clearly, the existing social safety net is not enough; the situation cries out for new and radically different approaches. Microenterprise development is one such approach; not a panacea but an alternative that focuses on the capacities of the poor, not their deficiencies. It is truly an empowering strategy -- one that seeks to restore individual initiative, responsibility and dignity. Microenterprise should be one of an array of new progressive approaches for liberating the poor from poverty and dependence.

About the Author

Lewis D. Solomon is Professor of Law at The George Washington University National Law Center. He has written, co-authored, or edited 16 legal texts, nearly 50 articles, and several monographs. A frequent guest professor, panelist and presenter at universities and professional organizations worldwide, Solomon concentrates particularly on corporate law and taxation policy. He has also consulted for the Government of Poland and many American municipal governments.

Notes

1. *An expanded version of this paper will be published in Volume Fifteen, Issue One of The Harvard Journal of Law & Public Policy (1992).

See generally S. Steele, The Content of Our Character (1990) (emphasizing the need for hard work, stable family life, individual initiative, and self reliance). See also J. Sleeper, The Closet of Strangers: Liberalism and the Politics of Race in New York (1990).

2. In general, nonprofit organizations are classified by their restriction on any distribution of profits or dividends to constituents. See, e.g., Model Nonprofit Corp. Act 17.07 (Exposure Draft 1986). Arguably inefficient because of a lack of a profit incentive, nonprofits nonetheless continue to thrive on a variety of contexts. See generally Hansmann, "The Role of Nonprofit Enterprise", 89 Yale L.J. 835, 840 (1980) (providing a paradigm to classify the myriad types of nonprofit organizations). This viability may be explained because of the private sector's inability to assure consumers that payment actually produced the desired good or service, id. at 847, such as in the donative setting, and the public sector's inability to adequately meet specialized demand, B. Weisbrod, The Nonprofit Economy (1988). The microenterprise loan fund meets both rubrics in that the enterprise can operate without reducing the total funds available for the borrower, and may partly satisfy a void left by government inefficiency.

3. Southern Growth Policies Board, Creating an Entrepreneurial Culture: Microenterprises in the Southern Economy 5 (April 1990).

4. H. de Soto, The Other Path: The Invisible Revolution in the Third World (1989) (documenting the success of the burgeoning free enterprise class in Lima, Peru); see also Annis & Franks, "The Idea, Ideology and Economics of the Informal Sector: The Case of Peru", Grassroots Dev. 13/1 1989, at 9 (finding Peru's informal economy to be its most viable alternative toward economic stability).

5. De Soto points out that most of these services operate illegally because Peruvian law is riddled with mercantile based requirements and obstacles hindering individual initiation. Bailey, "The Right Path", Forbes, Jan. 23, 1989, at 81.

6. Staff Report of the Select Comm. on Hunger, 100th Cong., 1st Sess., "Access and Availability of Credit to the Poor in Developing Countries and the United States" 2 (1988) [hereinafter Staff Report]. See also Aeppel, "Helping the Developing World - One Entrepreneur At a Time", Christian Sci. Monitor, Mar. 20, 1987, at 1.

7. Strassman, "Home-based Enterprises in Cities of Developing Countries," 36 Econ. Dev. & Cultural Change 121, 125 (1987-88).

8. Staff Report, supra note 6, at 3.

9. Otero, "Rethinking the Informal Sector", Grassroots Dev., 13/1 1989, at 4. Otero notes that while women may comprise up to 60% of the informal work force, they are concentrated in traditional domestic activities, which are least profitable.

10. Rigid collateral requirements, credit guarantees, and inflexible repayment schedules make it difficult, if not impossible, for microenterprise borrowers to obtain credit from formal financial sources. Females, in particular, who often lack collateral or access to guarantees, find themselves disadvantaged because of the strict requirements imposed by institutional lenders. More generally, commercial banks regard loans to microenterprises as too risky and costly to administer. Small-scale informal enterprises, which are not formally registered businesses, may automatically be deemed uncreditworthy. Substantial transactional costs, in terms of time and effort, deter aspiring micro-entrepreneurs from obtaining credit. Furthermore, the overwhelming percentage of the population of most Third World countries lacks the literacy requisite for bank transactions.

11. Yunus, "The Poor as the Engine of Development", 10 Wash. Q. 139, 142-43 (Autumn, 1987). Cash also enables the informal worker to select better quality materials more likely to sell, increasing sales volume and money earned. Otero, supra note 9, at 5.

12. Staff Report, supra note 6, at 41; see also Otero, supra note 9, at 5.

13. Farnsworth, "Micro-loans to the World's Poorest", N.Y. Times, Feb. 21, 1988, 3, at 1, col. 2.

14. Yunus, "Perspectives on Houston Summit", L.A. Times, July 9, 1990, at B5, col.4.

15. A 16% annual interest rate is comparable to the rate charged for agricultural loans by other Bangladesh banks. The interest payment, however, is 8.12% of the loan as repayment is amortized over fifty weeks. See infra note 31 and accompanying text.

16. Staff Report, supra note 6, at 9.

17. Staff Report, supra note 6, at 41 (65%); Yunus, supra note 11, at 145 (74%); Tempest, "Breaks Many Rules," L.A. Times, Nov. 28, 1987, at 1, col. 1 (about 80%). In 1986, females constituted 74% of the Bank's borrowers and accounted for 69% of outstanding loans. Hossain, "Credit for Alleviation of Rural Poverty: The Grameen Bank in Bangladesh", (Int'l. Food Policy Research Inst. Rept. 65, Feb. 1989).

18. Tempest, supra note 17; see also Hossain, supra note 17, at 34; Cohen, "How Far Can Credit Travel", 21 Econ. Dev. & L. Cent. Rep. 5 (1990).

19. Yunus, supra note 11, at 144-45.

20. Staff Report, supra note 6, at 42, 44. Hossain points out that when women do borrow funds for trading, they usually engage in shopkeeping within the home. Hossain, supra note 17, at 36.

21. Cohen, supra note 18, at 7. While Cohen acknowledges the concrete impact of the Bank on its female borrowers, she questions the Bank's broader impact on the social, cultural, economic, and political environment. Id.

22. Staff Report, supra note 6, at 42, 44.

23. Hossain, supra note 17, at 39-41. A factor behind the failure of the collective enterprise may have been adherence to the weekly loan repayment schedule, which may not suit relatively long-term fixed investments. The Bank currently has taken direct responsibility for initial management of these collective enterprises through joint ownership with borrowers. Id. at 79.

24. Yunus, supra note 11, at B5, col. 4.

25. Other factors contributing to the bank's laudable repayment success include (1) the ability of the Bank to confine services to only the most needy; (2) an intricate management system including a decentralized structure and intense training of Bank employees; (3) collection of repayment in small amounts suitable to the circumstances of the poor borrower; and (4) the attitude of the Bank employees who view their work as an opportunity to serve the poor rather than as merely a means of income. Hossain, supra note 17, at 10.

26. A five member group ensures mutual trust and confidence as well as responsibility. Through early experimentation, individual loans proved to be uncontrollable for Bank staff, and groups greater than five failed to foster the crucial group cohesion. Hossain, supra note 17, at 25.

27. Staff Report, supra note 6, at 10-11, 42. In addition to attending a training session, the group elects its officers (a chair and a secretary) and must pass a "test" at the end of the training session before obtaining a loan from the Bank. The members must satisfy the staff regarding their seriousness and integrity, knowledge of Bank's rules, procedures and programs, and demonstrate the ability to sign their names. These weekly meetings also involve a social development component. For instance, members reaffirm and discuss at weekly meetings a program known as Sixteen Decisions, which was introduced by the Bank to imbue members with discipline, unity, and the goal of improved standards of living. Such programs correspondingly improve loan recovery. Hossain, supra note 17, at 27.

28. Sherman, "Micro-Enterprise Lending", 20 Social Policy 64, 66 (Fall, 1989).

29. Id.

30. Hossain, supra note 17, at 26.

31. Staff Report, supra note 6, at 42.

32. Staff Report, supra note 6, at 6; Hossain, supra note 17, at 64-67 (finding that Bank members have incomes significantly higher than those of comparable non-Bank members).

33. Id. However, because traders and shopkeepers are overrepresented as Bank borrowers and agricultural laborers underrepresented, it is unclear how much of the vast income differential is due to initial differences in the composition of the Bank's borrowers and how much to the access to credit.

34. Staff Report, supra note 6, at 42.

35. Staff Report, supra note 6 at 15, 42. The group funds are accumulated in an account held by the Bank and are managed consensually by the group. Hossain, supra note 17, at 26.

36. Staff Report, supra note 6, 42.

37. Mydans, "A Bank Battles Poverty", N.Y. Times, July 12, 1987, Section 4, page 3.

38. Krance, "Banking on the Poor: Bangladeshis Get Credit for Improving Their Lot", Chicago Tribune, October 27, 1987, Tempo Section, page 1.

39. Id.

40. Id.

41. Id.

42. Id.

43. The cost of the Grameen Bank's loan operation is substantially higher than its 16% rate of interest for loans. Hossain, supra note 17, at 75. The high operating costs are not a result of loan loss, which is minimal, but rather stem from administrating an intensive micro-loan portfolio. Hulme, "Credit for Low Income Groups: Some Lessons of Experience", 25 Comm. Dev. J. 175, 177 (1990).

44. Hossain, supra note 17, at 70. Funds deposited by nonmember households constitute an insignificant source. Id.

45. Id. at 74; but see Southern Growth Policies Board, supra note 3, at 7 (stating that the Bank has earned a profit on its lending operation since 1986).

46. Hossain found that the Bank has avoided a subsidy thus far by drawing on a low interest, long-term loan (from the International Fund for Agricultural Development) in excess of its actual needs, and investing these funds in fixed and short term accounts. Hossain warns that adverse

conditions could require the Bank to seek a direct subsidy from the government or increase the borrower's interest rate. Hossain, supra note 17, at 76. Such dependence may present a considerable constraint of expansion and limits the Bank's relevance to those credit institutions which cannot rely on highly subsidized capital. Hulme, supra, note 43, at 175. Other studies recommend that the Bank charge a market interest rate instead of the current 16% rate. Southern Growth Policies Board, supra note 3, at 8. See generally Microenterprise Credit: Joint Hearing Before the Comm. on Hunger and the Subcomm. on Int'l. Dev. Inst. and Fin., 99th Cong., 2d Sess. 17 (1986) (comments of Muhammad Yunus, founder of the Grameen Bank).

47. See Cohen, supra note 18, at 8. For example, dozens of loan groups have organized community schools, gardens, and latrines. Durning, "Action at the Grassroots: Fighting Poverty and Environmental Decline" (Worldwatch Paper 88, 1989).

48. There are numerous organizations and programs offering support for self-employment ventures. See, e.g., The Neighborhood Institute, Self-Employment Circle Loan Fund (summarizing details of low income borrower groups and loan procedures). For a survey of U.S. and Canadian microenterprise lenders, see Corporation for Enterprise Development, Interim Lessons from Self- Employment Programs for the Disadvantaged: A Study of U.S. and Canadian Programs and Policy Perspectives (1990).

49. L. Gellatly, Women's Self-Employment Project: An Overview (1990).

50. Telephone interview, Lewis D. Solomon and Susan Matteucci, Enterprise Agent, Full Circle Fund, January 16, 1991.

51. Women's Self Employment Project, Year End Report on the Full Circle Fund (1990) [hereinafter Year End Report].

52. Gellatly, supra note 49, at 5.

53. Women's Self Employment Project, Fact Sheet, The Full Circle Fund (1991).

54. Telephone interview, Lewis D. Solomon and Susan Matteucci, Enterprise Agent, Full Circle Fund, April 1, 1991.

55. Gellatly, supra note 49, at 7.

56. Year End Report, supra note 51, at 3.

57. Fact Sheet, Full Circle Fund, supra note 53.

58. Gellatly, supra note 49, at 7.

59. Id.

60. Gellatly, supra note 49, at 8.

61. Id.

62. Telephone interview, Lewis D. Solomon and Susan Matteucci, Enterprise Agent, Full Circle Fund, January 16, 1991. See also "Welfare Recipients Go Into Business", Chicago Defender, Nov. 20, 1989 (documenting that 14 of 20 Fund participants no longer receive welfare).

63. See Year End Report, supra note 51, at 9-10.

64. List provided by Susan Matteucci, Enterprise Agent, Full Circle Fund, April, 1991.

65. Wolter, "Women's Self-Employment Fund Coming Full Circle", The Neighborhood Works, December 1990--January 1991, p. 8. See also McCarron, "Boutique Puts Poverty in its Place", Chicago Tribune, September 19, 1990, Chicagoland Section, page 1.

66. McLaurine, "From Rags to Entrepreneurship", Chicago Defender, September 1990.

67. Wolter, supra note 65, at 8.

68. McLaurine, supra note 66.

69. Wolter, supra note 65, at 8.

70. The Good Faith Fund, Fact Sheet (August 1990); Langan, "Helping the Poor Start a Business", Fortune, April 23, 1990, at 18; Gray, "Loan Program Shows Faith in Poor", Newsday, September 2, 1990, Business Section, at 88; Kern, "European Flavor: Southern Development Bankcorporation Imports Ingredients", 4 Arkansas Business Section 1, at 8 (September 28, 1987).

71. Women's Self-Employment Project, Group Lending Exchange, January 1990 Workshop Report, Appendix I - 5 to 6 (Peer Group Lending Programs Statistical File).

72. The Lakota Fund/Circle Banking Project; Morrison, "Grant Aids Lakota Fund", The Rapid City Journal, April 15, 1988, The Lakota Times; "Circle Banking Project: A New Lending Program for the Needy", October 3, 1989, page 3; "Changing Times", Giving Back, January 1990, at 77.

73. Community Information Exchange, Alert #29, May/June 1990, at 2.

74. D.T. Ellwood, Poor Support: Poverty in the American Family (1988).

75. Telephone interview, Lewis D. Solomon and Susan Matteucci, Enterprise Agent, Fund Circle Fund, April 1, 1991.

76. Moffat, "The Self-Employment Debate," in The Self- Employment Strategy: Building the New Economy 57 (1988).

77. See, e.g., Cohen, supra note 18, at 10.

78. See generally, U.S. Dept. of Commerce, "1990 U.S. Industrial Outlook" (1990) (documenting potential opportunity in these and other markets); U.S. Small Business Administration, "Report of the President: The State of Small Business" 14 (1988) (reporting growth in retail, food, health and other industries during 1987- 1988 period).

79. Feit, "The U.S. Experience" in The Self-Employment Strategy: Building the New Economy 37 (1988).

80. Id. at 8.

81. D. Evans & L. Leighton, "Self-Employment Selection and Earnings Over the Life Cycle" 27 (December 1987).

82. Telephone interview, Lewis D. Solomon and Susan Matteucci, Enterprise Agent, Full Circle Fund, April 1, 1991.

83. An analysis of The Independent Business Women Demonstration Program, a self-employment program in Chicago, indicates that 70% of the participants are currently off welfare thereby resulting in an average savings to the Illinois Department of Public Assistance of $2,655 per year per participant. While only 15% of the participants (3 of 20) were able to support their families solely from business activities within a one year period, income from self-employment endeavors, when added to wages from other activities, helped make another 10% of the participants economically self- sufficient. S. Scheinfeld, Final Report on the Independent Business Women Demonstration Program (October 1989).

84. Social Security Act, 42 USC 601-602 (1935). For an analysis of AFDC, see Handler, "The Transformation of Aid to Families with Dependent Children: The Family Support Act in Historical Context," 16 N.Y.U. Rev. L. & Soc. Change 457 (1987-1988).

85. 45 CFR 233.20(a)(3)(B). In addition, under Federal regulations, the equity (fair market value minus encumbrances) in an automobile owned by an AFDC recipient cannot exceed $1,500. Id. In computing the $1,000 asset limit, state AFDC regulations may bar deductions for: (1) depreciation on equipment or other business property or (2) payments on the principal amount on loans used to obtain capital equipment or durable goods. Inventory may be an allowable expense only to replace existing stock, not for expansion purposes. See, e.g., Women's Self-Employment Project, "Illinois Public Aid Policy Barriers and Disincentives to The Self-Employment Initiative of The AFDC Recipient", at 3-4, 10-11, 16 (1986). States generally authorize some business deductions including accounting fees, rent, utilities, advertising, as well as equipment leasing fees thereby forcing AFDC recipients to lease their business equipment. However, legal fees, payments on loans to buy equipment, travel costs, inventory expansion, and auto repair expenses, generally are not considered before an AFDC grant is reduced thereby lessening the chances for gainful self-employment. 45 C.F.R. 233.20(1)(6)(v)(B). This regulation provides that,

For AFDC, with respect to self-employment, the term "earned income" means the total profit from business enterprise, farming, etc., resulting from a comparison of the gross income received with the "business expenses," i.e., expenses directly related to producing the goods or services and without which the goods or services could not be produced. However, items such as depreciation, personal business and entertainment expenses, personal transportation, purchase of capital equipment and payments on the principle of loans for capital assets or durable goods are not business expenses. Id.

86. See, e.g., H.R. 5918, 102nd Cong., 1st Sess., 137 Cong. Rec. H78 (introduced by Congresswoman Cardiss Collins [D. Ill.]) (proposing that income from a family member attributable to a commercial enterprise with five or fewer employees, one or more of whom owns the enterprise, be disregarded for one year in determining aid eligibility).

87. IRC 168.

88. 42 U.S.C. 602(a)(8)(A)(ii) (West Supp. 1990). Furthermore, an AFDC recipient can disregard, net of the standard disregard, an additional $30 per month plus one-third of the remainder of the earned income for such month before calculating the AFDC grant. 42 U.S.C. 602(a)(8)(A)(iv) (1988). However, 42 U.S.C 602(a)(8)(B)(ii)(I) provides that the recipient loses the right to disregard the $30 per month if the recipient has already disregarded this amount for twelve consecutive months while receiving AFDC aid, and recipient loses the right to disregard the one-third remainder if the recipient has disregarded this amount for four consecutive months while receiving AFDC aid.

After a four month transition period, AFDC benefits drop one dollar for each dollar of earnings above a set limit. In forty nine states, a family of three who has worked for more than four months would become ineligible for AFDC at an income below the poverty level; in three-quarters of these states a family would become ineligible at an income that is below 75 percent of the poverty level. Center on Budget and Policy Priorities, Making Jobs Work 4 n.2 (March 1990).

89. The continuation of Medicaid for up to twelve months is divided into two six month periods. During the first six month period, AFDC Medicaid coverage continues, without an income test or payment for the coverage premium. In the second six month period, an earnings-based income test comes into existence and the states may charge a premium for coverage and have the option to eliminate most nonacute care benefits. 42 U.S.C 1396r-6 (West Supp. 1990). See generally Casey, "The Family Support Act of 1988: Molehill or Mountain, Retreat or Reform"?, 23 Clearinghouse Rev. 930 (1989); Congressional Budget Office, "Work and Welfare: The Family Support Act of 1988" (January 1989). See also H.R. 5918, 102nd Cong., 1st Sess. 137 Cong. Rec. H78 (introduced by Congresswoman Cardiss Collins (D-IL) proposing, among other items, a one year extension of Medicaid for individuals otherwise ineligible as a result of income attributable to participation in a commercial enterprise with five or fewer employees, one or more of whom owns the enterprise).

90. 42 U.S.C. 602(g)(1)(A)(ii) (West Supp. 1990). The guarantee of transitional child care benefits expires on September 30, 1998. Pub. L. No. 100-485, 304(b).

91. S. Scheinfeld, supra note 83, at 39 (October 1989).

92. 42 U.S.C. 1437f(o) (1988).

93. 42 U.S.C. 1437a(b)(2) (1988).

94. 42 U.S.C. 1437-1440 (1988).

95. 42 U.S.C. 1437a(b)(2) (1988). Income comprises income from all sources of each household member (42 U.S.C. 1437a(b)(4) (1990)), and

includes the net income from operations of a business or profession (42 C.F.R. 813.106 (1990)). Expenditures for business expansion or amortization of capital indebtedness cannot be used as deductions in determining net income (Id.).

96. J. Butler & J. Getzels, Home Occupation Ordinances 9 (1985).

97. Id. at 12.

98. Id. at 22.

99. Cohen, supra note 18, at 9. See also, Hossain, supra note 17, at 81.

100. Cohen, supra note 18, at 9.

101. Group Lending Exchange, January 1990 Workshop Report at 6.

102. Id. at 6.

103. "Micro Bankers Help the Poor Make Money", N.Y. Times, Sept. 3, 1990, 2, at 28, col. 5.

104. Wynter, "Workshops are Helping Blacks Become Entrepreneurs", Wall St. J., Dec. 19, 1990, at B2, col. 4.

105. Group lending practitioners should engage in workshops which serve as informational sharing sessions. See, e.g., Women's Self-Employment Project, Group Lending Exchange: January 1990 Workshop Report (1990).

106. Sandler, "Small SBA Loans Planned to Put the Poor in Business", Wall St. J., Dec. 14, 1990, at 132, col. 3 (proposed pilot program).

107. See generally, Ahmed, Rural Bank Takes Economic Reform to Bangladesh Villages, Reuter Library Rep., Dec. 26, 1989; Tempest, supra note 17. The Sixteen Decisions are as follows:

1. THE FOUR PRINCIPLES OF GRAMEEN BANK -- DISCIPLINE, UNITY, COURAGE AND HARD WORK -- WE SHALL FOLLOW AND ADVANCE IN ALL WALKS OF OUR LIVES.

2. PROSPERITY WE SHALL BRING TO OUR FAMILIES.

3. WE SHALL NOT LIVE IN DILAPIDATED HOUSES. WE SHALL REPAIR OUR HOUSES AND WORK TOWARDS CONSTRUCTING NEW HOUSES AT THE EARLIEST.

4. WE SHALL GROW VEGETABLES ALL THE YEAR ROUND. WE SHALL EAT PLENTY OF IT AND SELL THE SURPLUS.

5. DURING THE PLANTATION SEASONS, WE SHALL PLANT AS MANY SEEDLINGS AS POSSIBLE.

6. WE SHALL PLAN TO KEEP OUR FAMILIES SMALL. WE SHALL MINIMIZE OUR EXPENDITURES. WE SHALL LOOK AFTER OUR HEALTH.

7. WE SHALL EDUCATE OUR CHILDREN AND ENSURE THAT THEY CAN EARN TO PAY FOR THEIR EDUCATION.

8. WE SHALL ALWAYS KEEP OUR CHILDREN AND THE ENVIRONMENT CLEAN.

9. WE SHALL BUILD AND USE PIT LATRINES.

10. WE SHALL DRINK TUBEWELL WATER. IF IT IS NOT AVAILABLE, WE SHALL BOIL WATER OR USE ALUM.

11. WE SHALL NOT TAKE ANY DOWRY IN OUR SONS' WEDDING, NEITHER SHALL WE GIVE ANY DOWRY IN OUR DAUGHTERS' WEDDING. WE SHALL KEEP THE CENTRE FREE FROM THE CURSE OF DOWRY. WE SHALL NOT PRACTICE CHILD MARRIAGE.

12. WE SHALL NOT INFLICT INJUSTICE ON ANYONE, NEITHER SHALL WE ALLOW ANYONE TO DO SO.

13. FOR HIGHER INCOME WE SHALL COLLECTIVELY UNDERTAKE BIGGER INVESTMENTS.

14. WE SHALL ALWAYS BE READY TO HELP EACH OTHER. IF ANYONE IS IN DIFFICULTY, WE SHALL HELP HIM.

15. IF WE COME TO KNOW OF ANY BREACH OF DISCIPLINE IN ANY CENTRE, WE SHALL ALL GO THERE AND HELP RESTORE DISCIPLINE.

16. WE SHALL INTRODUCE PHYSICAL EXERCISE IN ALL OUR CENTRES. WE SHALL TAKE PART IN ALL SOCIAL ACTIVITIES COLLECTIVELY."

Group Lending Exchange, January 1990 Workshop Report, Appendix.

108. See "Capitalist Tool: The Good Faith Fund", N.M. Bus. Opportunity News, August, 1988, at 6.

109. Osborne, Bootstrap Banking, Inc., 69, 70 (August 1987).

110. "Boosting Cottage Capitalism", Time, Nov. 5, 1990, at 36.

111. See, e.g., The Neighborhood Institute, Organizational Description. The Neighborhood Institute, a nonprofit affiliate of Shorebank operates a low and moderate income housing development program which includes technical assistance, tenant organization, and housing referrals,

112. Id.

113. Osborne, "A Poverty Program That Works", The New Republic, May 8, 1989, at 22, 25. Another example of this combination is the Arkansas Enterprise Group (Group), a nonprofit affiliate of the Southern Development Bancorporation (Southern). Southern is a specialized bank holding company (launched in part by Shorebank), and funds the Group's microenterprise loan fund known as the Good Faith Fund. The Good Faith Fund utilizes peer group organization to finance self- employment ventures for low income persons without collateral. Southern presents a model of private banking's role in remedying social ills via economic development. Southern Development Bancorporation, The Arkansas Development Bank (1988). See generally The Good Faith Fund, Fact Sheet (1990) (outlining borrower group formation, training, and loan operation); Allen, "Faith, Hope, and Money," The Times, June 3, 1990, at 8G, col. 1; Development Banking: Giving Credit Where Credit is Overdue, Ford Foundation Letter, Nov. 1989, at 4.

114. Osborne, "The Kemp Cure-All: Why Enterprise Zones Don't Work", The New Republic, Apr. 3, 1989, at 21.

115. Id.

116. See J. Chubb & T. Moe, Politics Markets & America's Schools (1990).

117. 42 U.S.C. 1437(s) (West Supp. 1990). This provision encourages increased resident management and affords greater flexibility in use of revenues. For a critique of the concept of converting public housing to tenant ownership, see Schill, "Privatizing Federal Law Income Housing Assistance: The Case of Public Housing", 75 Cornell L. Rev. 878 (1990).

118. 42 U.S.C. 1437(s) (West Supp. 1990). This provision further enables the Secretary of HUD to provide training, technical services, and educational assistance to prepare tenants for ownership.

119. The policy of encouraging the poor to own their own home is an example of the "empowerment" theory. This theory postulates that empowering the poor with choices and opportunities decreases the cycle of dependency. See "Ideas to Help Poor Abound, But a Consensus is Wanting", N.Y. Times, Jan. 29, 1991, at 1. col.1.