



# Opening Opportunities, Building Ownership:

Fulfilling the Promise of  
Microenterprise in the United States

ELAINE L. EDGCOMB  
JOYCE A. KLEIN  
FEBRUARY 2005

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FIELD (The Microenterprise Fund for Innovation, Effectiveness,  
Learning and Dissemination), is a research and development  
organization dedicated to the expansion and sustainability of  
microenterprise development efforts, particularly those aimed at  
low-income Americans. Its mission is to identify, develop and  
disseminate best practices, and to broadly educate policy makers,  
funders and others about microenterprise as an anti-poverty  
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# Acknowledgments

**W**riting this review of the microenterprise development field in the United States has been a challenging undertaking. It is not easy to capture the dynamics of this highly complex and intriguing strategy used by a wide array of community development organizations to alleviate poverty, build ownership and assets among many who have had limited opportunity to develop either, and revitalize local communities. We hope that we have been able to do it justice in seeking to both point out its accomplishments and identify the challenges that lie ahead.

The Charles Stewart Mott Foundation has provided critical and long-term support to the microenterprise field in this country. In its funding and leadership, the Foundation has always recognized the importance of assisting the field's efforts to learn, innovate and raise performance, in addition to funding program services across the country. We are grateful for the Foundation's ongoing support for our work and for this publication. In particular, we extend thanks to our program officers Jack Litzenberg and Sue Peters for their encouragement and insightful perspectives on the industry.

We extend our appreciation to all the microenterprise development programs that participate in MicroTest, our performance data collection project, and whose data and experience forms the basis for many of the findings included in this report. Too numerous to mention here by name, these institutions have provided a great service to the industry by contributing their data to create an aggregate view of both institutional performance and the outcomes of program clients.

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Of course, in any project of this nature, there are bound to be errors and these are solely our own.

**Elaine L. Edgcomb**

**Joyce A. Klein**

## Foreword

**W**hen I spearheaded the Mott Foundation's interest in funding microenterprise in the mid-1980s, I was motivated, in part, by recognition that structural changes in the overall economy were leaving a segment of the workforce out in the cold. As individuals and organizations sought new ways to help those excluded from a growing global economy, self-employment was viewed as a viable prospect.

Indeed, even today, there are forces at play in our economy that are propelling people into entrepreneurship full or part time. Those forces include a decline in the number of livable wage jobs, erosion of the social safety net, an increase in the number of contract employees who receive neither benefits nor job security, and the growing number of immigrants who find it easier to start a business than find a job. Given that these factors aren't likely to disappear any time soon, the trend toward self-employment surely will grow.

And to help those new to self-employment is an industry with some 20 years of experience now behind it. To examine that industry – its past accomplishments, as well as the challenges ahead – the Mott Foundation commissioned this report.

The pages that follow offer a comprehensive look at the field's strengths and weaknesses. But this publication goes well beyond that to clearly articulate a set of directions the industry *must embrace* to ensure stability and sustainability into the future. From my perspective, the industry must become more efficient in delivering credit and training, and meet the test of performance standards. Microenterprise, the movement, grew because it allegedly could lead to the American Dream and help ordinary people achieve extraordinary things. Now it's time to prove that the movement can and will continue to live up to that legacy.

Embedded in this report, too, is a call for all of us who care about this industry to work collectively to build a better case for how microentrepreneurs are, indeed, creating the “ownership society” that the current administration in Washington is now embracing.

In my 20 years of grantmaking in the microenterprise field, I've met literally hundreds of entrepreneurs in communities across the country. I've visited garages, sheds, storerooms, studios, basements and plenty of other places where industrious entrepreneurs were carving, cooking, concocting or creating – all in the name of microenterprise.

The stories I've heard – and the passions expressed in the telling – have stayed with me. It seems to me that these individuals were, indeed, the forerunners of the newly coined “ownership society.” After all, their expressed goal was, more often than not, to grab hold of their future, control their work life and invest whatever time and money they could muster in a small business they could call their own.

What strikes me as I reflect on the Mott Foundation's long-term commitment to microenterprise is not only how many low-income entrepreneurs have managed to create thriving businesses and build critical assets, but also how many of these businesses

grew out of communities decimated by structural unemployment. In such cases, I've often wondered whether microenterprise wasn't, in fact, the only intervention that could have provided jobs and incomes to a population hit hard by a cruel economy.

Moreover, in some places, microenterprises have provided livelihoods to enough individuals that, in effect, they've created a new economy in a regional labor market.

And yet microenterprise must continue to prove itself worthy of support, from both the public and the private sectors. Overall domestic discretionary spending is getting thinner for many social programs, including such long-standing ones as Medicaid, education, job training and, yes, business development. As I write this, there is talk in Washington of eliminating *all* funding for the Small Business Administration's Microloan program, and of making substantial cuts in several other SBA programs that help low-income, minority, female and rural entrepreneurs.

In the face of such cutbacks, the challenges to keeping the microenterprise movement vibrant going forward will certainly grow. And yet, I remind myself that microenterprise has typically relied on local momentum to keep going and growing. Microenterprise programs – whether seated in the cornfields of the Midwest or our nation's inner cities, in border towns or coastal communities – have arisen not because of government fiat or philanthropic will, but because they offer realistic opportunities to aspiring entrepreneurs. Surely there is a message in that for advocates, policy makers and funders alike.

The microenterprise industry has been sustained, in no small part, because local people wanted it to continue. This same local energy should now be harnessed to carry out the recommendations herein.

I am heartened by the fact that the microenterprise movement has lasted for 20 years. This report provides the road map for navigating the next 20 years.

**Jack A. Litzenberg**

Senior Program Officer

Charles Stewart Mott Foundation



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# Executive Summary

**T**he notion that a person can turn a dream into a small business by applying healthy doses of ingenuity, elbow grease and grit has resonated with Americans from the earliest days of this nation. Indeed, there is something so intrinsically appealing about that scenario that more than 22 million Americans are small business owners today – including some 20 million who operate “micro” – or very small – enterprises.

Yet, while the vision of business ownership has deep roots in this country, the microenterprise field, which supports the smallest businesses, is relatively young. Emerging here about two decades ago, it was born first through the efforts of women’s organizations that sought to help women use business ownership to improve their economic situation. Over time, microenterprise programs – which today number more than 500 nationwide – have expanded their focus to provide business training, technical assistance and small loans to such traditionally underserved populations as low-income individuals, racial and ethnic minorities, welfare recipients, refugees, and people with disabilities.

Now as the microenterprise field reaches the 20-year mark, it seems appropriate to examine its current state – and both note its accomplishments and identify the major challenges that lie ahead. This is particularly important as a set of forces in our nation’s economy create opportunities and pressures for small-scale business ownership. Key among those forces are: the declining number of good-paying, middle-class jobs; increased outsourcing and use of temporary workers; the aging of the population; the growing need to balance work and family roles; growth in immigration; and declines in many rural communities.

Indeed, the field can rightly point to a number of significant accomplishments. Today, there are microenterprise programs operating in every state in the union. FIELD’s research on a set of these programs shows that they have successfully served the marginal and disadvantaged individuals the field seeks to assist. Industry leaders have demonstrated that credit-led programs can be run efficiently, effectively, and with a high degree of self-sufficiency, and that training programs can help emerging entrepreneurs gain business skills as well as open and expand businesses. Preliminary analyses also suggest that microenterprise programs can operate cost-efficiently and effectively, although more rigorous analyses are required to document the full social returns on the investments made in these programs.

Research also reveals that many of the businesses owned by clients of microenterprise programs survive and grow over time, and that they increase their income and assets and report increased empowerment. While for some the microenterprise plays a key role in providing household income, for others it is an important complement to wage employment. By giving low-income and disadvantaged individuals more skills and income-generating options, microenterprise provides a means to cope better with the vagaries at the lower-end of the labor market. And, while

most microenterprises remain small, employing only the owner, there is a small subset that grows beyond “micro” in size, and contributes larger numbers of jobs to local economies.<sup>1</sup>

Still, one cannot ignore that there are some serious challenges facing the industry. Training and technical assistance services remain largely subsidized. Because these services are the core of most programs, overall program cost recovery in the industry is fairly low and progress toward self-sufficiency remains slow. Scarce resources and limited cost recovery have affected the industry’s ability to reach larger numbers of microentrepreneurs. The result is that most programs remain relatively small, serving hundreds rather than thousands of entrepreneurs. Indeed, our research shows that at least 10 million microentrepreneurs fit the profile of individuals that microenterprise programs are designed to serve.

Adding to the complexity of this picture are the dramatic changes that have occurred over time in the context in which microenterprise programs operate – including vast changes in financial markets, the overall U.S. economy and the funding environment – as well as in the field’s own knowledge and understanding of what works and what its clients need.

Taken all together, it seems clear that if the field has hopes of solving the twin challenges of sustainability and scale, changes will be required in the design and delivery of products and services, as well as in the organizational structures through which they are offered.

Beyond underscoring some key challenges and necessary changes facing the industry, our research concludes that there are three compelling reasons for funders, policy makers and others to support microenterprise:

- In today’s economic environment, there is a segment of the population for whom self-employment is a necessary – and in some cases, the best – source of employment and income.
- By assisting individuals to build businesses and assets, microenterprise can open wealth and ownership opportunities to individuals who have been excluded from our economy.
- Microenterprises can play a role in the revitalization of local economies.

In sum, we believe that microenterprise development, and microenterprise programs, continue to hold promise in the United States. Yet, we also believe that the ultimate promise of microenterprise will hinge on the industry’s ability to openly and actively embrace a number of critical changes. And, while we recognize that times of transformation, shakeout and restructuring can be difficult, we maintain that this period ultimately could lead to a stronger, more viable industry in the decades ahead.

In addition to identifying promising opportunities going forward, this publication was designed to present a synthesis of the microenterprise field that clarifies its strategic importance, discusses its evolution, and accurately assesses its accomplishments and weaknesses.

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<sup>1</sup>Because only one study of the outcomes of microenterprise programs used an experimental design, the degree to which these benefits were a result of the services received by program clients is uncertain. Yet, the studies show that many clients experienced positive outcomes and ascribe some of their success to program services.

Thus, we begin the publication by explaining the context and scope of microenterprise in the United States and by describing some of the factors driving low-income Americans toward self-employment. Subsequent chapters examine the evolution of the industry; industry performance; and the value of microenterprise to low-income entrepreneurs, including what we know about their experiences. The final chapter not only details four critical challenges facing the industry today, but also articulates a set of new directions for the field.

Specifically, we recommend eight directions – or actions – that could help transform the field and position it for long-term growth and sustainability. While some organizations are already moving in these directions, it is now time for more practitioners, and the support organizations, donors and other stakeholders that assist them, to embrace them as well. They are:

**Direction 1: Improve understanding of the market.** To increase its scale and better define its role for the future, the microenterprise field must gain a better understanding of: the demand for microenterprise services and products among potential customers, the characteristics and preferences of those customers, the competing services in the marketplace, and where there are opportunities for collaboration and/or expansion of services.

**Direction 2: Differentiate and broaden products and services.** Microenterprise programs must continue the trend toward developing distinct products for different types of clients, developing management processes to ensure that new offerings achieve the growth, impact, efficiency and cost recovery goals set for them.

**Direction 3: Restructure the industry for greater scale and depth.** To build a nationwide structure with greater market relevance, impact and economies of scale, the field must reorganize and restructure. Microenterprise organizations must seriously look at a set of possibilities to make themselves stronger including: outsourcing functions; co-branding and distributing products offered by other national, regional or local players; mergers and acquisitions; and strategic alliances.

**Direction 4: Use technology to transform operations.** Microenterprise programs must turn to technology more than ever to achieve their goals. Improved management information systems and communications, and on-line and other distance learning technologies, will be key to the ability of programs to increase scale, expand product offerings and realize efficiencies. Practitioners should look to develop partnerships that can leverage the technological capabilities of other providers or, when possible, implement new internal systems.

**Direction 5: Measure and improve performance throughout the industry.** The field as a whole must dedicate itself to the discipline of pushing on the issues of scale, efficiency and cost recovery, as well as on improving program outcomes. This will require connecting to national efforts that support and enhance performance; making investments in systems and processes necessary to collect, analyze and act on performance data; and educating donors about how they can support and provide incentives for improved performance.

**Direction 6: Develop and support policies that directly benefit microentrepreneurs.**

One means of reaching larger numbers of potential microentrepreneurs is to identify and promote changes in social, legal and regulatory policies that can support or reduce barriers to business ownership. This is an area where policy organizations and trade associations should play a lead role, supported by practitioners.

**Direction 7: Develop new strategies to stabilize and sustain programs.** Making progress toward growth and sustainability will require greater efforts to both increase self-sufficiency and secure more stable sources of support. It is now time for the field to demonstrate its impact through rigorous experimental design research, thereby demonstrating to funders the value of more sustained, multiyear support, and to more entrepreneurially explore avenues for cost recovery and revenue generation.

**Direction 8: Repositioning the microenterprise field.** The very term “microenterprise” may be limiting the field’s ability to attract a broader market, a funding stream and strategic alliances. The industry needs to create new language and messages that better convey the relevance of microenterprise and the role it can play in the redevelopment of local economies.

As we put forth these recommendations and, more generally, in undertaking this review of the field, we believe it is important to state that we are engaged supporters of the industry. For more than a decade, FIELD has worked with U.S.-based microenterprise programs, gathering and reflecting on data on both their program operations and the experiences of their clients – with a goal of identifying leading practices to help the field improve its performance.

There is no doubt that as the industry moves into its next decade, it must continue to learn, innovate and stretch its capacity. Practitioners, working in tandem with new partners in both the private and nonprofit sectors, must play a key role in developing new approaches and in seeking efficiencies in their current work. Funders and intermediaries will play a vital role, both in providing the funding necessary to innovate and grow and in pushing practitioners to higher levels of performance. In addition, policy change will continue to be critical, both in removing barriers that face low-income business owners and in creating structures that provide the financial tools that can help these entrepreneurs achieve higher levels of success and economic security.

In today’s economy, low-income individuals need the option of microenterprise. The microenterprise field has opened it to some; now is the time to take the steps necessary to ensure that it is available to many.

# Introduction

**F**rom the very beginnings of our country, creating and owning a business has been a path to financial success and self-fulfillment. Indeed, as Alexis deTocqueville noted, in describing Americans' pursuit of enterprise, "What most astonishes me in the United States is not so much the marvelous grandeur of some undertakings as the innumerable multitude of small ones."<sup>2</sup>

While the vision of small-scale business ownership is as old as this nation, the microenterprise field is relatively young. Emerging about two decades ago in the United States, it was born largely through the efforts of women's organizations that sought to help women to use business ownership as a means to improve their economic situations. While other small business policies and programs existed to assist small and minority-owned firms, many women found that the services offered did not meet their requirements, and as a result, a new set of programs was created to provide training and credit to these entrepreneurs. Over time, microenterprise programs have reached out to other populations not served by traditional business assistance programs – such as racial and ethnic minorities, welfare recipients, refugees and individuals with disabilities.

During the past 20 years, many forces – including social and economic forces, such as increased corporate outsourcing and immigration, efforts to replicate microfinance models that were successful in developing nations, and increasing public sector recognition and awareness – have supported rapid growth of the field. The microenterprise strategy attracted interest because it represented an emerging approach to social welfare policy that saw low-income individuals not only as beneficiaries and employees, but also as entrepreneurs, savers and investors. Success stories have also fueled public support: every microenterprise program can point to examples of entrepreneurs – many of whom were low-income – who took a skill or idea and grew it into a business that could support a family. And, because business ownership is such a widely held and deeply rooted dream, support for microenterprise programs crosses political lines and can, therefore, tap public sector support.

But, while the field has grown, it also has entered a transitional time. Private giving has been challenged by dips in the securities markets, while state and federal public resources are increasingly constrained. These dynamics threaten the funding streams on which programs depend. At the same time, those seeking to generate support for microenterprise development programs have sometimes focused on their greatest strengths or successes, while ignoring their challenges, prompting critics to point out those challenges and weaknesses – although, in some cases, criticizing the field for falling short of expectations that are in fact inappropriate or unrealistic.

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<sup>2</sup>Alexis deTocqueville, *Democracy in America*; available from [http://xroads.virginia.edu/~HYPER/DETOC/ch2\\_19.htm](http://xroads.virginia.edu/~HYPER/DETOC/ch2_19.htm); Internet.

## **FIELD and the State of the Field**

At this pivotal 20-year point in the microenterprise field's development, it seems appropriate to examine its current state. What have we learned about the ability of microenterprise programs to reach out to individuals who have the potential to operate business, but lack access to key resources? Do programs succeed in helping these individuals start and operate their businesses? Do these businesses survive and make important contributions to the family's well-being? Or, are they destined to be weak and marginal in an economy that appears increasingly dominated by large, low-cost firms? Are microenterprise programs reaching enough of the individuals who could potentially succeed in self-employment? Are they cost-effective or are they an unwise use of public and private resources?

At the FIELD program, we have been working with U.S.-based microenterprise programs for more than a decade.<sup>3</sup> During that time, we have worked with more than 100 organizations, gathering and reflecting on data on both their program operations and the experiences of their clients, seeking to identify leading practices and to help the field to improve its performance.

In undertaking this review of the field, we believe it is important to state clearly that we are engaged supporters of the industry. Our mission clearly states this: FIELD's mission is to identify, develop and disseminate best practices in the field of microenterprise, and to publicize the value of microenterprise as an anti-poverty intervention. Nevertheless, we believe that advancing the reach, stability and impact of the microenterprise industry requires taking a deep and honest look at its strengths, weaknesses and challenges; that is the intent of this paper.

To examine the current state and future directions of the microenterprise industry in the United States, the first chapter of this paper begins with a discussion of the forces that lead low-income Americans to engage in business ownership and the role that microenterprise plays within our national economy. Chapter 2 describes the evolution of the microenterprise field to date, focusing specifically on the key program strategies and services in use by programs today. Chapter 3 outlines what the field has learned about the performance of microenterprise programs: who they serve, how large they are, and their costs and effectiveness in delivering key services. Chapter 4 focuses on the key issue of what research tells us about the outcomes experienced by microentrepreneurs in three key areas: business outcomes, household financial outcomes and non-financial outcomes. Chapter 5 concludes with a discussion of the key challenges and research questions that face the field today.

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<sup>3</sup>FIELD's work began as the Aspen Institute's Self-Employment Learning Project, a multiyear evaluation of seven microenterprise programs. Six years ago, FIELD emerged as the umbrella for a larger set of research, evaluation, grantmaking and other support activities.

## Defining Microenterprise

As we embark on this discussion, it is important to clearly define microenterprise. The microenterprise development industry, along with its trade association, has defined a microenterprise as a business with five or fewer employees that requires \$35,000 or less in start-up capital and that does not have access to the traditional commercial banking sector. From FIELD's perspective, we have often used an additional qualifier or lens for the field, focusing on business owners (or would-be owners) who are low-income, or struggling to make ends meet. While many entrepreneurs who lack access to commercial credit may be poor or struggling economically, not all are. For the purposes of this paper, we will focus largely on the issues confronting lower-income entrepreneurs and the organizations that seek to assist them.

The terms microenterprise and self-employment are both used in this paper, in part because small-scale enterprise activities are measured both ways in our economy: both as forms of businesses (microenterprises) and as a form of employment (self-employment). Self-employment refers to a situation in which individuals work for themselves, rather than for a separate public, private or nonprofit enterprise. Many, although not all, of the businesses owned by self-employed individuals are microenterprises.

Microenterprise development refers to the process by which entrepreneurs start and grow their businesses. Our primary focus in this paper is on microenterprise development programs. As Chapter 2 describes, these are initiatives typically run by nonprofit organizations to assist microentrepreneurs by providing them with a range of services, including technical assistance, training and finance.



Major forces shaping our economy are both “pushing” and “pulling” people toward entrepreneurship. We begin this chapter by looking at those factors in detail, and then offer some perspective on the scope of microenterprise in the U.S. and the market for microenterprise program services.

# The Context and Scope of Microenterprise in the United States

**S**mall-scale enterprise development has always been a core part of the American economy and value system. Yet over time, the structure of our nation’s economy has changed dramatically – and continues to change – affecting the role of microenterprise development and self-employment. In seeking to understand the role and importance of microenterprise development in the United States, it is important to put it in the context of the structure of our economy and the opportunities that exist for individuals at the lower end of our labor market.

This chapter, therefore, seeks to lay out the role that microenterprise and self-employment play in our nation’s economy and within the working lives of low-income families. It begins by describing a set of social and economic forces currently shaping our economy and how these affect both the availability of jobs and the opportunities for small-scale enterprise in the United States. It continues with a discussion of the role of microenterprise development and self-employment within the U.S. economy, and then focuses on the role of self-employment among the specific groups of American workers targeted by microenterprise programs: low-income individuals, the unemployed, women, welfare recipients, the disabled, rural residents, and immigrants and refugees.

## The Economic Context for Microenterprise and Self-Employment

The literature surrounding entrepreneurship clearly recognizes that there are factors that both “push” and “pull” individuals to start a business.<sup>4</sup> “Pull” factors are those that attract individuals to start a business: market opportunities, the desire to work for oneself rather than others, and the potential to make more money than in a wage or salary job. The factors that “push” are negative factors that have to do with diminished choices or opportunities in the labor market: unemployment, discrimination, lack of flexibility, and low wage levels. As our economy changes in significant ways, there continues to be a set of macroeconomic forces that affect the role of microenterprise in the United States – both why people choose it and what the value is that they can derive from it. These forces include:

- ▶ **The loss of well paying, secure “middle class” jobs.** One of the most significant forces transforming our economy today is the ongoing decline of the

<sup>4</sup>Extensive discussions of the academic literature regarding self-employment and microenterprise development can be found in: Margaret S. Sherraden and others, *Kitchen Capitalism: Microenterprise in Low-Income Households - SUNY Series in Urban Public Policy* (New York: State University of New York Press, 2004). See also: Cynthia K. Sanders, “Microenterprise Versus the Labor Market Among Low-Income Workers” (Ph.D. diss., Washington University, 2000).

manufacturing sector and the vast expansion of growth in the service and retail sectors. This change has been well documented and is the result of a myriad of factors including, but not limited to, trade patterns and policies and changes in technology.

For the purposes of this paper, what is significant about these trends is that they have resulted in a decline in the quality of jobs available to less-educated workers. That is: wages have generally stagnated or declined;<sup>5</sup> the potential for advancement and wage growth is diminished; fewer if any benefits are provided; and the tenure of work is less secure.<sup>6</sup> Corporations are increasingly contracting out work that used to be performed in-house. These forces lead individuals to look to microenterprise development as a primary form of employment, as a supplement to a low-paying wage job, or as a form of risk mitigation to guard against the more frequent job and income losses experienced by those at the lower end of the labor market. Workers are forced to be more entrepreneurial – looking to create for themselves new or stronger opportunities for work.

- ▶ **The move to downsize major corporations by outsourcing jobs and relying more heavily on contingent and temporary workers.** This is a related trend to the one above. As U.S. firms seek to remain competitive in world markets and, perhaps, to meet the earnings expectations of the securities markets, they have moved to reduce their workforces by outsourcing and relying more heavily on non-permanent employees. For example, during the most recent economic downturn, private firms have chosen to hire temporary rather than permanent workers when additional capacity is required.<sup>7</sup>

This trend has both a “push” and a “pull” effect on microenterprise development. The “pull” factor is the market opportunities it creates for businesses that can provide services and products to these major firms. In fact, as some of the data presented later in this paper indicate, some of the most remunerative microbusinesses appear to be those that provide business services. The “push” is that those who lose employment due to outsourcing are forced to find new sources of income and some turn to self-employment.

- ▶ **The need for working parents – particularly working women – to balance their working and caregiving roles.** Since 1979, the number of hours worked by wives and married couples with children has increased dramatically.<sup>8</sup> As women have increasingly moved into the workplace, parents are struggling to ensure that they can fulfill both their working and parenting obligations. Self-employment sometimes offers greater flexibility in structuring work hours around school or day-care schedules. In fact, research on self-employed women has found that women often choose self-employment, even when the resulting income may be lower, because it allows them to find a better balance between work and family.<sup>9</sup>

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<sup>5</sup>Lawrence Mishel and others, *The State of Working America 2002-2003* (Ithaca, NY: Cornell University Press, 2003), 127-140.

<sup>6</sup>Mishel, 141-148.

<sup>7</sup>Jared Bernstein, *Jobs Picture* (Economic Policy Institute, 2004); available from [http://www.epinet.org/content.cfm/webfeatures\\_econindicators\\_jobspict\\_20040702](http://www.epinet.org/content.cfm/webfeatures_econindicators_jobspict_20040702); Internet.

<sup>8</sup>Mishel, 109.

<sup>9</sup>Theresa J. Devine, “Characteristics of Self-Employed Women in the United States,” *Monthly Labor Review* (March 1994): 20-33; available from <http://www.bls.gov/opub/mlr/1994/03/art3full.pdf>; Internet.

This may be one force that is fueling the growth in self-employment and business ownership among women. According to IRS figures, the number of non-farm female-owned sole proprietorships grew from 6.13 million in 1995 to more than 6.8 million in 1998 and, in that four-year period, the percent of sole proprietorships owned by women increased from 33.4 percent to 35.3 percent.<sup>10</sup> Women also continue to comprise an increasingly large percentage of the self-employed (increasing from 37 percent in 1995 to 37.9 percent in 2000).<sup>11</sup>

- ▶ **The aging of the population.** Workers over age 50 have a higher rate of self-employment. In 2002, 16.4 percent of the 50-plus workforce was self-employed.<sup>12</sup> Engagement in self-employment peaks at around age 65, both because individuals working in wage employment retire at higher rates than those who are self-employed and because of some shifting from wage work to self-employment. Thus, as the baby boomers move toward retirement, it is likely that the nation will see increasing interest in self-employment. Research has shown that having a limiting health condition is one of the primary predictors of a transition to self-employment among older workers; this may be because it is easier to accommodate the health condition in a self-employment setting.<sup>13</sup>
- ▶ **Growth in immigration.** Business ownership has historically been an important route into the American economy for new immigrants. This is true for both legal and illegal immigrants. For all those new to the country, language and educational barriers can make it difficult to find wage employment; it is even more difficult for those who are undocumented to achieve. Thus, many new immigrants turn to business ownership. For example, interviews conducted by FIELD of Latino immigrants operating businesses in the informal sector found that many of these individuals began working in contingent or temporary wage jobs (often paid off the books). These individuals turned to business ownership in the hope that they could create a more stable and rewarding stream of income.<sup>14</sup> While rates of self-employment among immigrants have recently declined<sup>15</sup> – at least among those immigrants who are captured in government statistics – the continuing entry of legal and undocumented immigrants (estimated to be about 1 million individuals per year<sup>16</sup>) will fuel growth in the overall number of immigrant-owned firms.
- ▶ **Changes in the safety net that seek to require and/or support work.** During roughly the past decade, there has been a major shift in the structure of the U.S. safety net in the form of a move to require recipients of many forms of cash

<sup>10</sup>U.S. Small Business Administration Office of Advocacy, *Women in Business*, 2001 (SBA, October 2001), figure 8, p 13.

<sup>11</sup>U.S. Small Business Administration, figure 7, p 12.

<sup>12</sup>The rate for those self-employed in unincorporated or incorporated businesses for their primary job in the survey reference week. Lynn A. Karoly and Julie Zissimopoulos, *Self-Employment and the 50+ Population* (Washington, DC: American Association of Retired Persons, 2004).

<sup>13</sup>Karoly and Zissimopoulos, 95-96.

<sup>14</sup>Elaine Edgcomb and Maria Medrano Armington, *The Informal Economy: Latino Enterprises at the Margins* (Washington, DC: The Aspen Institute, 2003); available from [http://www.fieldus.org/publications/IE\\_Latino.pdf](http://www.fieldus.org/publications/IE_Latino.pdf); Internet.

<sup>15</sup>Steven A. Camarota, *Reconsidering Immigrant Entrepreneurship: An Examination of Self-Employment Among Natives and the Foreign-Born* (Washington, DC: Center for Immigration Studies, January 2000), 13; available from <http://www.cis.org/articles/1999/selfemployment/selfreport.pdf>; Internet.

<sup>16</sup>Lynn A. Karoly and Constantijn W. A. Panis, *The 21st Century at Work: Forces Shaping the Future Workforce and Workplace in the United States* (Santa Monica, CA: RAND Corporation, 2004), 29.

assistance to work. The most notable was the federal welfare reform in 1996, which created the new Temporary Assistance for Needy Families (TANF) program.<sup>17</sup> In addition to placing time limits on the number of years of assistance, the TANF program provides strong incentives to states to move recipients into work. There also have been moves in other programs, such as those assisting the disabled, to assist recipients to work. Although for many of these individuals wage employment may be the preferable form of work, there are some who seek to pursue self-employment.

The National Survey of America's Families (NSAF), conducted by the Urban Institute, includes a component that collects data on TANF leavers (individuals who are former recipients of TANF assistance). NSAF findings indicate that in both 1997 and 1999, 6.8 percent of working TANF leavers sampled were self-employed.<sup>18</sup> This figure is equal to the national rate of self-employment and higher than the rate of self-employment for women, which was 5.6 percent in 1999.<sup>19</sup>

Within the past 10 years, states have also been increasingly active in creating Vocational Rehabilitation policies that support self-employment. Patterns of self-employment among individuals with disabilities are even stronger. U.S. Census data from 1983 found that people with disabilities were almost twice as likely to engage in self-employment as those without – 14.7 percent vs. 8 percent.<sup>20</sup> Similarly, researchers with the U.S. Department of Labor found that women with disabilities were 1.5 times more likely to engage in self-employment than those without and that men with disabilities were 1.3 times more likely to engage in self-employment.<sup>21</sup> This is so despite the fact that many of these assistance programs – and the systems that support them – do not actively support or encourage self-employment as a form of work.<sup>22</sup>

- **The decline of many rural economies.** A variety of economic and social factors has led to significant declines in many rural areas. While out-migration has been one response to the loss of jobs and farming income, some individuals and families, bound by strong family and cultural ties, choose to remain in their communities. These families often seek to piece together sufficient income from a variety of sources – both wage jobs and small-scale businesses – in order to make ends meet. In these communities, non-farm self-employment plays a critical role

<sup>17</sup>The federal legislation that created the TANF program was the Personal Responsibility and Work Opportunity Reconciliation Act of 1996.

<sup>18</sup>Pamela Loprest, *How Are Families Who Left Welfare Doing Over Time? A Comparison of Two Cohorts of Welfare Leavers* (Federal Reserve Bank of New York: Economic Policy Review, September 2001), 13; available from <http://www.ny.frb.org/research/epr/01v07n2/0109lopr.pdf>; Internet.

<sup>19</sup>These rates are for unincorporated self-employment in nonagricultural industries. See Steven Hipple, "Self-Employment in the United States: An Update," Bureau of Labor Statistics, *Monthly Labor Review* (July 2004): 19.

<sup>20</sup>T. Seekins, *Rural and Urban Employment Patterns: Self-employment as a Metaphor for Rural Vocational Rehabilitation* (Missoula, MT: Rural Institute on Disabilities, The University of Montana, 1992).

<sup>21</sup>Jon C. Messenger and Andrew Stettner, *The Quality of Self-Employment Jobs in the United States* (Geneva: International Labour Office, 2001), 57; available from <http://www.ilo.org/public/english/employment/finance/download/us6.pdf>; Internet.

<sup>22</sup>Although states can find ways to support self-employment, there currently is no specific language in the TANF statute regarding self-employment. For more information on the TANF law as it relates to self-employment, see: Mark Greenberg and Nisha Patel, *Microenterprise Development and Self-Employment for TANF Recipients: State Experiences and Issues in TANF Reauthorization* (Washington, DC: The Aspen Institute, April 2002); available from <http://www.fieldus.org/publications/claspreport.pdf>; Internet.

in creating jobs and income. FIELD's study of informal entrepreneurs in rural Nebraska, as well as research conducted for the U.S. Department of Commerce's Economic Development Administration (EDA), found that microentrepreneurs living in areas of economic distress pursued business ownership because they did not want to leave their communities.<sup>23</sup> The need to create sources of income leads to an increased emphasis on enterprise in many rural communities. For example, a study by the Center for Rural Affairs found that self-employment accounted for 22 percent of total non-farm employment in rural farm counties throughout the Great Plains states and that non-farm self-employment accounted for nearly 60 percent of all jobs created in those counties between 1990 and 2000.<sup>24</sup>

- ▶ **The emergence of niche markets.** Economic and corporate restructuring, as well as changing demographic patterns, create new market opportunities that can be filled by small-scale enterprises. As discussed in this chapter, corporate downsizing has created opportunities for small firms in many sectors, including business services and construction. Similarly, researchers have documented that both the gentrification of urban communities (where higher-income residents demand high-end services, such as specialized carpentry and woodworking or hand-laundry), as well as the emergence of ethnic enclaves (which create demand for food products and other goods specific to a particular ethnic group), create market opportunities that have been filled in part by microentrepreneurs.<sup>25</sup>

Together, these forces help to set the context for individuals' choices to pursue business development.<sup>26</sup> The following section of this chapter lays out what national data sources suggest about how these trends have affected engagement in microenterprise development and self-employment in the United States – both among workers as a whole and among the struggling individuals and communities that microenterprise development programs seek to target.

## The Scope of Microenterprise in the United States

In considering the role and importance of microenterprise development in the United States, it is important to understand its scope – how big is it? How many microenterprises are there and what percent of jobs are found in businesses of five or

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<sup>23</sup>Elaine Edgcomb and Tamra Thetford, *The Informal Economy: Making It in Rural America*. (Washington, DC: The Aspen Institute, February 2004); available from [http://www.fieldus.org/publications/IE\\_Rural.pdf](http://www.fieldus.org/publications/IE_Rural.pdf); Internet.

Lisa J. Servon, *Microenterprise Development as an Economic Adjustment Strategy* (Washington, DC: Economic Development Administration, U.S. Department of Commerce, 1998); available from <http://policy.rutgers.edu/cupr/eda/microcover.pdf>; Internet.

<sup>24</sup>Jon M. Bailey and Kim Preston, *Swept Away: Chronic Hardship and Fresh Promise on the Rural Great Plains*. (Walthill, NE: Center for Rural Affairs, June 2003), 14-15; available from [http://www.cfra.org/pdf/Swept\\_Away.pdf](http://www.cfra.org/pdf/Swept_Away.pdf); Internet.

<sup>25</sup>See, for example, Saskia Sassen, "New York City's Informal Economy," *Institute for Social Science Research* Volume IV, Paper 9, as cited in Jan L. Losby and others, *Informal Economy Literature Review* (Washington, DC: The Aspen Institute, December 2002), 26.

<sup>26</sup>Several research efforts involving qualitative interviews with low-income microentrepreneurs document the role that these forces play in motivating their pursuit of self-employment. See Sherraden, *Kitchen Capitalism*.

Lisa J. Servon, *Bootstrap Capital: Microenterprises and the American Poor* (Washington DC: The Brookings Institution Press, 1999).

Martha Shirk and Anna S. Wadia, *Kitchen Table Entrepreneurs* (Boulder, CO: Westview Press, 2002).

fewer employees? How many businesses are owned by individuals that the microenterprise industry is targeting?

There is no one data set that provides a comprehensive answer to these questions. Thus, to address them, FIELD staff reviewed a range of research and data sets, described in Appendix 1. The Association for Enterprise Opportunity (AEO), the trade association of microenterprise programs in the United States, estimated that in 2001 there were 20.7 million microenterprises in the United States. This estimate includes all businesses with fewer than five employees and is based on data from the U.S. Census Bureau's Non-Employer Statistics combined with data from County Business Patterns, published by the U.S. Department of Commerce.<sup>27</sup> Together, these microenterprises comprise over 86 percent of all enterprises in the United States and contribute 16.6 percent of total nonfarm employment.<sup>28</sup>

Another general estimate of the number of microenterprises can be determined by examining the number of sole proprietorships. A sole proprietorship is an unincorporated business that is owned by one individual. According to the IRS, there were 20,378,335 non-farm sole proprietorships in 2001.<sup>29</sup> This represents a steady increase since 1995 when there were fewer than 18.4 million sole proprietorships. It is important to note that some sole proprietorships have employees and, thus, some of the firms included in this estimate may be larger than microenterprises.

Based on that review, *we believe there are at least 20 million microenterprises in the United States and that this figure is likely an underestimate given the lack of data on the number of businesses operating in the informal sector.*

## **The Market for Microenterprise Services**

While it is important to understand the overall scope of microenterprise activity in the United States, the microenterprise field targets its services largely to those who are underserved or disadvantaged in some way. These include individuals lacking access to commercial credit, living on low incomes, or facing other challenges in the labor market in terms of their ethnic or racial status, gender, or other factors.

In some cases, self-employment among these groups may be more significant, or hold more potential, because of barriers they face in securing and holding wage labor. This is particularly true of the disabled. Having a significant disability can have disastrous consequences on a person's ability to participate in the workforce. People with significant disabilities have an unemployment rate of approximately 70 percent.<sup>30</sup> This is the lowest rate of participation in the workforce and the highest rate of unemployment of any group in American society.

Microenterprise programs also target sets of individuals who face distinct disadvantages in establishing and operating their own businesses. As previously noted, women were an early focus of the microenterprise industry because of the

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<sup>27</sup>The methodology used by AEO was developed by James C. McConnon, Jr. and Thomas Allen of the University of Maine. For more information, see [http://www.microenterpriseworks.org/services/policy/mees/us\\_sheet.htm](http://www.microenterpriseworks.org/services/policy/mees/us_sheet.htm); Internet.

<sup>28</sup>See [http://www.microenterpriseworks.org/services/policy/mees/us\\_sheet.htm](http://www.microenterpriseworks.org/services/policy/mees/us_sheet.htm); Internet. Calculations by FIELD, as described in Appendix 1.

<sup>29</sup>See <http://www.irs.gov/pub/irs-soi/01sp10si.xls>; Internet.

<sup>30</sup>John M. McNeil, *Employment, Earnings and Disability* (Washington, DC: U.S. Bureau of the Census, 2000).

discrimination that they have long faced in both the credit markets and business world generally. Similarly, microenterprise programs target racial and ethnic minorities because many of these individuals face barriers in accessing credit and/or in acquiring the skills and contacts required to engage in business development. The premise behind this targeting is that providing assistance to individuals who face barriers can help overcome the legacy of discrimination and poverty that has led to lower levels of business ownership, particularly among Native Americans, African Americans and Hispanics. In 2003, the self-employment rate among whites was 7.3 percent, while the rates for Blacks or African Americans and Hispanics or Latinos were 4 percent and 5.5 percent, respectively.<sup>31</sup> Rates of entrepreneurship among Native Americans also lagged behind those of whites in states with large numbers of Native Americans.<sup>32</sup> Microenterprise programs reach out to potential entrepreneurs in these racial and ethnic groups, with the goal of enabling them to overcome the barriers they face in starting a business.

Understanding the size of the market that microenterprise programs seek to target is useful, because it can provide insights into the potential demand for the services of microenterprise organizations. Thus, it is useful to further specify these estimates based on additional characteristics of the owner. Table 1 below presents data and estimates on the number of self-employed individuals or microenterprises in many of the key socio-economic and demographic groups targeted by microenterprise programs. These estimates derive from various data sources and research efforts and, in some cases, from estimates made by FIELD

**Table 1: Size Estimates of Key Components of the Market for Microenterprise Services**

<b>Market Segment<sup>33</sup></b>	<b>Number of Microentrepreneurs</b>
Microenterprises with difficulty accessing bank financing	10.8 million
Women-owned microenterprises	5.13 million
Business owners with personal incomes < \$10,000	4.3 million
Low-income self-employed individuals	1.7 million
African American-owned microenterprises	650,000
Hispanic-owned microenterprises	800,000
Asian-owned microenterprises	650,000
Native American-owned microenterprises	170,083
<i>Individuals with disabilities</i>	3.12 million
<i>Welfare recipients who would become self-employed</i>	140,377
<i>Unemployed individuals who would become self-employed</i>	251,430

*Italics indicate the estimated number of individuals (most of whom are currently not working) who would be self-employed given the availability of services and more conducive policies.*

<sup>31</sup>Hipple, 19.

<sup>32</sup>Rates of entrepreneurship among Native Americans vary by state and region of the country. For example, the Corporation for Enterprise Development found that the Native Americans in North Dakota owned businesses at much lower rates than whites, while those in New Hampshire, Alabama, Mississippi and Pennsylvania owned businesses at a much higher rate than whites. See Jennifer Malkin and others, *Native Entrepreneurship: Challenges and Opportunities for Rural Communities*. (Washington, DC: Corporation for Enterprise Development, December 2004), 16.

<sup>33</sup>Note that these components of the market (or market segments) overlap. For example, many of the entrepreneurs who have difficulty accessing bank financing are women or minorities; similarly many low-income entrepreneurs are also likely women or minorities.

staff. In most cases, the estimates are based on survey research on existing businesses. However, for the market components listed in italics, the estimates are based on estimates of currently unemployed individuals who would become self-employed given the availability of services and more conducive policies (see Appendix 1 for a detailed discussion of the data sources on which these estimates are based). *Together, these figures suggest that the market for the targeted services provided by microenterprise programs is about 10 million individuals.*

It is important to note that this figure of 10 million individuals represents the size of the total market that microenterprise programs seek to assist. Not every microentrepreneur in this potential market will demand services from a microenterprise program. Some entrepreneurs who face difficulty accessing bank financing may turn to family and friends for money. Some of these entrepreneurs may already have the skills they need to run their businesses. Many existing business owners may not have the desire to grow their businesses. And, of course, ultimately the demand for microenterprise financing or business advice will depend not only on a business owner's generalized desire for assistance, but also on the specific features and costs of a particular product offered by a microenterprise program. For example, while payday and other alternative lenders may charge exceedingly high prices, they typically offer faster turnaround and more accessible locations than many microenterprise programs. Similarly, while entrepreneurs who are already in business may want assistance in specific areas, such as marketing or pricing, they may not want to sit through a full-fledged training course.

In fact, as Chapter 5 of this paper will discuss in greater detail, one of the critical questions facing the microenterprise industry today is the scope and nature of real demand for microenterprise program services. Although some microenterprise programs are actively developing new products, currently most programs' offerings focus largely on term loans, business start-up training and generalized business technical assistance. Increasingly, there are other sources of business loans and technical assistance in the market place. In articulating its future role, the microenterprise field will need a more detailed understanding of the number of entrepreneurs who would demand their services if they were available and how it can best structure itself to meet this demand.

## Conclusion

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**A**s the previous discussion illustrates, the microenterprise sector is an important component of our national economy. Major economic and demographic forces that are shaping our economy are creating both opportunities and pressures for small-scale business ownership. Many of these trends will likely continue and some will intensify; thus, microenterprise will continue to be an important option for individuals seeking opportunities to create income, work and wealth.

Within the set of individuals who seek to pursue self-employment and microenterprise, there are an estimated 10 million who, for a variety of reasons, lack access to the resources necessary for success – capital, business skills and access to business networks. Microenterprise programs have emerged in this country as a way to provide access to those resources, with the goal of broadening the opportunity for individuals to engage in small-scale enterprise. With almost two decades of experience in this country, now is a good time to revisit the record of these efforts.



The microenterprise field began to emerge in the U.S. in the 1980s. And though it owes a nod to the international microfinance movement, its roots also are entwined with the women's economic development movement, community development strategies and other such efforts. In this chapter we describe the origins of the industry, draw important distinctions between "microenterprise development" and "microfinance," and detail the types of services commonly offered to microentrepreneurs.

# The Evolution of the Microenterprise Industry

Just as the entrepreneurial spirit has had a long history in America, so, too, has the impulse to nurture it with financial assistance.<sup>34</sup> By and large, however, the modern U.S. microenterprise industry is a product of the past 20 years, growing out of a set of movements concerned with providing business development assistance to populations for whom these services had previously been severely limited or unattainable. This chapter will discuss the evolution of the industry in the United States, identifying the earliest innovators that inspired the field's development and summarizing its growth and evolution of program strategy.

While some observers<sup>35</sup> have linked the growth of the industry to interest in emulating the rapidly growing microenterprise field in the developing world, in fact the origins of the U.S. field are much more diverse. Its roots are as much domestic as international; its international influences included both European and developing nation sources. Previous research by John Else has identified five major sources of programmatic experimentation that stimulated the development of the industry in its present form.<sup>36</sup> They include:

- ▶ **Women's economic development organizations.** These emerged in the early 1980s as a response to the limited options that existed for women in both wage employment and business ownership and became alternate sources of business counseling and financing for women at all economic levels interested in business ownership.
- ▶ **Organizations inspired by international microenterprise development strategies used in the developing world.** Seeking to adapt these strategies to the United States, they instituted the first peer-lending programs, as well as adapted individual lending strategies to both urban and rural settings.

<sup>34</sup>Some observers of the history of community development finance in the U.S. trace the roots of microfinance here as far back as the later part of the 19th century. For an interesting analysis of the relevance of the rise and fall of "remedial loan associations" and the historical roots of contemporary microfinance, see Steve Shepelwich, *Remedial Loan Associations: A Historical Contribution to Current Microfinance Practice* (East Lansing, MI: Michigan State University, 2002).

<sup>35</sup>Servon, *Bootstrap Capital*, 3-4, 15-17.

James H. Carr and Zhong Yi Tong, *Replicating Microfinance in the United States* (Washington, DC: Woodrow Wilson Center Press, 2002), 1.

<sup>36</sup>John F. Else, "An Overview of the Microenterprise Development Field in the U.S.," in *The Role of Microenterprise Development in the United States*, ed. John Else and others (Geneva: International Labour Office, March 2001), 7-8; available from <http://www.ilo.org/public/english/employment/finance/download/usover.pdf>; Internet. Else also notes other early innovators in the field including some rural policy centers such as the Center for Rural Affairs in Nebraska and the North Carolina Rural Economic Development Center in North Carolina, both of which implemented programs that became prominent in the late 1980s and early 1990s. Others engaged early on included some Small Business Development Centers, refugee service organizations, community colleges, Head Start programs, employment and training programs, social service agencies, and youth development organizations.

- ▶ **Organizations interested in using the strategy for the unemployed.** Both the Corporation for Enterprise Development (CFED), a policy organization, and the U.S. Department of Labor were inspired by self-employment strategies used with unemployed workers in Europe and launched two U.S. demonstrations.<sup>37</sup> CFED operated the Self-Employment Investment Demonstration from 1988 to 1992, testing self-employment as a self-sufficiency strategy for welfare recipients, and the U.S. Department of Labor initiated demonstration projects that tested self-employment as a re-employment strategy for unemployed workers.
- ▶ **Community development corporations.**<sup>38</sup> They recognized the importance of indigenous business development as a means of addressing increasing structural unemployment. They initiated business counseling and credit access programs and argued for public support for microenterprise development.
- ▶ **Community action agencies.**<sup>39</sup> Also in the 1980s, they identified self-employment as an important option for people with limited opportunities in the labor force. They created demonstration programs with funding from the Office of Community Services of the Department of Health and Human Services as early as 1987.

Although most associated in the public mind with microcredit, the U.S. industry was, as these sources attest, always as much about training and technical assistance as it was about access to credit. Business development was recognized to be a complex process in a nation with a sophisticated market and a complex regulatory environment that demanded a range of support services matched to client experience, stage of business and growth goals.

This reality has resulted, in fact, in the development of two interrelated fields – the microenterprise development field and the microfinance field. As the graphic on page 21 illustrates, they overlap with respect to their interest in providing a range of business financing products to microentrepreneurs, but the larger purposes of each are also distinctive. *Microenterprise development* refers to the process by which entrepreneurs start and grow their businesses and microenterprise development programs assist them by providing a range of services, including technical assistance, training and financing. *Microfinance*, on the other hand, can be understood as the provision of small-scale financing to the working poor. While it includes loans to microbusiness owners, it also focuses on other low-income individuals and may offer a range of lending and savings products aimed at small-scale mortgage or home-improvement financing, educational and consumer needs, emergency loans, and sometimes money transfer. Often labeled

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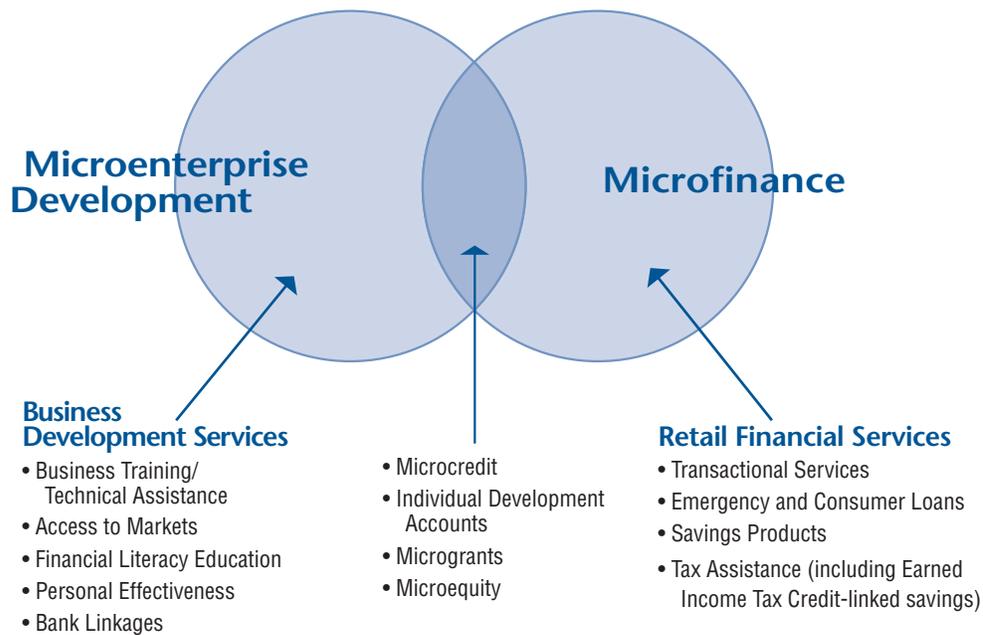
<sup>37</sup>Marc Bendick, Jr. and Mary Lou Egan report that the British and French efforts to support enterprise development through transfer payments to underemployed workers were not successful. They report that these programs turned “less than one percent of transfer payment recipients into entrepreneurs, and an even smaller proportion into successful ones.” See “Transfer Payment Diversion for Small Business Development: British and French Experience,” *Industrial and Labor Relations Review* Vol. 40, No. 4, 1987, 528–542 (quote, 540). Unlike these European programs that provided only payments with limited referrals to optional services, the U.S. projects provided some required counseling and/or classes.

<sup>38</sup>There is no established legal definition for CDCs. According to the National Congress for Community Economic Development (NCCED), they emerged in the 1960s and “are characterized by their community-based leadership and their work primarily in housing production and/or job creation ... CDCs are formed by residents, small business owners, congregations and other local stakeholders to revitalize a low- and/or moderate-income community. ... According to a national census of CDCs conducted by NCCED in 1998, there are an estimated 3,600 such groups across the United States.” National Congress for Community Economic Development, *Frequently Asked Questions*, available from <http://www.ncced.org/aboutUs/faqs.html>; Internet.

<sup>39</sup>Community action agencies were created in the 1960s to provide social services to low-income Americans.

retail financial services, these elements of microfinance are in their early stages of development in the United States. In this sense, the microenterprise development and microfinance fields can be seen as fields that clearly intersect in some ways, but also have distinct purposes and activities.

**Figure 1: The Intersection of Microenterprise Development and Microfinance**



## The Growth of the Industry

From its beginnings in the 1980s, the field<sup>40</sup> has grown dramatically. Starting with a small number of organizations, the industry now has microenterprise service providers across the country, delivering a range of business development and financial services. It has also developed an industry association with more than 400 member organizations, a growing number of state-level associations and financing intermediaries, and several research and policy organizations that focus on raising the visibility of microenterprise development in the United States, generating policy and funding support, documenting best practices, and providing training and technical assistance to implementing organizations.

<sup>40</sup>In describing microenterprise development activities in the United States, this report will use both the terms industry and field interchangeably, as do many practitioners engaged in the work. There are distinctions worth noting in the terms, however. As defined by the Compact Oxford English Dictionary, a “field” is “a subject of study or sphere of activity,” and an industry is “a particular branch of economic or commercial activity” ([http://www.askoxford.com/concise\\_oed/field?view=get](http://www.askoxford.com/concise_oed/field?view=get) and [http://www.askoxford.com/concise\\_oed/industry](http://www.askoxford.com/concise_oed/industry)). The first term suggests an area of work possibly involving research, experimentation and practice (as in the fields of medicine or psychology), while the second connotes organized, business-oriented activity and a set of institutions offering products and services for economic gain (as in the health care industry, which surrounds the fields of medicine and psychology). The Association for Enterprise Opportunity calls microenterprise development an industry (<http://www.microenterpriseworks.org/about/whatis.htm>), and this has some sense as a well-developed structure of implementers, intermediaries and support institutions are now engaged in or surround the work of the field. The paper will discuss both the evolution of practice in the field, as well as the growth of the institutions that are part of it.

This development of the industry had been spurred by the early support of several national foundations that funded not only many of the initial practitioners, but also research documenting program strategies and client outcomes, the development of national- and state-level support institutions, and innovative work in adapting developing-world methodologies to the United States and developing new ones here.<sup>41</sup> This funding also supported the policy advocacy work that led to the creation of targeted funding that offered important ongoing support for implementers and enabled many of them to grow. These funding streams include the SBA Microloan program, the Community Development Finance Institutions Fund (CDFI Fund), which invests in a range of community finance programs including microenterprise, and PRIME (the Program for Investments in Microenterprise), as well as several programs that provide resources at the state level. The policy work also led to changes in the regulations governing the Community Development Block Grant (CDBG) program, which helped to expand the use of CDBG dollars in support of microenterprise development.

The result of these efforts during the period of the 1990s can be seen in the periodic directories of U.S. microenterprise programs, which FIELD has produced since 1992 and which list all organizations and summarize key data on their outreach and performance. The first directory, in 1992, identified 108 organizations engaged in the industry. The last, published in 2002, identified 650 organizations.<sup>42</sup> Of these, 554 are microenterprise development programs providing services directly to current and aspiring entrepreneurs. The remaining are “support organizations” offering funding, training and technical assistance services to microenterprise practitioner organizations.

FIELD estimates that the microenterprise development programs served between 150,000 and 170,000 individuals in 2000, the last year for which robust survey data are available.<sup>43</sup> This estimate includes some 114,000 clients who received substantial services in the form of loans, training or technical assistance. The balance of participants received less intensive services.<sup>44</sup> FIELD also estimates that \$98.5 million was outstanding in microenterprise loans as of the end of 2002, representing 13,758 loans to microentrepreneurs. The average loan size is estimated at \$7,166.<sup>45</sup> In addition to microloans provided directly by microenterprise programs, a number of entrepreneurs receive bank financing with program assistance. There are limited available data on this

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<sup>41</sup>Most notably, these funders included the Charles Stewart Mott Foundation, which has been a sustained funder in the sector; the Ford Foundation; and the Levi Strauss Foundation.

<sup>42</sup>Britton Walker and Amy Kays Blair, *2002 Directory of U.S. Microenterprise Programs* (Washington, DC: The Aspen Institute/FIELD, 2002). Data for this directory was collected in association with the Association for Enterprise Opportunity.

<sup>43</sup>The Association for Enterprise Opportunity recently completed a new survey of the microenterprise industry. Analysis of that data was not complete by the time of this writing, but publication will be forthcoming.

<sup>44</sup>A total of 308 organizations provided complete responses to the 2002 Directory survey, reporting that they assisted 100,000 individuals, of whom 48,777 received substantial service in the form of loans or significant training or technical assistance. Assuming that the non-reporting organizations were similar in size, the total number of individuals served would be 179,870. FIELD also collects detailed performance data annually from a more limited number of microenterprise programs under its MicroTest program and subjects this data to more rigorous cleaning protocols. The estimate of between 150,000 and 170,000 participants is based on using the median numbers of clients (those receiving intensive services) and participants (those receiving any services) assisted by MicroTest members (205 and 273, respectively) as a proxy for those organizations that did not provide complete program entries.

<sup>45</sup>This estimate is drawn from an examination of three data sources: the *2002 Directory* (Walker and Blair), which reports \$58,526,208 in outstanding loans; MicroTest data for 2002, which documents 6,715 loans made by 45 reporting institutions and outstanding portfolios of \$37,558,061; and data from the Community Development Finance Institutions Data Project (CDP), which collects institutional data on a large universe of CDFIs. The CDP reported that 111 CDFIs had \$65,934,462 in 8,740 outstanding microloans at the end of FY 2002. The estimate of \$98.5 million in outstanding microloans overall is made by an examination of the three data sources and elimination of the overlap among them.

service, but as an example, 27 MicroTest organizations reported leveraging \$1.7 million in loans for their clients during Fiscal Year 2002.

It is important to note that the industry is still relatively young. Only 25 percent of the 324 microenterprise development programs that reported their program start dates in the *2002 Directory* were established before 1991.

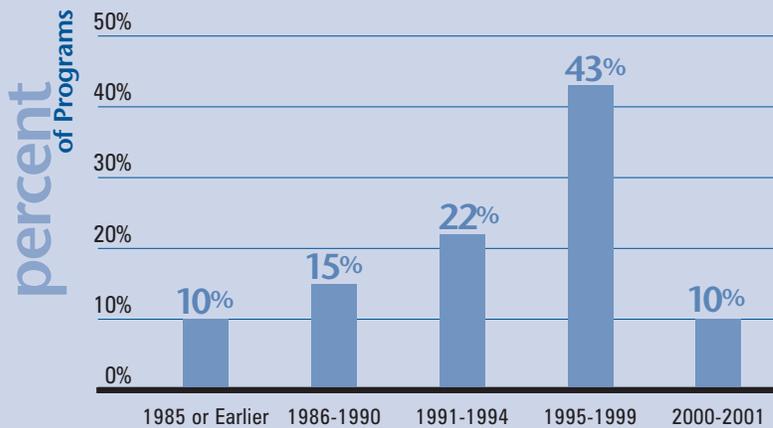
Of the remaining, 22 percent were established between 1991 and 1994. The largest group, 43 percent, were established between 1995 and 1999 and another 10 percent, since 2000. More than half the industry, it appears, has been in existence for fewer than 10 years. This may explain the small size of many programs. The average operating budget reported by respondents to the *2002 Directory* was \$378,781 and the majority of these programs (79 percent) had five or fewer full-time staff.<sup>46</sup>

## What is a Client?

**Clients** are those who receive substantial program service during a given fiscal year. All borrowers are clients, as are others who receive at least 10 hours of training or technical assistance services.

**Participants** include all clients and others who receive fewer than 10 hours of training or technical assistance during a given fiscal year and are not receiving financial services. These individuals may include both pre-entrepreneurs exploring business feasibility and more experienced entrepreneurs who, having completed core training and/or technical assistance services, recur to the programs for more limited, follow-up services.

**Figure 2: Date Practitioner Programs Were Established**



<sup>46</sup>For Fiscal Year 2002, 52 MicroTest organizations reported an average operating budget of \$689,000. Microenterprise organizations participating in MicroTest tend to be larger and somewhat more mature than the majority of the U.S. field.

The industry has developed in a very “bottom up,” grassroots way. This is manifested in the large number of relatively small programs spread across the country, as well as the array of institutions that have adopted microenterprise development as a strategy to assist the self-employed. True to its origins in a variety of development organizations, services are currently provided by specialist institutions dedicated strictly to microenterprise development (microloan funds and business development organizations), as well as by community development corporations, credit unions, community action agencies, employment and training institutions, immigration and refugee organizations, universities, and others. The variety of implementers demonstrates the attractiveness of the strategy to many organizations seeking better ways to serve their clients. It also demonstrates why it has been a challenge to advance institutionally. With small budgets and staffs and multiple services, it has been difficult for many organizations to build organizational capacity and develop economies of scale.<sup>47</sup>

**Table 2: Specialization Matters**

<b>Organizations focused strictly on microenterprise development reach more aspiring entrepreneurs than other types of organizations, as the comparative data below suggests.<sup>48</sup></b>				
	Specialist Microenterprise Development Organizations (n = 24)	Community Development Finance Institutions <sup>49</sup> (n = 17)	Community Development Corporations (n = 10)	Human Service Organizations (n = 7)
Clients (median)	367	207	135	251
Participants (median)	772	379	312	391

While microenterprise organizations are spread across the United States, they are not evenly distributed. The map found in Figure 3 relates the number of microenterprises in each state to the number of microenterprise development organizations located there;<sup>50</sup> the darker the shading, the greater the penetration of microenterprise development assistance. While the number of microenterprise organizations is an imperfect proxy for the number of clients receiving assistance, it is sufficiently close given that the majority of microenterprise programs across the country serve clients numbering in the hundreds and there are few programs that serve more than 1,000.

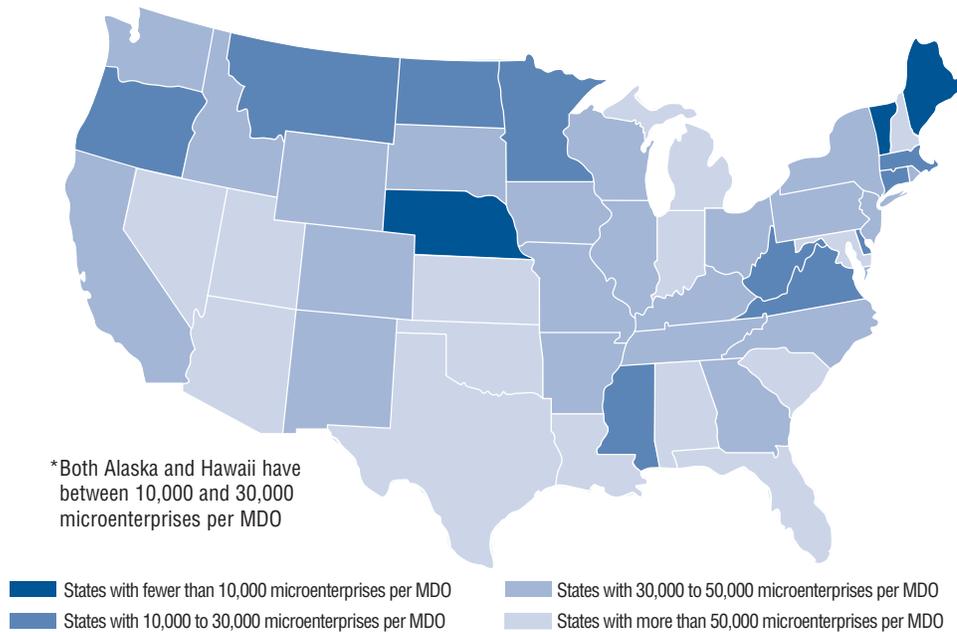
<sup>47</sup>Staff turnover also affects organizational capacity and program quality. Anecdotally, many program managers have reported difficulties in retaining experienced staff, as trained loan officers become attractive candidates for banking positions and others with business and industry expertise seek more remuneration, especially benefits, than programs are able to provide.

<sup>48</sup>Fiscal Year 2002 MicroTest data.

<sup>49</sup>According to the Community Development Finance Institutions Coalition, “Community Development Financial Institutions (CDFIs) are private-sector, financial intermediaries with community development as their primary mission. While CDFIs share a common mission, they have a variety of structures and development lending goals. There are six basic types of CDFIs: community development banks, community development loan funds, community development credit unions, microenterprise funds, community development corporation-based lenders and investors, and community development venture funds. All are market-driven, locally-controlled, private-sector organizations.” Coalition of Community Development Financial Institutions, *What are CDFIs?*; available from <http://www.cdfi.org/whatare.asp>; Internet.

<sup>50</sup>Identification of microenterprise development programs based on *2002 Directory* (Walker and Blair). The number of microenterprises in each state is based on calculations by the Association for Enterprise Opportunity using U.S. Census and Department of Commerce data. For more on this methodology and state-by-state numbers, see AEO, *Microenterprise Employment Statistics*; available from <http://www.microenterpriseworks.org/services/policy/mees/index.htm>; Internet.

**Figure 3: Penetration of Microenterprise Development Assistance Organizations (MDOs) Across the United States\***



As can be seen, the distribution is uneven in and across regions. While most of New England appears to have stronger coverage, New Hampshire appears to have much less representation. Similarly, in the mid-Atlantic region, while Connecticut, Delaware and Virginia appear to have a large number of service providers, New York, New Jersey and Pennsylvania have fewer, and Maryland has least of all. The western states of Nebraska, North Dakota and Montana also appear to have a stronger infrastructure of microenterprise service providers. States with the least penetration of microenterprise service providers appear to be in the South (Alabama, Florida, Louisiana and South Carolina) and West (Arizona, Nevada, Texas and Utah), although there are some in every region of the country. This is not to be taken as an argument for the creation of many more small-scale service providers, but one challenge for the industry is how to reach out to the large market that still remains unreached by current service providers.<sup>51</sup>

### The Methodological Landscape

During the past 20 years, the field has developed a range of methodologies to assist emerging microentrepreneurs. Depending on the needs of clients and the mission and capacity of local organizations, microentrepreneurs can access financial and business development services of a wide variety.

<sup>51</sup>One of the factors influencing the penetration of microenterprise assistance may be favorable state policy. Nebraska and Montana, for example, are two states that have developed policies supporting the industry.

## FINANCIAL SERVICES

Although prominent coverage of peer lending in the press and early documents on U.S. microenterprise practice might have suggested that peer lending would be the model of choice in the United States,<sup>52</sup> as it has in many less developed countries, in fact, direct, or individual, lending remains the principal financing product available to microentrepreneurs. Of 198 lenders reporting to the *2002 Directory*, only 36 reported offering a peer-lending product, while 182 reported making individual loans. The emphasis on individual loans is based on the preference of customers, as well as the challenge of constructing effective peer groups in most U.S. markets where little pre-existent group cohesion exists. Further, while the peer-lending model appears to offer some advantage in terms of scale and cost per client, the small size of the loans provided make it extremely challenging for peer programs to cover a substantial portion of their costs.<sup>53</sup>

At the same time, direct lending offers microenterprise programs the opportunity to couple the loan with training or one-on-one technical assistance services and many do provide both to their clients. Among organizations responding to the *2002 Directory* survey, only 4 percent of reporting agencies indicated that they provided lending alone without any training or technical assistance services.

Microloans remain the primary financing tool that programs offer their clients. In addition, some programs offer grant assistance, microequity investments, Individual Development Accounts (IDAs), and some additional savings options, all of which are attractive to microentrepreneurs who prefer equity to debt.<sup>54</sup> In most cases, the number of institutions offering these products is small. The one exception is IDAs, which appear to be growing in use. Among the survey respondents listed in the *2002 Directory*, 22 percent reported offering IDAs (during their Fiscal Year 2000), while only 5 percent reported offering other types of savings services. (There is no count on the other products.) With

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<sup>52</sup>For example, see Candace Nelson, *Going Forward: The Peer Group Lending Exchange, November 2-4, 1993. A Report on the Conference by Candace Nelson and Papers Presented at The Conference* (Toronto: Calmeadow, May 1994).

<sup>53</sup>A comparison of seven peer lenders in the MicroTest database with the other 54 lenders in the group (some of whom may do some peer lending, but are largely known for their individual loan product) showed that the peer lenders served more clients (an average of 444 to 335; a median of 442 to 222) and made more loans (an average of 125 to 85; a median of 46 to 22). They also spent less per client (an average of \$1,692 to \$2,825; a median of \$1,475 to \$2,355). However, their average loan size of \$847 compared to \$6,238 for the other lenders resulted in operational self-sufficiency rates of 6 percent on average (4 percent median) compared to the other lenders that were able to cover 31 percent of their credit operating costs on average and 19 percent on median.

Although they require more subsidy, this does not mean that there are not other important advantages to peer lending. Program operators cite the following benefits: peer support, advice, ideas, encouragement; relief from the isolation of self-employment; new relationships; alternatives to the negative or defeatist environment of disadvantaged neighborhoods; motivation, focus, accountability; skill development – business management, leadership, communication; business contacts, customer referrals, patronage marketing opportunities; increased confidence in oneself and one's ability to run a business; community impact through the creation of a business infrastructure working to improve neighborhoods and local communities. For more on these and other aspects of peer networks, see Candace Nelson, *Best Practice Guide: Volume 6: Staying Connected: Building Entrepreneurial Networks* (Washington, DC: The Aspen Institute, 2004); available from <http://fieldus.org/publications/PrimeVol6.pdf>; Internet. Also see Melissa Scudo, *Peer Plus: The Evolution and Success of Peer Lending in the United States* (Arlington, VA: The Association for Enterprise Opportunity, 2003).

<sup>54</sup>Some programs partner with the Trickle Up Program, a nonprofit organization specializing in microequity grants, to provide \$700 grants to qualifying entrepreneurs. Others seek out grant assistance programs for their clients, such as those found in local façade improvement programs. A few have also adapted equity investment instruments to infuse capital into client businesses. See, for example, The Aspen Institute, *Practitioner Training Kit – Developing a Micro-Equity Product: The Coastal Enterprises, Inc. Experience* (Washington, DC: The Aspen Institute/FIELD, Spring 2001). Individual Development Accounts are matched savings accounts that provide incentives for savings for specific assets, including home ownership, education or a microenterprise. Some programs, assisted by the Corporation for Enterprise Development's Local Capital Initiatives Fund, are also experimenting with products that combine microcredit with IDAs.

each passing year, more MicroTest organizations report providing IDAs – from 21 percent in 2000 to 47 percent in 2003.<sup>55</sup> The movement into other products may continue to increase as programs seek appropriate ways to help entrepreneurs inject capital into their businesses as well as to manage other financial needs.<sup>56</sup>

## BUSINESS DEVELOPMENT SERVICES

For years, the signature training product in the microenterprise industry has been the core, business-plan training course, which guides emerging entrepreneurs through the basic concepts needed to test the feasibility of a business idea and then to create a plan for the business. Whether the course takes 12 hours, 20 hours or more, depends to a large extent on who the target market for the course is – their interests, experiences and capacities – and the organization’s mission and how it envisions its core services. Short or long, most business-plan training presents the fundamentals of a business plan as a springboard for business start-up, for financing, and for business growth.

As experience has demonstrated how challenging it is for many microentrepreneurs to grow their businesses with just this support, services dedicated to start-ups and early-stage businesses have been joined by advanced services focused on marketing, business operations, finances and technology. Programs have added not only content but also delivery vehicles. In addition to classroom training and business consulting, programs offer coaching, manage mentoring services, and facilitate networks to develop skills and help entrepreneurs build markets. A few have developed distance learning strategies for both new and ongoing clients.<sup>57</sup>

Under the rubric *Access to Markets* (ATM), a number of programs have pioneered initiatives with the explicit goal of connecting microentrepreneurs to larger markets. The most notable of these efforts have been sector-specific and focus on industries in which many microentrepreneurs are engaged, such as specialty foods and crafts. The strategies used are various, work on either the supply or demand side of the market, and seek to increase the productive capacity of the businesses or create new market venues or opportunities. In some instances, programs have become direct marketers themselves, establishing social businesses to manage these operations. ATM strategies have been among the most challenging for programs to implement and the learning curve has been steep as success depends on substantial understanding of market trends and preferences, staff expertise in product development and refinement, and industry connections. Despite these challenges, programs continue to pursue these strategies in

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<sup>55</sup>The average number of IDAs reported by MicroTest programs was 20 in Fiscal Year 2003; the maximum was 177.

<sup>56</sup>FIELD funded five organizations to examine methods to increase business financing to low-income entrepreneurs. Among products tested were microequity investments, a “Jump Start” loan providing automatic access to a small amount of financing for training program graduates, and a loan rebate product that reinvested part of the loan proceeds back into the businesses of borrowers with good repayment records. Other products studied included “Goalsaver” loans offered by Bethex Federal Credit Union to help borrowers build their credit histories as well as assets, and IDAs integrated into microenterprise services. For more on the learning from this initiative, see: Field Web site, *Financing Products for the Poor*; available from [http://fieldus.org/li/financing\\_findings.htm](http://fieldus.org/li/financing_findings.htm); Internet.

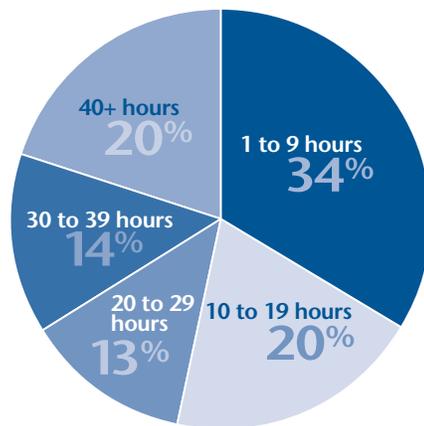
<sup>57</sup>FIELD has documented best practices in training and technical assistance in a range of publications that address core training, coaching, mentoring and business consulting, technology services, and networking. For more on these, see: Elaine Edgcomb and others, *Improving Microenterprise Training and Technical Assistance: Findings for Program Managers* (Washington, DC: The Aspen Institute/FIELD, February 2002); available from <http://fieldus.org/publications/improvingmicro.pdf>; Internet; and *FIELD Best Practice Guides: Volumes 1-6* (Washington, DC: The Aspen Institute/FIELD); available from <http://fieldus.org/li/bestpractice.html>; Internet.

response to explicit client demand for help in breaking through the boundaries of very local markets.<sup>58</sup>

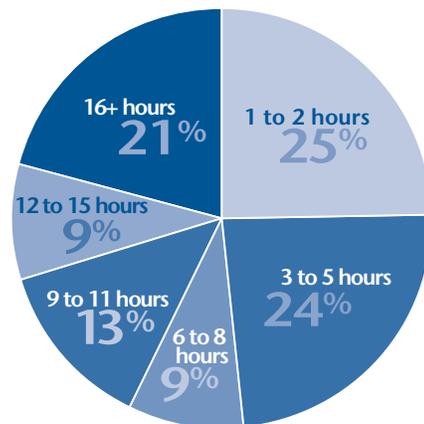
Finally, programs with strong missions focused on those with greatest barriers to business development – those transitioning from welfare, the disabled, immigrants and refugees – have adapted basic training and technical assistance strategies, adding case management services, personal development assistance and other supports to help clients achieve success.

Not surprisingly then, U.S. microenterprise programs offer substantial numbers of training and technical assistance hours to their clients. The median number of training hours per client reported by *2002 Directory* survey respondents was 18; the median number of technical assistance hours was six. However, the range is great. Figures 4 and 5 below show the distribution of service hours reported by *2002 Directory* respondents.

**Figure 4: Distribution of Microenterprise Development Organizations Based on Average Training Hours Provided Per Client**



**Figure 5: Distribution of Microenterprise Development Organizations Based on Average Technical Assistance Hours Provided Per Client**



<sup>58</sup>Findings from the Charles Stewart Mott Foundation demonstration on Access to Markets programs are available in Karen Doyle Grossman and others, *Connectors and Conduits: Reaching Competitive Markets from the Ground Up* (Washington, DC: The Aspen Institute/FIELD, July 2002); available from <http://fieldus.org/publications/ATMFinalReport.pdf>; Internet.

## Conclusion

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**T**his brief review of methodology underscores three key characteristics of the microenterprise industry in the United States. The dominant form of support provided program clients is business development services. Microenterprise development in the United States to date emphasizes training and technical assistance more than the direct delivery of microfinance. The strategies used by organizations are diverse. While core business-plan training and individual loans are emblematic of the field, they are complemented by a wide array of offerings that vary in intensity, content and style depending on the needs of clients and organizational capacity. And finally, programs are still engaged in significant innovation. There is still much that the industry is learning about how to best deliver services that match clients' characteristics, business status, growth goals and needs.



The microenterprise field can point to a number of accomplishments: programs are reaching the underserved as intended; annual costs of services are relatively modest and in line with other workforce and economic development costs; and lenders are learning to manage portfolio risk. Still, the field faces challenges: training and technical assistance are largely subsidized; and most programs remain small, limiting their ability to offer additional products and leaving much of the field's market underserved. This chapter examines the industry's performance record, shedding light on both strengths and weaknesses.

# The Institutional Performance of the Industry

The previous chapter laid out the growth and evolution of the industry. But, how is it performing? To understand this, one needs to know the answers to two sets of questions. The first set relates to the issue of the institutional performance of microenterprise programs: How effective and efficient are organizations in the delivery of their services? Do they reach substantial numbers? Are they sustainable? The second set of questions addresses the difference these services make to clients. Do clients succeed in launching and growing businesses? Do they generate a meaningful amount of income? Do households move out of poverty? This chapter will address the first set of questions and the following chapter will address the second set related to client outcomes. This chapter will review the industry's record with respect to outreach, scale, credit and training program performance, and cost recovery.

## Outreach to Underserved Populations

*The field has been largely successful in assisting individuals who experience greater barriers to business development, especially women, minorities, and low-income individuals.* As the first chapter indicated, the microenterprise industry emerged to serve the needs of individuals overlooked (or not adequately served) by traditional small business development services. Available data show that this goal has largely been realized. Organizations reporting to the *2002 Directory of U.S. Microenterprise Programs* reported that in 2000:<sup>59</sup>

- ▶ 65 percent of all clients assisted were women;

### Sources of Data for This Chapter

Primary sources of data referenced in this chapter include MicroTest's dataset, which contains data collected from member programs since Fiscal Year 2000 (63 organizations submitted data in Fiscal Year 2003) and the *2002 Directory* data, which contains detailed descriptive data on 308 organizations. Organizations that report to MicroTest are both similar to and different from the larger pool of microenterprise organizations. They serve urban and rural areas, as well as women and minority clients in nearly the same proportions as those listed in the *Directory*. On the other hand, they tend to be larger, more experienced, more "credit-led," and serve a higher percentage of economically disadvantaged clients.

For more on MicroTest members and performance data see: Jeremy Black and others, *A Measure of the Microenterprise Industry* (Washington, DC: The Aspen Institute/FIELD, March 2003) and Jeremy Black and others, *For Good Measure: Performance of the U.S. Microenterprise Industry* (Washington, DC: The Aspen Institute/FIELD, August 2002).

<sup>59</sup>The figures on target groups served are based on 258 programs that reported on the gender of their clients, 251 that provided data on the minority status of clients, and 162 that reported on income status of clients served.

- 55 percent were minorities; and
- 59 percent had incomes at or below 80 percent of area median income, the low-income standard for the U.S. Department of Housing and Urban Development.

MicroTest data reinforces this finding. In Fiscal Year 2003, the 63 reporting programs served 13,669 women, representing 56 percent of all clients served. They assisted 12,545 minorities, who comprised 53 percent of all clients, and 9,949 low- to moderate-income individuals, 62 percent of all clients served. This type of outreach is not anomalous; data reported for 2000 through 2002 have shown that the level of client targeting has remained consistent.

**Table 3: Targeting by MicroTest Programs: Median Results for all Reporting Organizations**

	FY 2000	FY 2001	FY 2002	FY 2003
Women	60% (n = 56)	57% (n = 64)	57% (n = 61)	56% (n = 63)
Minorities	50% (n = 55)	51% (n = 63)	58% (n = 61)	57% (n = 61)
Low income (HUD guidelines) <sup>60</sup>	65% (n = 48)	66% (n = 53)	61% (n = 48)	70% (n = 43)

These findings are particularly notable when contrasted with the overall statistics regarding rates of women and minority business ownership. While rates of business ownership are growing among women, recent data show that women represent only about one third of all self-employed workers and owners of non-farm sole proprietorships.<sup>61</sup> Minorities were also reported to own only 14.6 percent of all U.S. firms.<sup>62</sup>

A substantial number of microenterprise program clients meet even stricter definitions of poverty. MicroTest programs report clients' household income according to two low-income definitions in addition to the HUD standard. Programs report the percent of clients whose income at the time of program intake was at or below 100 percent of the Department of Health and Human Services poverty guidelines. Given the widespread recognition that the federal poverty line represents a level of income well below what is actually required to sustain a family, this is a very stringent measure that documents the number of extremely low-income clients served. Programs also report the percent of clients whose incomes are at or below 150 percent of that standard, a benchmark of low-income status that encompasses many of the working poor, in

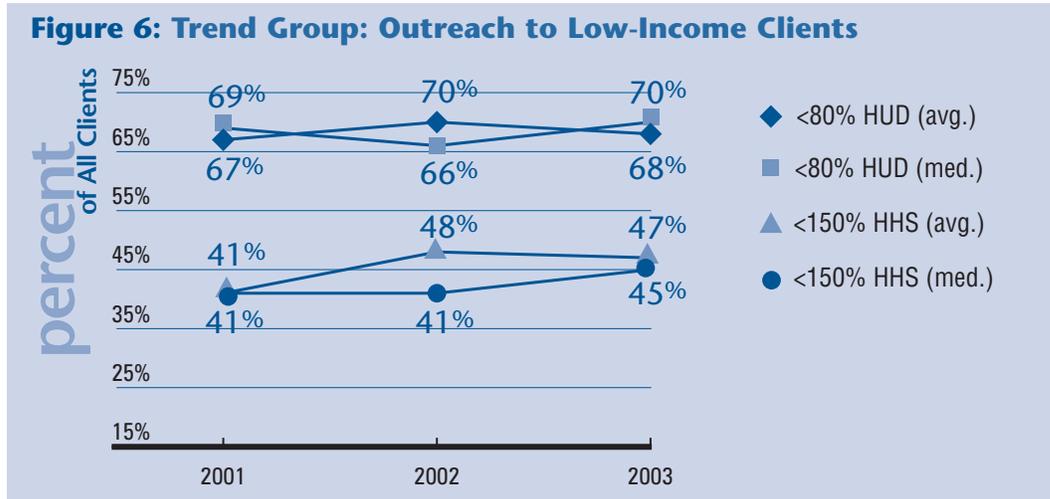
<sup>60</sup>The Department of Housing and Urban Development establishes income limits in relationship to the area median family income in each metropolitan statistical area and non-metropolitan county. Households with incomes at or below 80 percent of the area median are considered low- to moderate-income households and are eligible for a variety of services. Many federal and state funders of microenterprise programs require that recipients of services be at or below 80 percent of the HUD median. It is generally the broadest definition of low-income used by microenterprise programs. For more, see <http://www.huduser.org>.

<sup>61</sup>SBA Office of Advocacy, *Women In Business 2001* (SBA, October 2001). Women comprised 37.9 percent of self-employed workers in 2000 and owned 35.3 percent of non-farm sole proprietorships in 1998.

<sup>62</sup>U.S. Department of Commerce, Economics and Statistics Administration, U.S. Census Bureau, "1997 Economic Census: Survey of Minority-Owned Business Enterprises," *Company Statistics Series* (July 2001); available from <http://www.census.gov/prod/ec97/e97cs-7.pdf>; Internet.

addition to those living in deep poverty.<sup>63</sup> In addition, programs report the number of clients who were receiving TANF benefits upon program entry.<sup>64</sup>

For Fiscal Year 2003, 30 percent of all clients assisted by MicroTest programs lived at or below 100 percent of the HHS poverty guidelines. Forty-five percent lived in households with incomes at 150 percent of that standard and 11 percent entered programs on TANF. Again, these results are consistent over time.<sup>65</sup> Figure 6 shows the three-year performance of MicroTest’s “trend group,” a set of 29 organizations that have consistently reported their data against these measures.



The fact that at least 40 percent of clients during these years were at or below 150 percent of the HHS poverty guidelines demonstrates that the programs are targeting individuals who are strongly resource-constrained. They are the working poor, individuals transitioning off welfare, the economically displaced, and others struggling at the bottom of the economy.

The industry has succeeded in serving its low-income target market throughout its history. Between 1991 and 1996, the Self-Employment Learning Project<sup>66</sup> (SELP) tracked seven of the then-leading U.S. microenterprise development organizations against a variety of measures. At the end of 1996, these organizations reported that 70 percent of all their clients were women; 54 percent were minority; and 43 percent were reported to have household incomes below \$13,956 a year, the HHS poverty guideline for a household of four at that time. While the higher targeting to women was due to the presence of two women’s development organizations in the group, the targeting to minorities and the low-income reflects that of current programs. The data suggest that outreach to the underserved has been consistent across the years in the industry.<sup>67</sup>

<sup>63</sup>As an example, a family of four would be at 100 percent of the HHS guideline, if its income in 2002 was \$18,100. At 150 percent of HHS, its income would be \$27,150.

<sup>64</sup>TANF, or Temporary Assistance for Needy Families, is the name of the federal government’s welfare assistance program.

<sup>65</sup>Forty-five organizations reported data relating client income to the 100 percent and 150 percent HHS guideline; 35 organizations reported data on TANF recipients among their clients.

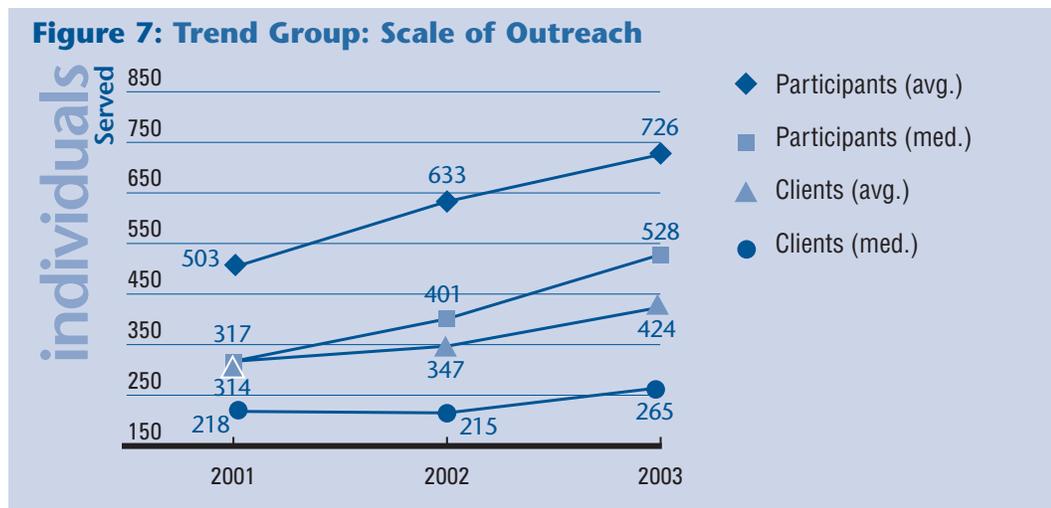
<sup>66</sup>The Self-Employment Learning Project was a learning assessment that studied seven senior microenterprise programs in the early 1990s. SELP, based at the Aspen Institute, was the precursor program to FIELD.

<sup>67</sup>Elaine Edgcomb and others, *The Practice of Microenterprise in the U.S.: Strategies, Cost and Effectiveness* (Washington, DC: The Aspen Institute, 1996), 15-17.

## Program Scale

Most programs serve a few hundred clients per year, a small number in relation to the estimated potential market for microenterprise services in most areas. The previous chapter noted the growth of the industry in terms of the number of organizations providing services and the estimated number of individuals served in 2000 – between 150,000 and 170,000. Over time, of course, the numbers reached have been much larger.<sup>68</sup> On an average basis, however, the number of clients served annually is fairly modest. In 2000, organizations surveyed for the *Directory* reported serving an average of 175 clients.<sup>69</sup> Counting all individuals served, in addition to clients who receive more intensive levels of service, the average number of participants served by programs reporting to the 2002 *Directory* was 361. The average and median client figures for programs reporting to MicroTest in Fiscal Year 2003 were 374 and 248, respectively. The average and median numbers of participants reported by MicroTest organizations for 2003 were 709 and 446.<sup>70</sup>

Trend data also suggest that while programs are growing, growth is incremental. This is illustrated by trend data on MicroTest organizations that have reported their outreach data during the past three years.<sup>71</sup> As the data in Figure 7 indicates, the number of clients grew on average 34 percent during a two-year period, but the increase in the median number of clients was a more modest 22 percent. Growth in the number of participants was stronger with the average increasing 44 percent during the period and the median increasing 68 percent. As programs mature, it is not surprising that their total number of participants grows, as they provide continuing services to clients from previous years as well as reach out to new people. Nevertheless, the fact is that the numbers of individuals served still average in the hundreds.



<sup>68</sup>For example, the 2002 *Directory* reports that 540,852 cumulative participants have been served by the 240 programs that reported data. The programs surveyed for the *Directory* represent fewer than half of all known programs, suggesting that the total number of clients served during the past 20 years is much higher. Because microentrepreneurs in the United States tend to stay with programs for a limited number of years, the cumulative numbers served far outweigh the current portfolio of any given institution. (For example, the 276 clients of nine microenterprise programs funded by the Ms. Foundation's Collaborative Fund for Women's Economic Development who were surveyed as part of an outcomes monitoring process were found to have been with their programs for a median of 1.8 years.) Clients choose to leave programs for many reasons: they may no longer need a loan; they may need only start-up assistance or very limited assistance related to specific business issues.

<sup>69</sup>Walker and Blair. A total of 270 organizations reported client data.

<sup>70</sup>Sixty-three MicroTest organizations reported client data; 60 reported participant data.

<sup>71</sup>Forty-one reported the number of clients during the past three years; 36 reported participant numbers.

*However, several programs have demonstrated it is possible to serve significantly larger numbers of clients.* Among the MicroTest group, there are nine organizations that served at least twice the median number of participants reported in Fiscal Year 2003 – assisting between 1,504 and 5,957 individuals.<sup>72</sup> Seven organizations assisted at least twice the median number of clients – between 829 and 2,110. Five programs served more than 1,000 clients each. Among these top performers were five credit-led organizations and two training-led organizations.

Some credit-led programs in the MicroTest group made substantial numbers of loans as well. In Fiscal Year 2003, eight high-performing credit programs made a total of 3,425 loans, making between 137 and 1,206 per organization. They disbursed between \$234,000 and \$6.3 million and their average outstanding portfolios were between \$189,401 and \$6.1 million. This stands in strong contrast to the total group of credit-led organizations represented in the MicroTest data set, for which the median number of loans disbursed was 46.<sup>73</sup>

The data on loans outstanding further reinforce the picture of a concentrated industry. Of a total of 230 lenders, 16 account for 45 percent of all microloans (5,899 loans valued at \$37.1 million). The other 213 account for 55 percent (7,352 loans valued at \$56.5 million).<sup>74</sup>

Several factors appear to influence the ability of microenterprise programs to achieve greater levels of scale. The targeted market is one: four of the nine largest programs reporting to MicroTest (in terms of numbers of clients) are state-wide in scope and three are in large urban markets. The age of the program is a second factor: each of these larger-scale programs is at least nine years old.

Nevertheless, the organization's degree of focus and commitment to increasing its scale is the most critical factor in its ability to grow. Among this group of nine MicroTest top performers, three are associated with the ACCION US Network and reflect the fact that these institutions were explicitly designed with scale and sustainability as their goals. Research conducted by FIELD on a set of microenterprise programs seeking to achieve greater scale revealed a set of common themes, as indicated in the box on the next page.

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<sup>72</sup>An additional organization served slightly less than double the median, 1,504.

<sup>73</sup>Twenty-six organizations reported themselves to be credit-led among the MicroTest organizations. The number and dollar value of loans disbursed includes all new loans made to borrowers in a given fiscal year. The number and dollar value of loans outstanding (or portfolio) represents all loans in the hands of borrowers and the dollars still owed against those loans, regardless of the year in which the loan was made.

<sup>74</sup>This estimate is based on an analysis of data reported in the *2002 Directory* and the MicroTest and CDFI Data Project databases for 2002. Each of the 16 volume lenders had more than 150 loans outstanding; the range was from 160 to 1,344.

## Achieving Top Performance in Scale-Up

FIELD's research on scale has identified a set of interrelated activities that growth-focused U.S. microenterprise organizations pursue:

- ▶ They have established scale-up as a key measure of their success, develop executive leadership and boards committed to achieving it, and monitor their progress against it relentlessly.
- ▶ They engage in substantial market research and marketing activities to identify who their target clients are, what products and services they seek, and how best to communicate with them.
- ▶ They generally offer multiple products or services that customers demand and that are feasible for the program to deliver with some volume.
- ▶ They build staff capacity in advance of stimulating demand.
- ▶ They are highly efficient in deploying staff and fulfilling key functions.
- ▶ They invest in a range of organizational infrastructure and especially management information systems and other technologies that support rapid decisionmaking and rapid product delivery.
- ▶ They develop sustainability plans that include cost recovery and emphasize funding diversification.
- ▶ They look to private sector business models for inspiration with respect to strategy and structure.<sup>75</sup>

These top performers have made substantial strides in increasing their scale of service delivery, offering models for emulation by other microenterprise programs. But, questions remain about what it will take for these programs to continue to grow at the rates they have achieved in the past and whether and if the rest of the microenterprise field will be able to follow suit. Programs face significant challenges to increasing their scale of operations. These include the fact that increased sustainability does not always follow from growth – and, as a result, programs may not be able to secure the resources necessary to take on and sustain higher levels of service. Furthermore, there may be trade-offs between the level of scale and the depth of service delivery – meaning that programs that seek to grow may see diminished impact at the client level. Sorting through these issues will be one of the key challenges that the field faces as it moves to the future.

## Credit Program Effectiveness

### PORTFOLIO QUALITY

*Microenterprise lenders have, over time, learned that it is possible to manage the risk in their portfolios effectively.* Microcredit programs seek to lend money to individuals who cannot access traditional credit markets. The barriers they face in accessing traditional sources of credit include a lack of assets and equity, as well as poor credit histories,

<sup>75</sup>Elaine Edgcomb and others, *Scaling up Microenterprise Services* (Washington, DC: The Aspen Institute/FIELD, May 2002), 5-22.

which mean that lending to these individuals entails higher levels of risk. Early research on the development of the microenterprise industry documented the struggles of particular institutions to develop effective systems for loan recuperation. For example, SELP's study *The Practice of Microenterprise in the U.S.* found that in 1993, the aggregate portfolios of the seven agencies studied had a loan loss rate of 10.95 percent and 21.6 percent of the portfolio was at risk. A look at the trends in the portfolios of the individual programs in the study revealed that many were challenged to maintain portfolio quality over time. The SELP risk and loss figures were slightly higher than those for a set of microenterprise programs funded by the Charles Stewart Mott Foundation. In 1993, 11 Mott-funded programs experienced an overall loan loss rate of 8 percent and 23 grantees had a combined portfolio at risk of 18.74 percent.<sup>76</sup> Other research focused on the performance of California microenterprise lenders found aggregate loan losses of 21 percent in four peer lending programs operating between 1989 and 1996.<sup>77</sup>

While these early studies captured the challenges that organizations faced in developing methodologies to lend to this client base, the larger and more recent MicroTest data set reveals a much stronger level of portfolio quality, at least among the more experienced lenders that are part of the MicroTest program. Table 4 below lists the average and median performance for 45 lenders that reported data on their Fiscal Year 2003 lending activities to MicroTest.

**Table 4: Credit Program Performance<sup>78</sup>**

<b>Data on 45 Lenders in MicroTest</b>	<b>Total Portfolio At-Risk Rate &gt; 30 days</b>	<b>Restructured Loan Rate</b>	<b>Loan Loss Rate</b>
Average for FY 2003	14%	8%	9%
Median for FY 2003	11%	9%	7%

The averages and medians do not tell the full story. While half of the 45 programs reporting portfolio at-risk rates achieved a rate of 11 percent or less, 13 of them reported rates below 6 percent. While the median for these programs reporting restructured loan rates was 9 percent, 20 of them reported rates lower than 4 percent. And finally, while half of the 45 programs reported loan loss rates at or below 7 percent, 21 reported rates below 4 percent and 16 of them reported rates below 2 percent.

<sup>76</sup>Elaine Edgcomb and others, *The Practice of Microenterprise in the U.S.*, 54.

<sup>77</sup>Nitin Bhatt, *Inner City Entrepreneurship Development: The Microcredit Challenge* (Oakland, California: Institute for Contemporary Studies, 2002), 94.

<sup>78</sup>Portfolio at-risk is defined as the dollar amount of principal outstanding on all loans with payments past due 31 days, divided by the total dollar amount of microloans outstanding at the end of the fiscal year. Restructured loan rate is defined as the dollar amount of restructured loans outstanding at the end of the fiscal year, divided by the total dollar amount of microloans outstanding at the end of the fiscal year. Restructured loans are further defined as those whose terms have been adjusted in response to difficulties a borrower has experienced in meeting his or her repayment obligations. Loan loss rate is the dollar amount declared non-recoverable and written off, net of recoveries, during the fiscal year, divided by the average dollar amount of microloans outstanding during the fiscal year.

The credit performance of MicroTest members has remained consistent over time. Even as membership in MicroTest programs has varied between 1999 and 2003, portfolio performance has generally remained within a relatively small band, as the data in Table 5 demonstrate.<sup>79</sup>

**Table 5: Credit Performance of All MicroTest Programs**

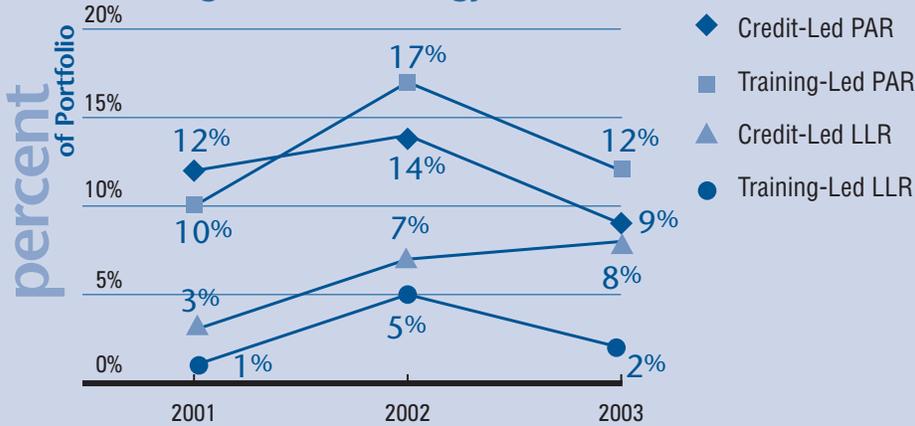
	<b>1988</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>	<b>2002</b>	<b>2003</b>
	<b>n=8</b>	<b>n=33</b>	<b>n=45</b>	<b>n=56</b>	<b>n=56</b>	<b>n=45</b>
Median portfolio at risk	14%	11%	10%	12%	13%	11%
Median restructured loan rate	13%	7%	5%	6%	7%	9%
Median loan loss rate	7.6%	4%	4.8%	5%	4%	7%

The higher loan loss and restructured loan loss rates for Fiscal Year 2003 reported here are partly due to the composition of the MicroTest group for that year. Trend data reported by a set of organizations that reported to MicroTest for three consecutive years show how these ratios may move from year to year for individual organizations. Figure 8 portrays the median performance according to program methodology and includes data from both 16 credit-led programs and 12 training-led programs.<sup>80</sup> The data suggest that while the credit-led programs have faced challenges in terms of loan losses during the past two years, evidently suffering the effects of the post-9/11 recession and other issues, training-led programs have been able to maintain much greater quality control over their generally smaller portfolios, at least in terms of loan losses. This difference may be due to the fact that most training-led organizations manage much smaller portfolios and, therefore, can monitor client performance more carefully. The cost implications of this approach are presented later in this chapter. It is not unusual to see these movements up and down as economic conditions increase the challenges for micro-businesses and for microcredit programs. Finding the right balance between taking appropriate risks and maintaining solid portfolio performance is a task that programs continually face in their efforts to serve borrowers with few other options.

<sup>79</sup>The “point in time” data in this table provides a look at the performance from year to year of all MicroTest members reporting each year. These data do not capture the trend of a specific group of individual organizations, but they provide a window into the overall performance of an increasingly larger number of microenterprise organizations.

<sup>80</sup>MicroTest organizations define themselves as training- or credit-led based on their assessment of which services are the “lead” services offered to clients and which consume the majority of the organization’s staff time and financial resources.

**Figure 8: Trend Group: Portfolio At Risk and Loan Loss Rates by Program Methodology**



### CREDIT PROGRAM EFFICIENCY

*Microenterprise lenders have also made important strides in efficiency; however, large-scale lenders are significantly more efficient.* MicroTest data on the median operational cost rate – an important measure of efficiency that examines the cost a program incurs to make and manage each dollar in its loan portfolio – show that costs are decreasing over time as both the group has expanded to include more programs and individual program performance has improved (Table 6).<sup>81</sup>

**Table 6: Operational Cost Rates of All MicroTest Programs**

	1998 n=8	1999 n=33	2000 n=43	2001 n=49	2002 n=51	2003 n=43
Median operational cost rate	2.33	1.88	0.81	0.75	0.58	0.42

The data also show a marked difference between larger, mostly credit-led, organizations that have shown they can be quite efficient and smaller-scale lenders that incur a considerable premium in offering microcredit. Table 7 illustrates the differences between smaller and larger credit programs, using 50 loans as the dividing line between the two.

<sup>81</sup>MicroTest defines operational cost rate as total credit program operating expenses divided by the average outstanding loan portfolio for the fiscal year in question. MicroTest programs that provide both microcredit and business development services disaggregate their expenses to isolate all credit program costs from other services using costing tools provided by MicroTest.

**Table 7: FY 2002 MicroTest Data: Credit Program Size, Quality and Efficiency**

<b>Credit programs with 50 or more microloans outstanding, n=24</b>								
	Number of Microloans Outstanding	Dollar Amount Outstanding	Average Loan Size	% of Portfolio in Start-ups	Restructured Loan Rate	Loan Loss Rate	Total Portfolio At Risk	Operational Cost Rate
Median	131	\$807,868	\$8,367	10%	5%	4%	12%	0.40
<b>Credit programs with fewer than 50 microloans outstanding, n=26</b>								
	Number of Microloans Outstanding	Dollar Amount Outstanding	Average Loan Size	% of Portfolio in Start-ups	Restructured Loan Rate	Loan Loss Rate	Total Portfolio At Risk	Operational Cost Rate
Median	20	\$102,455	\$5,911	56%	2%	1%	14%	0.90

As these data suggest, smaller microloan programs often direct more of their lending to start-up enterprises (measured in terms of the percentage of the total portfolio outstanding) than do larger loan programs. While these start-up loans may carry more risk, the median portfolio quality is good. However, because there are some important fixed costs associated with running an effective credit program, smaller loan programs show higher operational cost rates than do larger credit programs that are able to spread these costs over a larger average outstanding portfolio.

At some point, though, the smaller a credit program is, the more difficult it can be to justify in terms of cost efficiency (see Table 8). Operational cost rates that exceed 4, for example, indicate that the program spends more than \$4 for every dollar it is trying to manage in its loan portfolio. MicroTest data suggest that the smallest credit programs – those with fewer than 20 microloans outstanding – often have very high operational cost rates. Small credit programs need to consider whether the service they offer is worth this level of subsidy, or whether there might not be more efficient ways to connect these borrowers to the credit they need.

**Table 8: FY 2002 MicroTest Data: Performance of Very Small Credit Programs**

<b>Small credit programs with less than 20 microloans outstanding, n=13</b>								
	Number of Microloans Outstanding	Dollar Amount Outstanding	Average Loan Size	% of Portfolio Lent to Start-ups	Restructured Loan Rate	Loan Loss Rate	Total Portfolio At Risk	Operational Cost Rate
Median	10	\$69,063	\$5,000	25.3%	0%	0%	16%	4.83

## **Training and Technical Assistance Effectiveness**

*MicroTest data reveal that microenterprise programs have been successful in helping entrepreneurs complete key business planning steps that are associated with business outcomes.* Research conducted by FIELD in association with five selected training and technical assistance programs found that there are a variety of factors that influence the likelihood that a client will start, sustain or grow a business after participating in training or technical assistance activities. Among these factors are personal characteristics and circumstances; the set of business skills acquired; and, somewhat less strongly, the type of training style experienced (participatory as opposed to didactic). In addition, the

research found that training completion and other markers of participation and achievement (such as the completion of business plans and class attendance) are also associated with having a business outcome after training, defined as a business start-up, stabilization or expansion.<sup>82</sup> While certainly not the sole determinant of whether a client will successfully engage in or grow a business, the research suggests that completing a set of specific business planning tasks does represent an important intermediate marker of an individual's likelihood to succeed.

MicroTest programs have reported high completion and graduation rates on the part of their clients who participate in business planning courses and other core training services.<sup>83</sup> Table 9 below shows the average and median data for all reporting MicroTest programs during the past six years.<sup>84</sup>

**Table 9: MicroTest Training Performance – All Reporting Organizations**

MicroTest Training Program Measures	1998	1999	2000	2001	2002	2003
Average training completion rate	72%	77%	78%	81%	78%	78%
Median training completion rate	70%	74%	79%	86%	82%	83%
n=	13	32	33	42	43	47
Average business plan completion rate	67%	72%	58%	59%	71%	67%
Median business plan completion rate	63%	75%	57%	64%	80%	71%
n=	13	25	28	31	34	40

These results are consistent from year to year among those programs that have reported to MicroTest over time and across types of programs. Even those programs strongly targeted to low-income individuals exhibit high training completion rates. For Fiscal Year 2003, 23 low-income targeted programs reported an average training completion rate of 81 percent (the median was 85 percent). Nineteen low-income targeted programs reported an average business plan completion rate of 67 percent (the median was 73 percent).

<sup>82</sup>Edgcomb, *Improving Microenterprise Training and Technical Assistance*, 14-15. Two of the participating organizations tracked these measures in particular. Women's Initiative for Self-Employment graduates from the core training were 40 percent more likely to experience business growth than those who did not complete the workshop. The organization found that 75 percent of graduates experienced business growth events (defined as new start-ups, stabilizations or expansions; stabilizations were defined as having achieved or exceeded break even); only 36 percent of non-graduates experienced these growth events. Furthermore, 100 percent of clients who attained self-sufficiency due to self-employment alone graduated from training. The Institute for Social and Economic Development (ISED) found that having a business outcome (a start, stabilization or expansion) after training completion correlated with a set of actions including: completing a business plan, making progress on securing needed financing, completing class assignments, and a high attendance rate. For more detail on their findings, also see their full research reports at <http://fieldus.org/li/pdf/ISED.pdf> and <http://fieldus.org/li/pdf/WL.pdf>; Internet. Note that correlation does not imply causality. As indicated in the discussion above, there are a number of factors that are associated with client success. For training and technical assistance programs that are interested in program quality, however, having a majority of clients successfully complete a set of challenging tasks does suggest something positive about trainer and curriculum effectiveness, at least from the perspective of the clients who choose to stay with the programs.

<sup>83</sup>The term "core training" describes the multi-part training courses that many microenterprise programs offer their clients. It is the centerpiece of their training and is generally designed for pre-business and early stage business owners. It usually includes training on key business planning concepts, may include feasibility assessment work (although this is sometimes offered as a separate, pre-core training course), and may have other components such as personal effectiveness or financial literacy training.

<sup>84</sup>MicroTest defines the training plan completion rate as follows: the number of training graduates (or completers) during a given fiscal year, divided by the total number of clients expected to graduate or complete training during that fiscal year. The business plan completion rate is similar.

It should be noted that these measures are imperfect measures of success. They are akin to reporting on the portfolio quality of credit programs. They indicate that programs are skilled at facilitating and supporting clients' behavior in positive ways, but do not prove a causal link between program services and client impact. To truly assess the effectiveness of training and technical assistance services, programs need to look at a larger range of intermediate measures, including skills acquisition, as well as look at client outcomes. FIELD applied research with five microenterprise training organizations documented some early outcomes achieved by their clients.<sup>85</sup> A sample of these outcomes is found in the box below. One of the challenges the industry faces, however, is the development of uniform measures to capture markers like these across a broader array of institutions, and ultimately demonstrating a causal link between these changes and microenterprise program services. In the meantime, training completion and business plan completion rates offer the simplest way to capture performance quality across the industry. The following chapter provides additional data on the outcomes experienced by those who receive microenterprise training (and credit) services.

### **Sample Outcomes Experienced by Clients of FIELD Training/Technical Assistance Cluster Programs**

Microenterprise programs tracked changes over a two-year period among clients participating in training and technical assistance activities. The numbers of clients tracked varied among programs, depending on program size and methodology, and ranged from a low of 20 (in one qualitative study) to a high of 478 (in one quantitative study). The research captured initial outcomes for clients during that time.

#### **Skills Acquisition**

- ▶ 88 percent of Women's Initiative's clients graduated during the study period and follow up surveys documented that all the skills taught are being used by at least some clients (n = 83).
- ▶ ISED found that clients' confidence levels in 15 specific business concepts increased on average from 47.54 at baseline to 64.31 at the end of core training (maximum score possible: 75 points); (n = 478).

#### **Business Ownership**

- ▶ Business ownership increased among Women's Initiative's sample from 33 percent at enrollment to 73 percent within 1.5 years of training completion.
- ▶ At ISED, 33.6 percent expanded or stabilized an existing business and 17.7 percent opened a new business within eight months after training completion (n = 478).
- ▶ Within two years, the 12 pre-start-ups in Women's Housing and Economic Development Corporation's day-care program had started businesses (n = 20).
- ▶ Central Vermont Community Action Council's clients increased business ownership from 25 percent at enrollment to 65 percent six months after training (n = 36).

#### **Survival Rates**

- ▶ WHEDCO's clients had an 85 percent survival rate after two years.
- ▶ Women's Initiative's clients achieved a 76 percent survival rate of at least one year.<sup>86</sup>

<sup>85</sup>The five organizations were selected through a Request for Proposal process as part of a round of grantmaking that FIELD implemented in 1998. Grants were provided to organizations determined the best qualified to participate in a two-year learning assessment designed to determine how best to assess the effectiveness of training and technical assistance. Applicants were assessed on their capacity to implement evaluation research alongside their capacity building services and to participate in a facilitated learning process designed to uncover best practices in training assessment and in the delivery of training and technical assistance services.

<sup>86</sup>Elaine Edgcomb and others, *Improving Microenterprise*, 6-7.

FIELD research with these grantees further identified a set of practices associated with effectiveness in training and technical assistance. Most important among them are the following:

- ▶ Acknowledging the importance of client readiness for business and offering a range of services to help clients acquire the resources and experiences necessary, including well-designed client assessment processes, pro-active referral to needed social services, links to relevant work experiences, and training designed to improve goal-setting skills and to clarify and test business ideas.
- ▶ Using the best adult learning theory in classroom training, including emphasizing content with immediate and practical relevance, clear expectations for the students and the program, the use of participatory and dynamic training methods that build on client experience, and ample opportunity to practice new skills through a series of small, short-term attainable steps. Effective training emphasizes the importance of attendance and completion of key assignments and creates multiple opportunities for clients and staff together to monitor and measure progress.
- ▶ A focus on key financial and marketing skills, as well as the “soft skills” or basic competencies that increase a microentrepreneur’s ability to apply them effectively.
- ▶ Placing the initiative on clients to access continuing services, but offering them within a structure that keeps clients connected to the program and reminded of available opportunities, especially within the first two years of business start-up.<sup>87</sup>

These practices are hard to measure across an industry, but should be evidenced in the training and business plan completion rates experienced by clients and in their ultimate outcomes.

## Cost Recovery

*Large and growing credit-led programs have been most successful in achieving substantial levels of cost recovery, although some smaller institutions have also demonstrated strong progress.*<sup>88</sup> Cost recovery is the capacity of an organization to pay its expenses with revenues generated by program operations and/or the management of program financial resources. Microenterprise programs, like many other nonprofit organizations, have grown increasingly concerned with strategies to increase cost recovery and, thereby, their institutional sustainability in the face of scarce resources and fluctuating donor interest. To that end, there is a growing body of practice and literature guiding nonprofit managers in the language and tools of social entrepreneurship, defined as an approach to nonprofit management that involves “the art of simultaneously pursuing both a financial and a social return on investment (the “double bottom line”).<sup>89</sup> For microenterprise programs, financial returns are pursued typically

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<sup>87</sup>For a full discussion, see Elaine Edgcomb and others, *Improving Microenterprise*, 4-21. For more detailed findings on training and technical assistance best practices, see *FIELD Best Practice Guides: Volumes 1-6*.

<sup>88</sup>These organizations appear to do this through either extremely low operating expenses or through earned revenues on donated loan funds.

<sup>89</sup>The Institute for Social Entrepreneurs, *Toward a better understanding of social entrepreneurship: Some important definitions*; available from <http://www.socialent.org/definitions.htm>; Internet.

through interest and fee payments on loans, interest earned on unused loan funds, and fees charged to clients for training and technical assistance services and materials.

Programs reporting to MicroTest that characterize themselves as credit-led (that is, consider lending their primary service) documented, on average, that they recovered 47 percent of the operating costs associated with their lending operations in Fiscal Year 2003. The median was 43 percent.<sup>90</sup> Top performers in the group achieved an operational self-sufficiency ratio of 60 percent or higher.<sup>91</sup> Most programs achieved this return through growing the scale of their lending and/or increasing efficiency in their operations.

But, most programs are not just credit operations. They provide training and technical assistance services for which clients have traditionally paid little or nothing. The average and median cost recovery for training and technical assistance services in 2003 was 6 percent and 4 percent, respectively.<sup>92</sup> There are a few programs that are advancing beyond those numbers, however. The highest cost recovery for training services reported by one organization was 89.5 percent. It is a credit-led organization with a relatively small training program; the course it offers is a one-day training accompanied by up to 10 hours of technical assistance. It has achieved a high level of cost recovery by charging fees for the course and using graduate students who are paid a relatively low rate as trainers. The second highest rate of cost recovery was 41.4 percent, earned by an organization that covers its costs through member fees and revenue sharing with clients who sell products and services through their physical and virtual facilities. In addition, two other organizations earned between 25 and 30 percent of their training and technical assistance costs through methods that included charging sliding-scale fees to clients and curriculum sales. Six others generated between 11 and 17 percent cost recovery. These results suggest that some business development service providers are beginning to increase their sustainability through internally generated resources. Nevertheless, this still remains a challenge for most training and technical assistance providers.

Because most microenterprise programs engage in both lending and training and technical assistance activities, total program cost recovery remains fairly low. The average total program cost recovery for 65 MicroTest programs was 16 percent; the median was 14 percent. The top performers against this measure had total cost recovery rates between 28 and 64 percent and, not surprisingly given the discussion above, were heavily weighted toward credit organizations. The data also show that progress toward self-sufficiency has been made by organizations focusing on the issue, as the trend data below suggest. But, the progress has been hard. The challenge of achieving sustainability in the industry remains critical to its future.

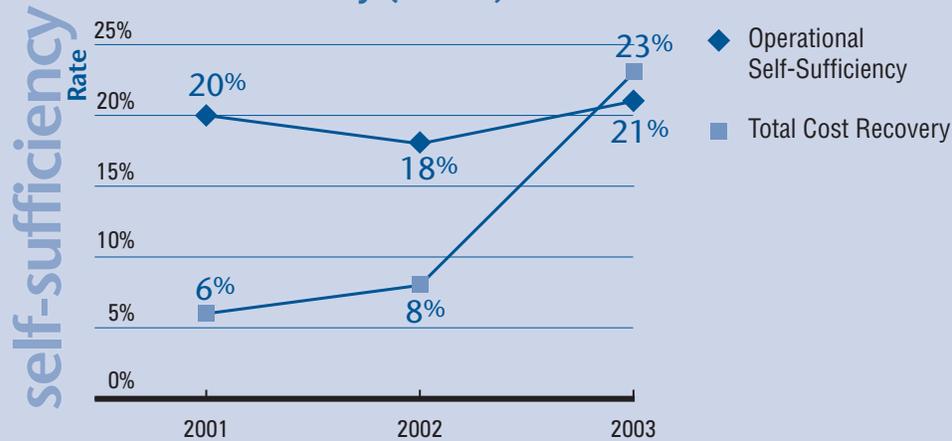
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<sup>90</sup>Twenty-two organizations reported this data.

<sup>91</sup>MicroTest calculates operational self-sufficiency as total financial income (interest and fees on loans and interest on unused loan funds), divided by credit program operating costs for the fiscal year. The top performers are those whose result for the measure falls within the top 20 percent of all reported results.

<sup>92</sup>Sixty organizations reported this data.

**Figure 9: MicroTest Trend Group: Performance on Self-Sufficiency (n = 32)<sup>93</sup>**



## Costs of Service and Costs of Outcomes

Because microenterprise programs are likely to depend on subsidy from private and public sources for some time, it is important to understand whether those funds are being used effectively. The most recent examination of costs and outputs that has been undertaken in the industry is that under MicroTest, where organizations submit a detailed accounting of their costs in relation to services rendered. In addition, new outcomes tracking data presented by a number of MicroTest members allow for a more detailed look at how these costs relate to the early outputs of program services.<sup>94</sup> An initial comparison of program costs to those of other employment strategies aimed at low-income individuals suggests that microenterprise programs have similar costs.

### COSTS OF SERVICE

*MicroTest data during the past four years reveal that the annual costs of service are relatively modest.* Table 10 presents cost data for all reporting MicroTest organizations in two ways – the cost per participant and the cost per client.<sup>95</sup> The first relates total program costs to all participants the program assisted during the course of a fiscal year, including those who may have received minimal amounts of service. The second relates these same costs to individuals that programs consider to be clients, that is, those who receive a substantial amount of service in a given year and who the program anticipates should demonstrate some outcomes as a result of program services.<sup>96</sup>

<sup>93</sup>The MicroTest trend group is slightly weighted toward training organizations. Seventeen of the organizations are training-led and 15 are credit-led. The credit-led organizations in the trend group reported higher rates against each measure.

<sup>94</sup>Please note that this section relates costs to units of service and to the outcomes that clients report after receiving services. Only one study to date has been able to present a full cost-benefit analysis, based on its control group design. See Jacob M. Benus and others, *Self-Employment Programs: A New Re-Employment Strategy, Final Report from the UI Self-Employment Demonstration*, Unemployment Insurance Occasional Paper 95-4 (Washington DC: U.S. Department of Labor, 1995).

<sup>95</sup>The cost per client formula is all program costs/total number of clients. The cost per participant formula is all program costs/total number of participants.

<sup>96</sup>On average, clients who complete a training program and go on to receive a loan receive approximately 45 hours of direct service. This figure is based on an analysis of 4 years of MicroTest data concerning the average number of hours of business development and credit-related training and technical assistance delivered to program clients. Those clients interested in just business development training and technical assistance get, on average, 31 hours of direct service, while those whose training and technical assistance is strictly concerned with getting and repaying a microloan receive approximately 14 hours of direct service.

**Table 10: Microenterprise Program Costs of Service — All Reporting Organizations<sup>97</sup>**

	2000	2001	2002	2003
<b>Cost per Participant</b>				
Average	\$2,392	\$2,309	\$1,775	\$1,346
Median	\$1,119	\$1,309	\$1,082	\$881
n =	49	53	53	60
<b>Cost per Client</b>				
Average	\$3,529	\$3,683	\$2,683	\$2,416
Median	\$2,068	\$2,302	\$2,251	\$1,750
n =	56	59	56	63

These costs of service are in line with those reported by Self-Employment Assistance Programs, implemented by states to assist Unemployment Insurance claimants to establish themselves in self-employment. Costs were reported to range between \$471 and \$4,706 in the seven states of California, Maine, Maryland, New Jersey, New York, Oregon and Pennsylvania.<sup>98</sup>

Furthermore, these costs of service are in line with those of other job creation strategies designed to help low-income individuals improve their incomes. For example, case studies conducted by the Aspen Institute found that a set of workforce development programs using a “sectoral employment strategy”<sup>99</sup> spent between \$2,900 and \$7,911 per trainee for services leading to jobs in a variety of industries – some higher-end like machining, woodworking and construction, and some lower-end like garment making and home health care.<sup>100</sup> In addition, a set of eight social purpose businesses on which Aspen tracked costs between 2000 and 2003 had annual training costs that averaged between

<sup>97</sup>This table presents point-in-time data for all organizations submitting data during a given year. While many organizations are included in each year’s data set, there are others that vary from year to year.

<sup>98</sup>William T. Kosanovich and Heather Fleck, *Final Report: Comprehensive Assessment of Self-Employment Assistance Programs* (Washington, DC: Office of Workforce Security, U.S. Department of Labor, June 2001); available from <http://wdr.doleta.gov/owsdrr/papers/sea.pdf>; Internet. Table 6-7 contains the cost data. Note that the authors report that in some instances, not all costs are included because they were not tracked separately by the states and, in those instances, “actually overall costs are likely higher than those represented in the table.”

<sup>99</sup>Sectoral employment development programs seek to increase employment for low-income workers and/or improve the quality of their jobs by focusing training on a particular, promising industry sector. These programs also seek to influence the industry in which they operate to create better access and to improve job quality.

<sup>100</sup>These costs are based on an analysis of six sectoral employment training programs and use data drawn from financial statements between 1998 and 2000 depending on the institution. The cost per participant for the Garment Industry Development Corporation (New York) in 1998 was \$2,984, for Project Quest (San Antonio) in 1999 was \$4,836, for Cooperative Home Care Associates (New York) in 2000 was \$3,155 (average from 1998 to 2000 was \$2,896), for Asian Neighborhood Design (San Francisco) was \$6,460, for Focus Hope (Detroit) was \$7,911 in 1997, and for Jane Adams Resource Center (Chicago) was \$3,106 in 1998. Participants included all individuals enrolled in the programs’ training services. For more see:

Maureen Conway and Suzanne Loker, *The Garment Industry Development Corporation* (Washington, DC: The Aspen Institute, 1999), 51.

Ida Rademacher and others, *Project Quest* (Washington, DC: The Aspen Institute, 2001), 70.

Anne Insera and others, *The Cooperative Home Care Associates* (Washington, DC: The Aspen Institute, 2002), 73.

Maureen Conway and Marshall Bear, *Asian Neighborhood Design* (Washington, DC: The Aspen Institute, 2000), 58.

Jeffery W. Thompson and others, *Focus:Hope* (Washington, DC: The Aspen Institute, 2000), 55.

Amy K. Glasmeier and others, *Jane Addams Resource Corp* (Washington, DC: The Aspen Institute, 2000), 58.

\$1,567 and \$3,345 during the four years. These businesses trained and employed disadvantaged women in health and child care, crafts, cleaning businesses, and restaurants.<sup>101</sup> Finally, programs that offered transitional jobs and support services to individuals who lacked the work experience, education or training necessary to obtain unsubsidized employment on their own were found to have costs per participant ranging from \$2,011 to \$14,406 for services only, and from \$4,825 to \$16,616, including wages paid by the programs during the period of transitional employment.<sup>102</sup>

## COSTS OF OUTCOMES

More important to understanding the cost effectiveness of microenterprise programs is the consideration of the costs associated not only with serving a client, but also with producing a business outcome. MicroTest's outcomes process helps programs to measure business outcomes for a sample of clients one year after receiving program services. A client is defined as having a "business outcome" if he or she reports being in business at the time of the survey. That business may be a new business started during or after the receipt of program services or a pre-existent business that survived as of the date of the interview. Pre-existent businesses include a range from those that have experienced little or no change to those that report considerable growth in sales and employment.

*FIELD estimates find that the outcomes associated with participation in microenterprise services exceed the costs of providing them and compare favorably to the costs of outcomes associated with other workforce development strategies.* FIELD can estimate the cost per business outcome for 17 organizations that recently submitted data on client outcomes in 2003 and on program costs for Fiscal Years 2000-2002. These estimates find that the cost per business outcome for these microenterprise programs ranged from \$3,255 to \$22,422. The wide range of estimated costs across these organizations appears to flow from differences in their program methodology and the characteristics of the clients served. Although not uniformly the case, programs with lower costs tended to be credit-led organizations, while those with higher costs per business outcome tended to be training-led institutions assisting more disadvantaged individuals. The average cost per business outcome, however, was estimated to be between \$7,420 and \$7,801 (based on a 95 percent confidence interval of the number of business owners among the overall client population).<sup>103</sup>

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<sup>101</sup>Unpublished data from four-year assessment of Ms. Foundation Collaborative Fund for Women grantees, conducted by Aspen/FIELD. For other data from this evaluation, see Jeremy Black, *Enhancing Employment for Low-Income Women: Lessons learned from the third round of the Collaborative Fund for Women's Economic Development*, (Washington, DC: The Aspen Institute/FIELD, August 2004).

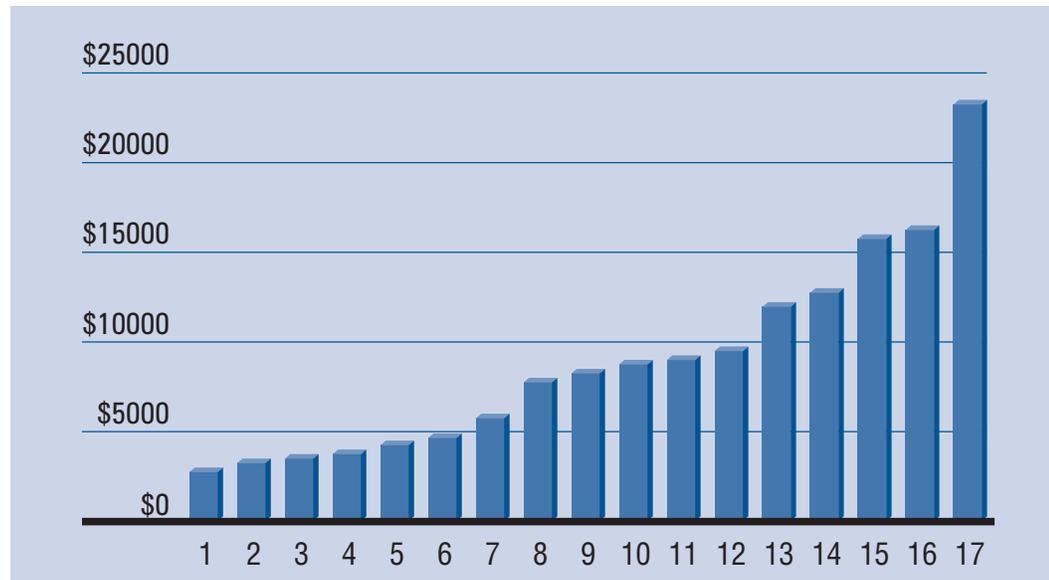
The Aspen Institute, *Enhancing Employment Opportunities for Women: 2003 findings from the third round of the Collaborative Fund for Women's Economic Development* (Washington, DC: The Aspen Institute/FIELD, 2004).

<sup>102</sup>Gretchen Kirby and others, *Transitional Jobs Programs: Stepping Stones to Unsubsidized Employment* Document No. PR02-15 (Washington, DC: Mathematica Policy Research, Inc., April 2002), 47-49; available from <http://www.mathematica-mpr.com/publications/PDFs/transitionalreport.pdf>; Internet.

<sup>103</sup>See Appendix 2 for a discussion of the MicroTest outcomes research and the methodology used to estimate cost per business outcome. Note that because the outcomes research does not use an experimental design, it is not possible to identify to what extent the clients' business outcomes are a result of the program intervention. The methodology does assume that at least some of the benefit was attributable to the program, but not necessarily all of it.

**Table 11: Estimated Cost per Business Outcome for 17 MicroTest Organizations**

Total No. FY 2002 Clients	Estimated Number of FY 2002 Clients in Business	Total Program Costs for Average Period of Client Services (2.6 years: FY 2000 through FY 2002) <sup>104</sup>	Cost per Business Outcome
3,740	2,917 – 3,067	\$22,756,429	\$7,420 – \$7,801



As a comparison, the Aspen-studied workforce development programs mentioned earlier measure costs per job placement and per job retention, with job retention measured at 90 days. Costs for that group of programs ranged between \$4,825 and \$17,141 per job placement and between \$4,260 and \$21,697 per retained job. The costs at the higher end of these ranges are for programs that make placements in highly technical fields like machining. Those at the lower end of the ranges are for programs placing clients in the garment industry, health care and data processing positions.<sup>105</sup> Other workforce studies provide additional points for comparison. The transitional jobs programs, also discussed earlier in this chapter, appear to cost between \$10,010 and \$32,591 per placement of a participant in an unsubsidized job.<sup>106</sup>

In addition, some researchers have looked at the costs of job creation through industrial recruitment strategies involving tax credits and abatements, worker training

<sup>104</sup>Note that 2.6 years of total program costs are included as the average years of program participation per client through the end of FY 2002.

<sup>105</sup>Ida Rademacher and others, 70; Anne Inserra and others, 73; Maureen Conway and Marshall Bear, 58; Jeffery W. Thompson and others, 55; Amy K. Glasmeier and others, 58.

<sup>106</sup>Aspen/FIELD's calculations based on data in Kirby, Hill and others, based on program cost data and placement rates. See Page 49, Table V.3 for costs of program services and supports and Page 62, Table VI.5 for placement rates of four programs. With costs between \$4,825 and \$16,616 and placement rates between 0.467 and 0.703, the costs per placement range between \$10,010 and \$32,591.

programs, infrastructure investments, and site preparation. These studies have also produced a range of results including:

- ▶ Costs per job between \$1,906 to \$10,800 due to cuts in state and local taxes (Bartik, 1992).
- ▶ Costs per factory job ranging from \$11,000 to \$50,580 due to a range of incentive packages assembled for Midwest automobile plants (Milward and Newman, 1989).
- ▶ Cost per job of \$4,857 for jobs produced through an Economic Development Administration-funded Public Works program (May 1997) and between \$3,822 and \$19,393 for an EDA-funded Defense Adjustment Program that provided both infrastructure development and revolving loan funds for military base conversions (Burchell, 1997).<sup>107</sup>
- ▶ A cost of \$13,500 per job due to the New Jobs Tax Credit that offered federal tax credits to employers who expanded employment between 1977 and 1978, and an average cost of \$4,100 (with a range of \$2,460 to \$15,375) for jobs created by the Targeted Jobs Tax Credit that was designed to provide wage subsidies for the disadvantaged.<sup>108</sup>

It should be noted that these cost analyses refer to a range of jobs with varying job quality and designed for individuals with varying levels of disadvantage relative to the labor market. As Servon and Doshna note, microenterprises “do not generate jobs as quickly or in as great quantities as do more traditional economic development strategies.” They also “pay less than traditional industrial jobs,” and they tend not to offer health insurance, retirement plans or other benefits. At the same time, the authors note other advantages of the strategy not captured in traditional economic development analyses, including social welfare outcomes related to “economic literacy, asset generation, increased self-esteem, time management and more stable households.”<sup>109</sup>

*FIELD estimates suggest that the benefits of these microenterprise programs outweigh the costs.* Are the costs of these investments in microenterprise programs justified, given the business outcomes they produce? Assuming that the business produces a multiyear stream of revenue into the household and that revenue exceeds the program’s investment, the answer is “yes.” Data from MicroTest can be used to estimate at least some of the benefits associated with these programs and this analysis suggests that the costs are justified. Of the set of 17 microenterprise programs that reported their costs and business outcomes above, 10 were able to provide pre- and post-program data on the amount of money that this sample of their clients drew from their businesses (as either owners’ draw or salary) in the

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<sup>107</sup>Studies cited in Lisa J. Servon and Jeffrey P. Doshna, “Microenterprise and the Economic Development Toolkit: A Small Part of the Big Picture,” *Journal of Developmental Entrepreneurship* vol. 5, no. 3 (December 2000): 183-208. The studies cited include: Timothy J. Bartik, “The Effects of State and Local Taxes on Economic Development: A Review of Recent Research,” *Economic Development Quarterly* Vol. 6, 1992, 102-110.; R. Burchell, *Defense Adjustment Program. Performance Evaluation* (New Brunswick, NJ: Center for Urban Policy Research, 1997).; R. Burchell, *Public Works Program. Performance Evaluation* (New Brunswick, NJ: Center for Urban Policy Research, 1997); H.B. Milward and H. Newman, “State Incentive Packages and the Industrial Location Decision,” *Economic Development Quarterly* 3(3) 1989, 203-222. Please note that these studies used a variety of methodologies including regression analysis in the case of Bartik and case study methodology in the case of Milward and Newman. They also cover different time periods from the late 1980s through the late 1990s. The figures have not been adjusted to be comparable to the 2003 dollars cited as the costs for MicroTest programs.

<sup>108</sup>Timothy J. Bartik, *Jobs for the Poor: Can Labor Demand Policies Help?* (New York: Russell Sage Foundation, 2001), 226, 229.

<sup>109</sup>Servon and Doshna, 191-192, 196.

year prior to the survey.<sup>110</sup> They also reported the employment generated by these same businesses at program enrollment and at the time of survey. As Table 12 shows, the net change in average draw for all the business owners surveyed was \$4,808. In addition, these same businesses produced a total of 167 full-time and 388 part-time jobs for a total of 361 FTEs (full-time equivalents), for a total increase of 171 employees or .44 employees per business, since program intake.<sup>111</sup> Calculated at federal minimum wage rates, this yields an additional \$4,532 in salaries paid per business. Thus, the total benefit per business is equal to the \$4,808 increase in owner's draw plus the \$4,532 in increased wages, for a total of \$9,340. With a per-business investment estimated between \$6,580 and \$7,094 (again applying a 95 percent confidence interval of the number of businesses),<sup>112</sup> it is estimated that the initial economic return is between 1.3 and 1.4 times the investment.

**Table 12: Costs Compared to Owners' Draw and Estimated Wages Paid by Microenterprises: 10 Microenterprise Programs Reporting<sup>113</sup>**

	Aggregate at Intake	Aggregate at Time of Survey	Change from Intake	Net Change per Business
Cost per business outcome	\$6,580-\$7,094			
Owners' draw	\$2,357,406	\$3,862,448	\$1,505,042	\$4,808
FTEs per business (other than owner)	190 FTEs	361 FTEs	171 FTEs	.44 FTEs
Wages paid per business (estimated)	\$1,957,000	\$3,718,300	\$1,761,300	\$4,532 <sup>114</sup>
Total change:				\$9,340

These data are not based on control group research, and therefore, the change in the income earned and employment generated cannot be ascribed causally to the microenterprise services that these clients received. It also must be acknowledged that program clients entered with varying levels of business experience and received different services. If it is assumed that the whole change is due to microenterprise services, then these services generate “returns” in terms of owners’ draw and wages paid that, on average, exceed the dollars programs invest in them. If it is assumed that half of the change is due to microenterprise services, then the initial return would appear to be less than the investment made to produce it. But, it is important to recognize that this estimate only captures the value of one year of owners’ draw and wages (the year immediately preceding the survey)

<sup>110</sup>While it is more typical to look at change in business profits as an outcome of business development services, this study uses owners’ draw or salary as the outcome measure. In FIELD’s survey research with microentrepreneurs, we have found that microentrepreneurs could much more clearly identify what income they drew from their businesses for personal or household use than they could report profits. For more on this, see Chapter 4.

<sup>111</sup>These job-creation figures are higher than reported data from other studies cited in Chapter 4. The job-producing businesses included in this survey are largely owned by clients from two credit programs (which tend to work with pre-existent businesses seeking financing).

<sup>112</sup>Calculation of costs based on the costs of 10 organizations that provided complete intake and outcomes data on all key variables. Again, please see Appendix 2 for more on these calculations.

<sup>113</sup>Calculations based on clients surveyed by 10 organizations. For owners’ draw, the number responding was 226 at intake and an additional 87 new business owners at the time of survey for a total of 313 respondents; for employees, the number was 277 at intake plus an additional 114 at time of survey for a total of 391 respondents.

<sup>114</sup>Estimate based on the Federal minimum wage rate.

and that individuals who were clients for multiple years would likely have experienced additional benefits in those intervening years. Furthermore, this estimate does not include the full range of financial benefits that the businesses may produce, such as reductions in public benefits and other economic effects in local communities.<sup>115</sup> Moreover, assuming that even half of these businesses survive five years,<sup>116</sup> a reasonable assumption based on longitudinal research, and that the businesses produced owners' draw and wages for these remaining years, then the value of these program investments increases considerably.

Of course, this is just an abbreviated estimate of the outcomes experienced by clients participating in microenterprise programs. There is a larger body of research that more completely addresses the range of outcomes and the specific changes experienced by a broader number of individuals. The learning to date about the outcomes of microenterprise programs will be addressed in the following chapter. While more research clearly is needed on the costs and benefits of microenterprise programs, these initial cost figures do suggest that microenterprise programs are similar in cost to the set of employment interventions for low-income individuals discussed here, and that the average returns from these programs exceed the initial investment.

## **Toward a Social Return on Investment**

Estimating the full social returns on the investments made in microenterprise programs requires a more detailed calculation of the range of benefits produced by the businesses supported. In addition to income drawn from the business to support the owner's household and the value of wages paid to employees, these businesses produce other returns. Many microbusinesses generate and collect sales tax or licensing fees. In addition, clients who use self-employment as their pathway from welfare to work draw less in TANF payments and other public assistance. There are also nonfinancial social benefits that clients report after program participation (as discussed further in Chapter 4).

Researchers interested in developing a social return on investment calculation for microenterprise assistance are looking at a range of possible measures to be included in the calculation, some more generally accepted than others. An early analysis by John Else<sup>117</sup> calculated the value of income and employment produced by typical microenterprises and the reduction in welfare transfers. A more recent study by Marian Doub of Women's Initiative for Self-Employment suggested that in addition to these measures, a social return might also include the estimated increase in revenue circulating in local communities due to the multiplier effect of local expenditure of business revenues, as well as savings to those who self-assess out of the program and

<sup>115</sup>Servon and Doshna, 195. The authors report, for example, that "for every job created by an NEF [Northeast Entrepreneur Fund] customer's firm, an additional 0.9 jobs are created in the local economy." This estimate is based on using "direct-effect multipliers" used for jobs from the RIMS II model for the state of Minnesota.

<sup>116</sup>The Self-Employment Learning Project's longitudinal assessment of microentrepreneurs found that 49 percent of surveyed entrepreneurs were still in business at the fifth year of the study. See Peggy Clark and Amy Kays, *Microenterprise and the Poor: Findings from the Self-Employment Learning Project Five Year Survey of Microentrepreneurs* (Washington, DC: The Aspen Institute), 48.

<sup>117</sup>John F. Else, "Microenterprise Development in the U.S.: Is There a Case for Public Support?" in *The Role of Microenterprise Development in the United States*, ed. Else and others (Geneva: International Labour Organization, 2001) 57-60; available from <http://www.ilo.org/public/english/employment/finance/download/us1.pdf>; Internet.

thereby avoid the loss of resources in failed business ventures.<sup>118</sup> In addition, a study of ACCION Texas by Texas Perspectives, Inc., an economic analysis firm, also calculated the increase in “total economic activity” along with the value of labor compensation and state and local tax revenue.<sup>119</sup> With these additional returns, all these studies report higher returns than the FIELD estimates noted previously.

These studies and others like them face the challenge of attempting to estimate net benefit in the absence of impact data, leaving it to the readers to judge which benefits appear most reasonably the result of microenterprise program interventions and how much of these benefits are due to the intervention, as opposed to other factors. FIELD is now working with others in the industry to develop a more consistent and grounded approach to estimating social returns on investment.

## Conclusion

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**A**s this chapter describes, while the microenterprise industry continues to grow and mature, it already has a number of accomplishments to its credit, as well as serious challenges ahead. The data demonstrate that microenterprise development programs have successfully served the marginal and disadvantaged individuals that the field was designed to assist. Training and technical assistance services can demonstrate considerable effectiveness in helping clients achieve and apply new skills, and credit programs have demonstrated the capacity to manage risk effectively. MicroTest programs have increased their efficiency – as evidenced by declining unit costs – over time. In addition, some preliminary analyses suggest that effective microenterprise programs also operate cost-efficiently and effectively, although more rigorous and extensive analyses need to be done to document the full extent of social returns to the investments made in these programs. Programs also have demonstrated the capacity to cover a portion of their costs with earned revenues, and credit-led programs, in particular, have documented some substantial earned revenue, accounting for 40 percent of their lending costs, on average. Some programs have evidenced even higher levels of self-sufficiency.

Still, training and technical assistance services remain largely subsidized, meaning that the overall program cost recovery in the industry remains fairly low and progress towards self-sufficiency remains slow. Also, while there are strong grounds for advocating public investments in this type of training (virtually no where in the United States are consumers of educational services expected to pay the full cost of their education or training), the reality of scarce resources and limited cost recovery

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<sup>118</sup>Women’s Initiative for Self-Employment, *Women’s Initiative Measures Up: A Report on the Post-Training Outcomes for Microenterprise Training Participants from 1999-2002* (San Francisco: Women’s Initiative for Self-Employment, April 2004), 15; available from <http://www.womensinitiative.org/Publications/WI%20Measures%20Up%20FINAL.pdf>; Internet.

<sup>119</sup>Texas Perspectives, Inc. *The Economic and Community Impact of ACCION Texas Lending*, February 9, 2004, i-iii.

has affected the industry's ability to scale-up to serve more microentrepreneurs. The result is that most programs remain relatively small, serving hundreds rather than thousands of entrepreneurs. As we will explore in Chapter 5 of this paper, solving the twin challenges of sustainability and scale-up may require changes in the design and delivery of products and services, as well as in the organizational structures through which they are offered.



Low-income individuals use and benefit from microenterprise in various ways. Some create their own jobs through self-employment and in so doing increase their family income. Others use self-employment to supplement income from wage employment. Additionally, operating a microenterprise can provide wealth and ownership opportunities to a group that often faces economic exclusion and discrimination. In this chapter we explore the value of microenterprise to low-income Americans.

# The Value of Microenterprise to Low-Income Americans: What Do We Know About the Experiences of Microentrepreneurs?

**T**o assess the value of microenterprise development as a strategy for struggling families and workers, as well as for communities, it is important to understand the outcomes experienced by those who pursue it. Do businesses owned by low-income entrepreneurs survive over time? Do they grow? Do they create jobs? How do low-income families use self-employment as a strategy for creating employment and generating income for themselves? Why do they choose self-employment? What is the contribution of the microenterprise to the family's overall economic condition? Do microentrepreneurs experience other, more qualitative, outcomes that are also important?

Several research efforts have looked at the outcomes experienced by microentrepreneurs (see Table 13 for a summary of the key research efforts discussed here). Only one of these, an evaluation of the U.S. Department of Labor's Unemployment Insurance Self-Employment Demonstrations (UISED), used an experimental design and, therefore, can be considered to test the "impact" of self-employment or microenterprise programs for a particular population – in other words, to identify the relative costs and benefits in a rigorous manner.<sup>120</sup> On the other hand, the other demonstration and research efforts have identified some interesting findings regarding patterns of self-employment and small-scale business ownership among various low-income populations. These findings contribute to our understanding of the value of microenterprise development or self-employment for families struggling at the margins of our economy and labor market. They also provide insights that are useful in informing the design of microenterprise programs. This section presents a review of those research findings, with the goal of distilling what has been learned to date regarding the value of self-employment to low-income families.

In examining these research findings, it is important to recognize that program operators and funders approach microenterprise assistance with varying goals. For some, microenterprise assistance is a means to help low-income individuals to increase their income and assets, thereby seeking to reduce poverty. For others, microenterprise programs are an economic development strategy – a means to create or strengthen small businesses in order to create new jobs and economic activity in a particular neighborhood, city or region. In large part, research on microenterprise programs has focused on the outcomes associated with the former strategy – on low-income individuals and on the increases in income, assets and family well-being that they

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<sup>120</sup>See Benus and others.

experience after receiving microenterprise services. This is largely because the donors that have supported the research are interested in microenterprise as a poverty-alleviation strategy. There has been relatively little study of the economic development outcomes – in the form of job creation, increases in sales and taxes, and so forth – of microenterprise programs. However, there is a growing interest in entrepreneurship within the economic development community, and this may well lead to further research on the economic development outcomes of these programs.

In considering outcomes, it is also important to consider the goals that entrepreneurs are pursuing when they embark on business ownership. Clearly, one of the key goals is to build successful businesses – that survive and grow over time in terms of sales and owners' draw. But, other factors go into individuals' decisions to pursue microenterprise ownership and, therefore, definitions of "success" are not simple. Contribution to, and growth in, family income is an important measure, particularly to those interested in self-employment as a self-sufficiency strategy. Others may look to own a business in order to build an asset for their families or communities. These individuals may choose to reinvest in the business – to grow that asset over time – rather than to draw money out of it to increase their families' standard of living. As has been noted elsewhere in this paper, others may choose business ownership because it offers flexibility to engage in caring for family members or because it allows them to stay in a community despite the lack of wage employment opportunities. In such cases, individuals might be able to earn more money in wage employment, but self-employment is still the preferred choice because it reduces child-care or other caregiving expenses or simply because it allows them to achieve other important family goals. Finally, many individuals pursue owning a business for important non-financial reasons: the ability to be in control of their work environment, to work for themselves rather than others, and to feel a sense of pride in their ability to build a business and engage successfully in the economy.

In this chapter, we examine what research to date tells us about the experiences of low-income microentrepreneurs relative to each of these goals, or measures of success.

### The State of Existing Research

There have been a number of studies conducted on the outcomes of microenterprise programs in the United States.<sup>121</sup> These studies have tracked the experiences of individuals who have received services from a microenterprise program, seeking to describe what these microentrepreneurs and their businesses look like and what changes they experience over time. For the most part, these studies have focused on earliest and large microenterprise programs in this country.

Among these evaluations, two types of bias likely affect the research findings: self-selection bias and survivor bias. Self-selection bias is a factor if individuals who choose to receive microenterprise assistance also possess other traits that could lead to business success. For example, individuals who are attracted to microenterprise programs may also possess such other traits as strong initiative, good planning skills, etc., that would support their success in business ownership.

<sup>121</sup>As discussed in Chapter 3, there have been research efforts focusing on program performance as well.

In the absence of an experimental design, which uses random assignment of those who apply to the program into control and treatment groups, it is not possible to determine to what extent the program services, rather than these traits, led to the outcomes documented in the research.<sup>122</sup> As is noted above, only one of the studies in question (UISED) used an experimental design. Thus, the findings in the other studies are likely affected by some degree of self-selection bias.

Each of the microenterprise program evaluations (including UISED) also faces the limitation of survivor bias. Survivor bias exists when the individuals who are selected into or remain in the study sample exhibit different characteristics from participants who drop out of (or are not included in) the study. In the case of these studies, it is likely that those individuals who remain in the study sample (those who can be located and interviewed in subsequent survey rounds) may be those who are most successful. In at least one study, survivor bias is an issue because the survey sample consisted not of a random or exhaustive sample of all clients, but rather only those clients who received multiple loans.<sup>123</sup> The remaining studies face the issue of sample attrition over time. Several of the studies do include a “respondent analysis” that looks at how those who responded to the follow-up surveys compare to those in the original sample on key observable characteristics. However, there may be some non-observed characteristics which influence outcomes.

Despite lack of experimental design and the issue of survivor bias, we still believe that the findings from these research efforts are valuable. They have provided initial insights on many key issues, including: the types of businesses that the program clients created, the extent to which clients engaged in both self- and wage employment (patching), the types of businesses that performed best, the scale of businesses operated by program participants, employment in the microenterprises, the growth of the businesses over time, and the acquisition of assets by business owners. Practitioners and funders have used these research findings to inform the design of microenterprise services. And, as this chapter will describe, while definitive impact data are not available, there is evidence from the research that clients found value in program participation, and that the information and skills they received were used in running their businesses. As a result, it is likely that at least some of the changes observed in these microenterprise program clients are attributable to the services they received. As we note at the end of the chapter, additional research, including studies using a more rigorous, experimental research design, is needed in order to further identify the outcomes and impact associated with investments in microenterprise programs. The research conducted to date provides a good starting point for the design and direction of this future research.

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<sup>122</sup>There are econometric techniques that can be used to address the issue of self-selection bias. It is important to note, however, that it is not clear that either such statistical techniques, or the use of an experimental design, can completely control for self-selection bias.

<sup>123</sup>Christina Himes and Lisa J. Servon, *Measuring Client Success: An Evaluation of ACCION's Impact on Microenterprises in the United States*. U.S. Issues Series, Document No. 2 (Cambridge, MA: ACCION International, April 1998), 18.

**Table 13: Key Studies of Microenterprise Outcomes for Low-Income Individuals**

Research/Report Title	Research Sample	Research Design	Authors/Research Organization; Date of Study
Microenterprise as a Welfare to Work Strategy: Two-Year Findings (WTW)	595 recipients of Temporary Assistance for Needy Families who received microenterprise services.	Interviews conducted at enrollment in microenterprise program and at one- and two-year follow-up (1990-2002). Pre/post design. No control group or comparison group.	FIELD; Joyce Klein, Ilgar Alisultanov, Amy Kays Blair; 2003
Microenterprise and the Poor: Findings from the Self-Employment Learning Project Five-Year Survey of Microentrepreneurs (SELP)	133 microentrepreneurs with incomes below 150% of the federal poverty line; entrepreneurs enrolled after receiving services from a microenterprise program.	Interviews conducted over a five-year period (1991-1997) at roughly 1-1/2 year intervals. Not a pre/post design; no control or comparison group.	Self-Employment Learning Project; 1999
Kitchen Capitalism: Microenterprise in Low-Income Households	86 low-income entrepreneurs from the SELP sample (see above).	Qualitative interviews conducted in the fourth year of the SELP study (1996-97). Analysis of quantitative data on the entrepreneurs in the SELP study. No comparison or control group.	Margaret Sherrard Sherraden, Cynthia K. Sanders, Michael Sherraden; 2004
Self-Employment Investment Demonstration Final Evaluation Report (SEID)	120 AFDC recipients who started businesses, and had received services from a microenterprise program.	Interviews conducted in 1994. Random sample of business owners from the SEID demonstration sites. No comparison or control group.	Salome Raheim and Catherine Alter; 1995
Self-Employment Programs: A New Re-Employment Strategy, Final Report from the UI Self-Employment Demonstration (UISED)	1,507 unemployment insurance claimants in Washington State (755 in treatment group; 752 in control group). 1,222 UI claimants in Massachusetts (614 in treatment group; 608 in control group).	Data collected in on-line Participant Tracking System, plus two telephone surveys (at approximately 20 and 32 months after enrollment). Uses experimental design including control groups.	Jacob M. Benus, Terry R. Johnson, Michelle Wood, Neelima Grover and Theodore Shen; 1995
Measuring Client Success: An Evaluation of ACCION's Impact on Microenterprises in the United States (ACCION)	Clients of ACCION's U.S. network who had received multiple loans as of June 30, 1997.	Quantitative analysis of data collected from clients at the time of loan application; qualitative analysis of interview data from 72 ACCION clients. No comparison or control group.	Christina Himes with Lisa J. Servon; April 1998
Women's Initiative Measures Up: A Report on Post-Training Outcomes for Microenterprise Training Participants from 1999-2002	196 who participated in Women's Initiative core training between 1999 and 2002.	Baseline information from client applications at program intake; follow-up surveys with program clients at 6, 12 and 18 months after training graduation. No comparison or control group.	Marian Doub; April 2004
Enhancing Economic Opportunity through Entrepreneurship: Lessons Learned from the Third Round of the Collaborative Fund for Women's Economic Development	276 clients who received services from eight Ms. Foundation-funded microenterprise programs during Fiscal Year 2002.	Baseline information from clients taken at program enrollment, follow-up surveys with clients conducted in 2003. Program performance data also submitted for fiscal year 2002.	FIELD; 2004
Microenterprise Versus the Labor Market Among Low-Income Workers	80 low-income SELP program clients who were interviewed in both 1991 and 1995; matched to 109 self-employed workers and 241 low-income wage workers in the Panel Study of Income Dynamics.	Quasi-experimental research design using matched comparison groups and repeated measures.	Cynthia K. Sanders; August 2000
Micro-Enterprise and Women: The Viability of Self-Employment as a Strategy for Alleviating Poverty	Data from the U.S. Bureau of the Census' Survey of Income and Program Participation (SIPP) for 1984, 1986, 1987 and 1988 on: self-employed current and former welfare recipients, women who packaged either wage or self-employment work with welfare, and non-employed welfare recipients.	Analysis of quantitative data from SIPP, combined with qualitative data from interviews and focus groups with women participating in microenterprise programs.	Roberta Spalter-Roth, Enrique Soto, Lily Zandniapour; 1994

## The Size, Growth and Survival of Microenterprises

At their core, of course, microenterprise programs are about starting and growing businesses. Thus, any effort to assess their success or value must begin with a look at the extent to which programs are effective in reaching this goal. In many communities, microenterprise is pursued as an economic development strategy – toward the goal of growing and supporting small, locally owned businesses. As the first chapter of this report details, not all microentrepreneurs are low-income. In fact, most probably are not. In addition, microenterprise programs vary in the extent to which they target low-income individuals – in part based on whether their primary goals are to support individuals facing economic difficulties or to support broader community development goals. Nevertheless, research shows that the businesses owned by low-income individuals can and do contribute to the local economy, as well as to the well-being of the owner and his or her family. To understand the extent to which this is so, it is important to understand the size, durability and growth rates of these small firms.

Therefore, this section outlines what is known about the development of businesses owned by low-income microentrepreneurs.

*Individuals who participate in microenterprise programs increase their rate of business ownership.* Studies that use a “pre- and post-program” design found that program clients showed a higher rate of business ownership after receiving services from a microenterprise program.<sup>124</sup> This was the case in both sites in the UI Self-Employment Demonstration, although the effects in Washington State were much stronger than those in Massachusetts.<sup>125</sup> In the study of TANF recipients conducted by FIELD (referred to in this report as the WTW study), 23 percent of study participants<sup>126</sup> were engaged in self-employment at the time they enrolled in a microenterprise program. When interviewed two years later, 37 percent were currently engaged in self-employment and 49 percent had been self-employed at some time during the previous year.<sup>127</sup>

*The types of businesses owned by low-income entrepreneurs are predictable given the labor market skills of the owners.* Microenterprise programs are built around the premise that there are low-income individuals who have productive skills, but often lack adequate opportunities for wage employment. Microenterprise programs seek to provide these individuals with the business knowledge and access to capital that can enable them to create a business that builds upon those productive skills. Research on low-income microentrepreneurs reinforces the finding that the businesses they create build off the existing labor force skills of the owners. Most low-income entrepreneurs start businesses in sectors such as child care; cleaning, construction and repair services; health and personal services (such as hair care); retail sales; and arts and crafts.<sup>128</sup>

<sup>124</sup>Only some of the outcomes studies collected data on clients both before and after receiving services from a microenterprise program.

<sup>125</sup>Benus and others, vi–vii.

<sup>126</sup>In this chapter, the term “participants” is used differently from the previous chapter. This chapter discusses the outcomes experienced by individuals who received microenterprise services, and in many cases, refers to those studied as the “study participants.” In many of the studies cited, these individuals received a sufficient level of services to be considered a “client” rather than a “participant” under the MicroTest definitions described in Chapter 3. In other cases, the level of services received by the study participants varies, such that some would be program “clients” and others “participants” under the MicroTest definitions.

<sup>127</sup>Joyce Klein and others, *Microenterprise as a Welfare to Work Strategy: Two-Year Findings* (Washington, DC: The Aspen Institute, 2003), 15–16.

<sup>128</sup>Amy Kays Blair and Joyce Klein, *Microenterprise as a Welfare to Work Strategy: One-Year Findings*. (Washington, DC: The Aspen Institute, October 2002), 42.; Salome Raheim and Catherine Foster Alter, *Self-Employment Investment Demonstration Final Evaluation Report* (Washington DC: Corporation for Enterprise Development, April 1995), 33.; Peggy Clark and Tracy Huston, *Assisting the Smallest Businesses: Assessing Microenterprise as a Strategy for Boosting Poor Communities* (Washington, DC: The Aspen Institute, August 1993), 14.; Jeremy Black, *Enhancing Economic Opportunity Through Entrepreneurship* (Washington, DC: The Aspen Institute, August 2004), 8–10.

*Microenterprises owned by low-income program clients are generally small in terms of sales.* As the table below indicates, research shows that the businesses owned by most microenterprise program clients have less than \$50,000 in annual sales.

**Table 14: Annual Revenues of Microenterprises**

Name of Study	Annual Revenues		Number of Businesses	Follow-up Period
	Median	Average		
Ms. Foundation <sup>129</sup>	\$18,000	\$47,381	222	Average 2.9 years after program enrollment
SELP <sup>130</sup>	\$17,600	\$30,436	30	Five years
WTW <sup>131</sup>	\$6,500	\$12,225	128	Two years
SEID <sup>132</sup>	n/a	\$21,231	120	Average 2.6 years

The finding that the annual revenues of businesses in the SEID and WTW studies were lower than those in the SELP and Ms. Foundation studies is not surprising, given that the former studies focused on welfare recipients who were less likely to be in business at the time they enrolled in the microenterprise program. As is described below in greater detail, microbusinesses that are older tend to have higher levels of sales and owners' draw.

*While small, the microenterprises owned by low-income individuals are not substantially different in size from other very small firms.* Most sole proprietorships and non-employer firms – owned by individuals of all income levels – are quite small in terms of revenues. For example, in 1998, 86.3 percent of women-owned sole proprietorships<sup>133</sup> in the United States had total receipts less than \$50,000, and 41.75 percent had receipts less than \$5,000. Average gross receipts were \$23,170.<sup>134</sup> Non-employer businesses (businesses of all legal structures that employ the owner only) were somewhat larger, with average sales of \$42,988 in 2001.<sup>135</sup> To the extent that business sales are lower among the firms owned by low-income entrepreneurs, this may be partly attributable to the fact that their businesses are concentrated in industries that have generally lower average sales.<sup>136</sup>

<sup>129</sup>Unpublished data from Ms. Foundation study conducted by FIELD. For information on this study, see Black, *Enhancing Economic Opportunity Through Entrepreneurship*, 3-5.

<sup>130</sup>Clark and others, 51. These data are for 30 low-income entrepreneurs who reported business revenues in Years 1 and 5 of the study; figures are expressed in 1995 dollars.

<sup>131</sup>Klein and others, 50.

<sup>132</sup>Raheim and Alter, 37.

<sup>133</sup>A sole proprietorship is an unincorporated business with a single owner. It is the most commonly used legal form of ownership for new businesses. SBA Office of Advocacy, *Dynamics of Women-Operated Sole-Proprietorships, 1990-1998* (Washington, DC: Small Business Administration, March 2003); available from [http://www.sba.gov/advo/stats/rwosp\\_03.pdf](http://www.sba.gov/advo/stats/rwosp_03.pdf); Internet.

<sup>134</sup>SBA Office of Advocacy, March 2003, 13.

<sup>135</sup>U.S. Bureau of the Census, *EPCD Nonemployer Statistics* (2001); available from <http://www.census.gov/epcd/nonemployer/2001/us/US000.HTM>; Internet.

<sup>136</sup>For example, among women-owned sole proprietorships, some of the largest grossing businesses are those in the carpentering and floor carpenters, specialty trades, real estate and consulting, and research industries. While some low-income entrepreneurs do work in the contracting and specialty trades industries, relatively few are in the real estate and consulting fields. SBA Office of Advocacy, March 2003, 20.

*There is a set of microentrepreneurs whose businesses become very successful, moving beyond microbusinesses to small businesses.* Every microenterprise program can identify its real success stories – those whose products or services break through to larger markets and grow to become significant revenue and employment generators. The study of Ms. Foundation-funded programs identified a set of 15 high-performing businesses.<sup>137</sup> The median sales for these businesses were more than \$125,000. As the table below indicates, these 15 high-performing businesses also generated impressive employment, employing a total of 40 full-time and 25 part-time workers, including the owner. Counting the owners, the high-performing businesses employed 95 people (6.3 per business) – 27 percent of all jobs created by businesses in the overall sample.<sup>138</sup>

**Table 15: High Performing Businesses in the Ms. Foundation Study**

	Average	Median	Total	Sample Size
Business sales	\$194,784	\$127,000	\$2,921,753	15
Owners' draw	\$23,933	\$25,000	\$359,000	15
Household income at program intake	\$42,450	\$48,000	\$551,854	13
Household income at survey	\$52,429	\$48,250	\$734,000	14
Owners' draw/household income	48%	n/a	n/a	14
Full-time jobs (includes owner)	3.7	3	55	15
Part-time jobs (includes owner)	2.7	1	40	15
Total jobs	6.3	n/a	95	15

*Microbusinesses that receive assistance from microenterprise programs grow over time.* Entrepreneurs in WTW, SELP and ACCION studies grew their businesses over time. Among the businesses that survived for two years in the WTW study, median monthly sales increased by \$600, or 200 percent. Business assets grew by \$3,400, an increase of 243 percent, while median net worth grew by almost \$3,000, more than 250 percent.<sup>139</sup> The SELP study found that while average business revenues decreased slightly over the five-year course of the study (from \$32,211 in Year 1 to \$30,436 in Year 5), median annual revenues more than doubled, from \$9,124 to \$17,600.<sup>140</sup> Finally, ACCION clients who had received three loans increased their average monthly profits by 47 percent, their business equity by 42 percent, and their take-home income by 38 percent over an average of 17 months.<sup>141</sup> These research findings do demonstrate that the businesses grew in the period after the owners received services from a microenterprise program. However, it is important to note that these studies did not use experimental designs, so it is unclear how much of this growth would have occurred without assistance from the microenterprise program.

<sup>137</sup>These 15 high-performing businesses each achieved at least \$70,000 in annual sales.

<sup>138</sup>Black, *Enhancing Economic Opportunity Through Entrepreneurship*, 6-7.

<sup>139</sup>Klein and others, 51.

<sup>140</sup>Clark and others, 51.

<sup>141</sup>Himes and Servon, 73. It is important to note that these findings are likely influenced by survivor bias, in that clients that received three loans are likely to be the program's most successful business owners.

*The survival rates of businesses owned by low-income entrepreneurs compare favorably with those of other small businesses.* Some observers of the U.S. microenterprise industry have expressed concern that given the challenges that low-income entrepreneurs face, their businesses will be doomed to high failure rates. However, the research evidence to date suggests that this is not the case. In the WTW study, 68 percent of respondents who were in business at the time they enrolled in the microenterprise program were still in business two years later.<sup>142</sup> The SELP study found that 49 percent of the microbusinesses survived over a five-year period, and the SEID research found that 79 percent of businesses in the sample survived until the time of the follow-up study (an average of 2.6 years).<sup>143</sup> These survival rates are comparable to those of non-employer firms; the SBA reports that “two-thirds of new employer firms survive at least two years, and about half survive at least four years.”<sup>144</sup>

*Microenterprises owned by disadvantaged individuals provide jobs for individuals other than the owners of the businesses; however, generally job growth is concentrated in a relatively few firms.* Studies of low-income microenterprises generally find that each business generates about 1.5 jobs. Most microenterprises employ only the owner. For example, the SELP study found that in the baseline year, 25 percent of the businesses owned by low-income entrepreneurs employed workers other than the owner,<sup>145</sup> while the WTW study found that 12 percent of the businesses had additional employees.<sup>146</sup> While some of the jobs in these microenterprises are full time, most are part-time or seasonal jobs. Firms in the WTW study employed, on average, one-half a job (in addition to that for the owner); the large majority of additional jobs created were part-time jobs. Findings from the SEID study were strikingly similar; these businesses created an average of .53 jobs in addition to that for the owner; of 72 jobs created, 10 were full time, 54 were part time, and 8 were seasonal jobs.<sup>147</sup> The study of Ms. Foundation-funded microenterprise programs found that the enterprises created an average of 2.2 jobs per business.<sup>148</sup> ACCION’s study of its loan clients who received two to four loans found that they generally created about 1.5 FTE jobs. It does appear, perhaps not surprisingly, that more job creation does occur in microenterprises owned by less-disadvantaged individuals. In the SELP study, 31 percent of businesses in the overall sample had employees, compared to 25 percent in the poverty sub-sample.<sup>149</sup> Similarly, the ACCION study examined the characteristics of the businesses that created more jobs and found, not surprisingly, that the job creators were generally more financially stable than their typical client.<sup>150</sup>

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<sup>142</sup>Klein and others, 48.

<sup>143</sup>Clark and others, 48; Raheim and Alter, ix.

<sup>144</sup>Small Business Administration Office of Advocacy, *Small Business by the Numbers* (May 2003); available from <http://www.sba.gov/advo/stats/sbfaq.html>; Internet.

<sup>145</sup>Clark and others, 49.

<sup>146</sup>Klein and others, 50. The WTW study found that two years after enrolling in a microenterprise program, 16 of 133 operating businesses employed workers other than the owner.

<sup>147</sup>Raheim and Alter, xi.

<sup>148</sup>The Aspen Institute, 3. The employment outcomes for Ms. grantees are likely higher because the Ms. funding focused specifically on supporting business growth.

<sup>149</sup>The Aspen Institute, *SELP Longitudinal Study of Microentrepreneurs: Major Findings Change Over Time* (Washington DC: The Aspen Institute, April 1998), 14; available from <http://fieldus.org/publications/SELPLong.pdf>; Internet.

<sup>150</sup>Himes and Servon, 23.

*While these microbusinesses as a group grew and survived over time, the returns varied dramatically across industry sectors.* In particular, firms in the services sector show higher survival rates, and higher returns in the form of owners' draw, than those in the retail sector. In the SELP study, the large majority of business failures were in the retail and wholesale trade sectors; those in the services and manufacturing sectors fared much better.<sup>151</sup> The WTW study examined levels of business sales and earnings (owners' draw) by sector and found that businesses in the child care, personal, business and professional services, and the construction and home and vehicle repair industries showed higher levels of sales and earnings. On the other hand, businesses that made and/or sold food, clothing, apparel and accessories, gifts, parties and flowers, and arts and crafts showed low levels of sales and earnings. Findings from the Ms. Foundation-funded programs were very similar.<sup>152</sup> As we note below, several factors likely underlie the key role that business sector plays in the performance of these businesses. Given that one of the microenterprise industry's key goals is to improve the economic lives of low-income individuals, it will be important for programs to learn more about and respond to this information.

### **Why are Microenterprises in Service Industries Higher-Performing ?<sup>153</sup>**

Several microenterprise studies have found that clients with businesses in service sectors show higher average levels of sales and earnings than those that are retail-oriented. There are several factors that likely contribute to this outcome:

- ▶ The services sector is growing rapidly in the U.S. economy.
- ▶ Service businesses face less competition from the types of large-scale, low-cost firms that exist in the manufacturing and retail sectors.
- ▶ Businesses in several of the services industries – notably business and professional services – may be able to tap more upscale markets than those focused on the sales of items – particularly if the retail business is located in a low-income community.
- ▶ Service businesses often involve lower non-labor costs, as they do not require the acquisition of significant inventory, materials, or retail or production space. In many cases, the primary cost is that of the labor involved in providing the service. Thus, to the extent that the primary labor in the business is the owner, he or she can draw more income out of the business. For example, in the SBA's study of women-operated sole proprietorships, the top service-oriented businesses showed a ratio of net income to gross receipts that ranged between 35 percent and 54 percent. On the other hand, for businesses in the contracting, carpentry and door-to-door sales industries, this percentage ranged from 3 percent to 15 percent.<sup>154</sup>
- ▶ Finally, for entrepreneurs without much access to business credit, it may be easier to grow a service business, as the level of financing required (to purchase inventory or materials) is reduced.

<sup>151</sup>Clark and others, 49.

<sup>152</sup>Black, *Enhancing Economic Opportunity Through Entrepreneurship*, 8-10.

<sup>153</sup>Excerpted from Klein and others, 57.

<sup>154</sup>SBA Office of Advocacy, 20.

In summary, low-income entrepreneurs who receive assistance from microenterprise programs do increase their rate of business ownership, and most of their businesses do grow and survive over time.<sup>155</sup> Although the firms created by low-income entrepreneurs are small, they are similar in size to other sole proprietorships and non-employer firms in the industries in which they are located. Some microenterprises also contribute jobs to the local economy, although initially most of the jobs created are part time in nature, and many of the jobs are concentrated in a few high-growth firms. Importantly, research is beginning to indicate that some industries hold stronger promise for growth and success in microenterprise; it will be important to explore the implications of this finding for program practice.

## **The Contribution of Microenterprises to Employment and Family Income**

Because microenterprise development – particularly as targeted to low-income or disadvantaged entrepreneurs – has been advanced as a poverty alleviation strategy, there have been several research efforts that have looked at the income changes experienced by low-income and disadvantaged individuals pursuing self-employment. These studies have found individuals who participate in microenterprise programs experience increases in income. The businesses they start play various roles within the household’s “economic portfolio” – the mix of activities and resources that the household engages in and applies to generate income and assets for the family.<sup>156</sup> Sometimes these enterprises provide full-time work for a family member and are a significant source of income; in other cases, the businesses are part time and serve as a supplement to wage income. The research also finds that low-income individuals who pursue self-employment on average experience substantial percentage increases in household income, and some are able to move above the poverty line.

The key studies that examine outcomes experienced by low-income entrepreneurs include several studies of self-employment among welfare recipients, two studies that looked at the experiences of unemployed individuals who participated in self-employment programs, and several studies that examined the role of microenterprise in low-income households.<sup>157</sup> The broad findings of these efforts follow.

*Those pursuing business ownership experienced income growth over time.* Each of the studies that tracked incomes of individuals who pursued microenterprise development found that their incomes increased over time. It is important to note that studies did track incomes differently; some looked at personal or earned incomes, and others examined family incomes. However, in each case, those pursuing self-employment experienced absolute growth in incomes. For example, in the evaluation of the Mott Foundation’s Welfare to Work (WTW) initiatives, TANF recipients with self-employment earnings experienced a 78 percent increase in household income in the two years after participating in a microenterprise program – from a median of \$10,400 to

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<sup>155</sup>Because the studies cited in this section did not use an experimental design, it is unclear to what extent the growth and survival of these firms results from the microenterprise assistance they received.

<sup>156</sup>For more on this model, see Martha Alter Chen and Elizabeth Dunn, *Household Economic Portfolios* (Washington, DC: U.S. Agency for International Development, AIMS, 1996); available from <http://www.usaidmicro.org/pubs/pubsTemplate.asp?page=/componen/aims/pubs/english/desk7.htm>; Internet.

<sup>157</sup>Among these studies only the UISED research used an experimental research design.

\$18,500.<sup>158</sup> Similarly, the final evaluation of the Self-Employment Learning Project (SELP) found that the 72 percent of low-income entrepreneurs experienced growth in household income over a five-year period,<sup>159</sup> and that median household income of the study participants grew by \$10,303, or 91 percent, during that same period.<sup>160</sup> It is important to note that in both of these studies, growth in a range of income sources, including income from other family members, contributed along with business income to the overall growth in household income. However, entrepreneurs who participated in Women's Initiative for Self Employment's core training program experienced an 85 percent growth in average personal earned income in the 18 months after they completed training.<sup>161</sup> Similarly, the study of microentrepreneurs who received multiple loans from affiliates of the ACCION U.S. Network found that average monthly take-home income from the business grew.<sup>162</sup>

*For many families, the increase in family income is sufficient to take them above the poverty line.* The SELP study found that 53 percent of the low-income entrepreneurs it tracked were able to move out of poverty (defined in that study as 150 percent of the federal poverty line)<sup>163</sup> over the five-year study period. In the WTW study, the percent of respondents living above 100 percent of the federal poverty line increased from 20 percent to 56 percent over a two-year period.<sup>164</sup> Similarly, the Women's Initiative study found that the percent of its training clients in poverty declined from 70 percent at baseline to 28 percent eighteen months later.<sup>165</sup> Again, in at least some of these studies, increases in other forms of household income also contributed to the movement out of poverty, but the business was one source of additional financial resources.

*Low-income individuals show particularly strong growth in income.* Interestingly, two of the studies found that low-income individuals show the strongest growth in family income after participation in a microenterprise program. For example, ACCION's study found that while the incomes of all entrepreneurs grew on average, low-income entrepreneurs experienced the greatest growth in income (in both percentage and absolute terms).<sup>166</sup> The SELP study found that while the average incomes of low-income entrepreneurs increased over the five years of the study; those of non-poor respondents actually decreased.<sup>167</sup> It is important to note that low-income entrepreneurs may see more growth in family income because they need to – because they have less of an ability to defer income growth in favor of reinvesting profits into their businesses. For example, the ACCION study found that as the incomes of their

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<sup>158</sup>Klein and others, 25.

<sup>159</sup>Clark and others, 18.

<sup>160</sup>Unpublished data from the SELP study. Published data from the SELP study found that average income grew by \$8,484, or 61 percent. Clark and others, 16.

<sup>161</sup>Women's Initiative for Self-Employment works with microentrepreneurs in the San Francisco Bay Area. Almost all of its clients are low-income according to HUD guidelines; 24 percent had incomes below federal poverty guidelines. See Women's Initiative for Self-Employment, *Women's Initiative Measures Up*.

<sup>162</sup>Himes and Servon, 18. Fifty-six percent of ACCION clients were low-income according to HUD guidelines; 13 percent had incomes below the poverty line.

<sup>163</sup>Clark and others, 16.

<sup>164</sup>Klein and others, 35.

<sup>165</sup>Women's Initiative, 16.

<sup>166</sup>Himes and Servon, 18.

<sup>167</sup>The Aspen Institute, *SELP Longitudinal Study*, 8; available from <http://fieldus.org/publications/SELPLong.pdf>; Internet.

## Measuring Profits or Income?

Ideally, the best way to measure the value of the business to the household would be to track profits (business revenues less business expenses) over time. However, in the course of its research with low-income microentrepreneurs, FIELD has learned that many entrepreneurs do not have a very clear idea of their profits. This stems from a variety of factors, including: that some entrepreneurs vary in how they pay themselves (e.g., taking an owners' draw or alternatively a regular salary), the quality of their financial recordkeeping, and the degree to which household and business finances are commingled.<sup>169</sup> In the course of conducting interviews, FIELD has found that answers to questions about how much money the entrepreneur took out of the business seem to be more reliable than answers to questions relating to "profits." As such, FIELD's more recent survey research looks at the issue of income drawn from the business, rather than profitability.

clients grew (to a level of roughly \$25,000 annually), they were able to direct more of their business earnings toward investment in the business.<sup>168</sup>

*Some families use self-employment income as a key supplement to wage income.* Several studies have found that some of those who pursue microenterprise development use their businesses as part of an income-generating strategy that also includes wage employment – referred to here as "income patching".<sup>170</sup> For example, 37 percent of the entrepreneurs in the SELP study worked at a job as well as running a business.<sup>171</sup> And, in the WTW study, 25 percent of respondents combined wage and self-employment.<sup>172</sup> At least in the short run, these businesses tend to be small and contribute a modest amount of

the total family income. While those who pursue these multiple-income strategies tend to work more hours, they also show higher family incomes as a result.

For example, the WTW study took a close look at the experiences of participants who chose to engage in both self- and wage employment. It found that "patchers" had the highest household incomes (compared to those who earned income solely from either wage or self-employment, or those without any earned income). These "patchers" experienced a 126 percent growth in median income – an increase of more than \$12,000 – over a two-year period.<sup>173</sup> At the same time, the patchers worked more hours (median of 47 hours per week) than those who engaged solely in wage or self-employment (median of 40 hours per week).<sup>174</sup> This finding is echoed in research conducted by the Institute for Women's Policy Research, which found that self-employed welfare recipients who also had earnings from other sources (including from other earners in the family) spent fewer months in poverty and had a higher level of

<sup>168</sup>Himes and Servon, 20.

<sup>169</sup>Margaret Sherraden and others also discuss the challenges involved in obtaining financial information from low-income entrepreneurs. Sherraden and others, *Kitchen Capitalism*, 109.

<sup>170</sup>These include FIELD's WTW study and its research on the informal economy, as well as the Women's Initiative study. In FIELD's work on the informal economy, patching is defined as "a term used to describe the multiple economic activities that one individual engages in to generate an income. In addition, a household may have other income streams contributed by other family members." Edgcomb and others, *The Informal Economy: Making it in Rural America*, 21.

<sup>171</sup>The Aspen Institute, *SELP Longitudinal Study*, 5.

<sup>172</sup>The study found that 25 percent of respondents engaged in both self-employment and wage employment during the second year after program enrollment. Klein and others, 16.

<sup>173</sup>Klein and others, 25.

<sup>174</sup>Klein and others, 18

family income relative to the poverty level than other groups of welfare recipients. The research also found that those who were engaged in self-employment, among other income generating activities, worked more hours.<sup>175</sup>

*The contribution of business draw to family income varies based on several factors, including the amount of time spent working in the business and the length of time in business.* In the WTW study, business draw comprised 42 percent of family income for those who earned income solely from self-employment. Among earned-income patchers, business draw contributed 16 percent of family income.<sup>176</sup> In the ACCION study, the microenterprise contributed between 62 percent and 70 percent of family income for low-income entrepreneurs.<sup>177</sup> In the Ms. Foundation study, business owners who operated their businesses as a full-time enterprise drew an average of slightly less than \$11,000 from their businesses; this draw represented almost 30 percent of the total household income. Business owners who worked in their enterprises on a part-time basis took an average of \$2,305, or 6 percent of the total household income, from their businesses.<sup>178</sup>

As the table below indicates, in the study of Ms. Foundation-funded programs, the businesses contributed an average of \$10,309, or 28 percent, of household income. The percentage contribution was larger for businesses in existence for longer periods of time.<sup>179</sup> Note these findings may partially be explained by the fact that businesses that contribute small amounts to the family may be less likely to survive over time.

**Table 16: Business Contribution to Household Income:  
Client Outcomes for Ms. Foundation-funded Programs  
FY 2003 Clients**

Years in Business	Number of Businesses	Household Income	Owners' Draw	Owners' Draw as Percent of HH Income
Up to 12 months	10	\$28,021	\$1,320	5%
1 to 3 years	53	\$34,575	\$8,549	25%
3 to 5 years	59	\$39,163	\$8,430	22%
5 or more years	59	\$38,674	\$15,292	40%
All businesses	181	\$37,044	\$10,309	28%

*While some studies have shown dramatic changes in the economic situations of low-income entrepreneurs, others find that while the majority of households are able to achieve incomes above the poverty line, many still struggle to afford key needs.* In the Women's Initiative study, 50 percent of participants achieved economic self-sufficiency

<sup>175</sup>Roberta Spalter-Roth and others, *Micro-Enterprise and Women: The Viability of Self-Employment as a Strategy for Alleviating Poverty* (Washington, DC: Institute for Women's Policy Research, 1994), 12 and 21.

<sup>176</sup>Klein and others, 28.

<sup>177</sup>Himes and Servon, 20.

<sup>178</sup>Black, *Enhancing Economic Opportunity Through Entrepreneurship*, 5.

<sup>179</sup>Unpublished data from Ms. Foundation study conducted by FIELD. Key study findings can be found in The Aspen Institute, *Enhancing Opportunities for Entrepreneurship*, and Black, *Enhancing Economic Opportunity Through Entrepreneurship*.

within 18 months of completing microenterprise training.<sup>180</sup> While the progress shown in that study was substantial, the income changes in other studies were more modest. The SELP study found that low-income entrepreneurs had average household incomes of \$22,374 (in 1995 dollars) and median household incomes of \$21,600 in the fifth year of the study, and that 53 percent of entrepreneurs had incomes above 150 percent of the federal poverty line.<sup>181</sup> The WTW study found that study participants had average incomes of \$22,288 and median incomes of \$18,952 two years after enrolling in microenterprise programs. Among these, those with earned income solely from self-employment had median incomes of \$18,500; earned income patchers had median incomes of slightly less than \$23,000.<sup>182</sup> Fifty-six percent of respondents had incomes above the federal poverty line at the two-year follow-up.<sup>183</sup>

Thus, while the incomes of most families had risen above the poverty line, many remained within the ranks of the working poor. For these families, affording health insurance was a significant challenge. While 79 percent of the WTW study participants had health insurance two years after enrolling in the microenterprise program, 59 percent received their insurance from public sources such as Medicaid. Earned-income patchers and those who were self-employed only were somewhat less likely to have health insurance than those who were working in wage jobs or who were unemployed.<sup>184</sup> Low-income entrepreneurs in the SELP study were even more challenged to secure health insurance; only 50 percent of these business owners had health insurance in the fifth year of the study.<sup>185</sup> More recent data on the outcomes of low-income entrepreneurs assisted by microenterprise programs funded by the Ms. Foundation for Women found that two-thirds of respondents had health insurance, and that, for these individuals, the most common source of insurance was a wage job held by the entrepreneur or her spouse.<sup>186</sup> As we discuss further in the final section of this paper, this finding challenges microenterprise programs to find ways to help low-income entrepreneurs strengthen their businesses and policy makers to find ways to more broadly support families who are working, but still lack the capacity to meet basic family needs.

*There is also some evidence that self-employment skills provide low-income and disadvantaged individuals with greater resiliency in the labor market.* The impact evaluation of the Unemployment Insurance (UI) demonstration found that in Massachusetts and Washington State, participants who received selected self-employment assistance experienced a significant and positive effect on the length of employment. Participants in Massachusetts also experienced a significant and positive effect on the likelihood of employment both 19 and 31 months after receiving services.<sup>187</sup> Similarly, a three-state study of Self-Employment Assistance programs for recipients of

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<sup>180</sup>In the study, economic self-sufficiency is defined according to a self-sufficiency standard created by Wider Opportunities for Women. In San Francisco County, the standard for a family of four (two adults and two children) was \$49,156, or about three times the federal poverty standard. See: Women's Initiative, 17.

<sup>181</sup>Data on median household income is unpublished data from the SELP study. For data on average household income and poverty status, see: Clark and others, 16.

<sup>182</sup>Klein and others, 25.

<sup>183</sup>Klein and others, 35.

<sup>184</sup>Klein and others, 68-70.

<sup>185</sup>Clark and others, 24.

<sup>186</sup>Black, *Enhancing Economic Opportunity Through Entrepreneurship*, 6.

<sup>187</sup>Benus and others, 97-99 and 140-142. It is important to note that at the Washington site, participation in the demonstration did not increase the combined likelihood of employment (in either wage or self-employment), although it did, as noted above, increase the likelihood of being employed at the time of the second survey.

unemployment insurance found that program participants experienced higher rates of re-employment (in either wage or self-employment) than non-participants.<sup>188</sup> The WTW study found that the median length of unemployment for income patchers was half that of those who engaged solely in wage or self-employment.<sup>189</sup>

*Most research findings suggest that the income gains of disadvantaged or unemployed individuals who pursue self-employment are similar to those of individuals who engage in wage employment.* Many low-income individuals pursue self-employment because they believe that they have the potential to earn more than they could in a wage job. As discussed in this chapter, there are clearly some microbusinesses that are very successful and some entrepreneurs who do very well. Several studies have looked at the question of whether low-income individuals who pursue self-employment do “better” on average than those who pursue wage employment. The results of these studies vary. Sanders found that low-income self-employed and wage workers exhibited similar income gains.<sup>190</sup> In their study of unemployed individuals who pursued self-employment, Benus and others found that those who received self-employment services in Washington State experienced no earnings differential, but that participants in Massachusetts experienced combined positive earnings (self- and wage employment) impact of almost \$6,000.<sup>191</sup> On the other hand, the WTW study found that participants with income from wage employment had higher household income gains than those engaging in self-employment (with earned income patchers having the highest incomes, as noted above).<sup>192</sup>

*There are indications that self-employment programs may have some positive effect on wage employment.* Microenterprise practitioners have always believed that their programs play a role in increasing wage opportunities or earnings among clients. Some research findings suggest this could be the case. For example, the WTW study found that clients experienced strong growth in wage as well as self-employment income. Because these studies did not use an experimental design, these increases cannot be attributed to participation in the microenterprise program. The UI demonstration found dramatically different wage employment impacts across its two sites: in Washington State, study participants who participated in the self-employment option earned less in wage employment than their counterparts who did not, while in Massachusetts the opposite was true.

In summary, it appears clear that self-employment can be a tool to help some low-income and disadvantaged individuals to increase their household earnings and to move out of poverty and toward greater economic self-sufficiency. For some of these individuals, the microenterprise will play a key role in providing household income. For

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<sup>188</sup>Kosanovich and Fleck. The higher rates of re-employment were statistically significant. However, because this study used a comparison group rather than a control group, the findings are likely influenced by self-selection bias.

<sup>189</sup>In the study, 55 percent of the respondents experienced some unemployment (meaning that they were not working in any form of employment, either their businesses or a wage job) during the second year after enrolling in the microenterprise program (the remaining 45 percent were employed continuously during that year). Among those who were unemployed for some time, those who were only in wage or self-employment were unemployed for a median of six months, while those who worked in both wage and self-employment were unemployed for a median of three months. Klein and others, 16-17.

<sup>190</sup>Sanders, 121.

<sup>191</sup>Benus and others, viii-ix. It is important to note that this finding pertained to the earnings differential between those who participated in the treatment group and those participating in the control group of the study. While the treatment group members in both states were more likely to have been engaged in self-employment and were self-employed longer, the findings on earnings differentials were not disaggregated according to employment status.

<sup>192</sup>Klein and others, 24-5.

others, the microbusiness is an important complement to wage employment. By giving low-income and disadvantaged individuals more skills and income-generating options, it provides a means to better cope with the vagaries of the lower-end of our labor market.

## **Microenterprise and Self-Employment as an Asset-Building Strategy**

Microenterprise development is also viewed as an asset-building strategy. While a business is a means of generating income, it is also a vehicle for building assets and net worth – as resources are invested in business assets, such as cash, inventory and equipment, that can earn a return over time. A few studies have looked at patterns of asset accumulation among low-income entrepreneurs and found evidence that business ownership does have positive effects at both the business and personal levels.

*Low-income entrepreneurs accumulate business assets over time.* For example, the final participant study of the Self-Employment Investment Demonstration (SEID) found that welfare recipients with businesses had average business assets of \$10,501 and business net worth of \$4,867 per business.<sup>193</sup> Similarly, the welfare recipients in the WTW study had median business assets of \$4,800 and business net worth of \$4,000 two years after enrolling in microenterprise programs. Furthermore, these individuals saw the value of both their business assets and their net worth grow by about 250 percent during the two-year period.<sup>194</sup>

*Self-employed individuals show growth in personal assets over time, although the effect on household net worth is less clear.*<sup>195</sup> Both the WTW and SELP studies found that household assets of microentrepreneurs grew over time. Analysis of the SELP data found that median household assets grew by \$13,140 over five years, and that in the fifth year of the study, households had accumulated median net worth of \$2,055.<sup>196</sup> In the WTW study, the gains in household assets and net worth were stronger among those who were solely self-employed than among those who patched wage and self-employment income. Among those who earned income from self-employment only, median household assets grew by \$4,875, or 1,219 percent. Patchers, by contrast, saw their median household assets grow by \$1,155, or 226 percent. Perhaps more importantly, median household net worth dropped for both groups, with the decline being greatest among earned-income patchers.<sup>197</sup> Thus, while these individuals saw an increase in assets, their liabilities grew more quickly.<sup>198</sup> This finding also was true for study participants who were unemployed and those who earned income solely from wage employment. In fact, individuals who earned income solely from self-employment showed the smallest decline in net worth, the smallest percentage growth in credit card debt, and the largest growth in mortgage debt.<sup>199</sup> Importantly, the research suggests

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<sup>193</sup>Raheim and Alter, xiv.

<sup>194</sup>Klein and others, 51.

<sup>195</sup>It is important to note that most households in these studies had multiple streams of income; thus, increases in personal assets cannot be attributed directly or solely to the microenterprise.

<sup>196</sup>Data on median household assets and net worth are from an unpublished analysis of the SELP survey data conducted by FIELD staff.

<sup>197</sup>Both groups had \$0 net worth at the time they enrolled in the microenterprise program; two years later, the net worth of those with self-employment only was -\$449; for patchers, it was -\$1,550. Klein and others, 42-43.

<sup>198</sup>Study respondents experienced increases in credit card debt, educational loans, mortgages and car loans. The greatest increases were in credit card and educational loan debt. Klein and others, 40.

<sup>199</sup>Klein and others, 41.

growth in assets does not always signal a stronger household financial condition, and that microenterprise programs – and others who work with low-income individuals – may need to help clients understand how their choices affect personal debt.

*There are suggestions in some studies that self-employed individuals showed the greatest growth in homeownership (relative to those without businesses).* In her research on low-income workers, Sanders found that wage workers were less likely than self-employment program participants to acquire a home over a four-year period.<sup>200</sup> The WTW study similarly found that respondents who earned income solely from a business showed the greatest increase in homeownership (greater than those with wage earnings, income patchers, and those who did not earn income). Among those with business earnings, 14 percent of respondents owned homes at the time they entered the microenterprise program; this increased to 22 percent two years later.<sup>201</sup> Data from the SELP study (which looked only at low-income entrepreneurs and did not provide a comparison to non-business owners) also found that the primary source of asset growth among low-income entrepreneurs was an increase in the value of their housing assets. Because of limitations on the data from these studies, it will be important to conduct additional research on this question. However, the findings do suggest two potential research hypotheses. One is that self-employed individuals are more likely to invest in housing assets than low-income wage workers. The second is that low-income business owners – who primarily operate businesses out of their homes – are able to treat investments in their housing as a business expense, thereby facilitating their ability to improve their housing assets.

Clearly low-income microentrepreneurs experience economic benefits in the form of business assets and net worth – benefits that typically do not accrue to those who engage in wage employment. Initial research findings also suggest that microenterprise may also have positive effects on personal assets, although the effects on personal net worth are less clear. Research on the asset effects of microenterprise development is in its early stages. Given the growing interest in assets as a tool for combating poverty, it will be important to learn more about these effects and to consider the role of self-employment in building assets, as well as in creating income, in judging the economic value of microenterprise to struggling workers and families.

## **Non-Economic Effects of Microenterprise Development**

As is the case with more advantaged entrepreneurs, low-income individuals pursue self-employment for non-economic as well as economic reasons. While finding a means to generate a source of income may be the primary consideration, these other non-economic benefits may be the factors that cause some individuals to choose self-employment over wage employment.<sup>202</sup> Research shows that these non-economic factors include the following:

*Supporting family roles.* The fact that self-employment can be a means for better balancing work and family roles is a key benefit to many families with children or other family members requiring care.<sup>203</sup> As is noted by Messenger and Stettner in their work

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<sup>200</sup>Sanders, 130.

<sup>201</sup>Klein and others, 100.

<sup>202</sup>For a more comprehensive discussion of the non-financial reasons that low-income individuals choose self-employment, see Sherraden and others, Chapter 7.

<sup>203</sup>Servon, *Bootstrap Capital*, 86. See also Sherraden and others, 60-1.

on the quality of self-employment jobs, this benefit can accrue to self-employed individuals at all income levels, not just those who are low-income.<sup>204</sup> Importantly, this flexibility can have economic as well as non-economic benefits to the family in the form of reduced child care, health care or transportation costs. In their interviews with entrepreneurs in the SELP study, Sherraden and others also found that respondents often cited family benefits in the form of role modeling and opportunities for their children, who learned business and goal-setting skills by observing their parents' businesses.<sup>205</sup> The SEID study also found that more than one-third of the welfare recipients who pursued self-employment had employed their children in their business.<sup>206</sup> It is also important to note, however, that the time and energy that a business demands can have negative effects on a family. Ten percent of the business owners interviewed in Sherraden and others noted that business ownership created a strain on their families.<sup>207</sup>

*Greater autonomy and control over the work environment.* Many microentrepreneurs also value the control over both their livelihoods and their day-to-day work environment afforded by self-employment. Some individuals pursue self-employment because of previous negative experiences with a boss or workplace setting. Sometimes these are related to discrimination; other times to personality conflicts or simply the poor quality of low-wage work. For these individuals, owning a business can be a means of creating a more attractive work environment.<sup>208</sup> Interestingly, despite the risks of business ownership, some entrepreneurs pursue it because they believe it gives them greater control over their economic destiny. After being laid-off from a job – at the mercy of the decisions of others – such individuals feel more secure knowing that their livelihoods are in their own hands.<sup>209</sup>

*Personal development and increased self-esteem.* Many microenterprise practitioners will attest to the dramatic growth in self-esteem and personal efficacy that low-income entrepreneurs express when they achieve their business goals. Several qualitative research efforts have documented these effects. For example, Sherraden and others found that almost two-thirds of the low-income entrepreneurs they interviewed believed that the business contributed to their personal growth and learning.<sup>210</sup> Raheim and Alter also document increases in the self-efficacy and self-esteem experienced by low-income entrepreneurs.<sup>211</sup> While success in any form likely helps to contribute to increases in self-esteem, a low sense of self-efficacy is one of the key challenges that low-income individuals face in seeking to connect to the economy. Therefore, many microenterprise programs have components aimed at increasing personal effectiveness. And, the tasks involved in planning for and running a business involve significant initiative on the part

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<sup>204</sup>Messenger and Stettner cite research that shows that women with children are significantly more likely to choose self-employment than those who are not, and that their motivation is to find a way to balance their work and parenting responsibilities. Messenger and Stettner, 57.

<sup>205</sup>Sherraden and others, 167.

<sup>206</sup>Raheim and Alter, 35.

<sup>207</sup>Sherraden and others, 168.

<sup>208</sup>See Sherraden and others, 163-168; also, Servon, *Bootstrap Capital*, 49.

<sup>209</sup>Sherraden and others, 165-167.

<sup>210</sup>Sherraden and others, 159.

<sup>211</sup>Raheim and Alter, 65.

of the would-be entrepreneur. Thus, participation in a microenterprise program may also contribute to greater self-esteem. For example, Servon describes that nearly half of participants in one microenterprise program, including those who did not start businesses, reported increases in self-esteem.<sup>212</sup>

While they can be difficult to measure, these non-economic benefits are clearly important to entrepreneurs – enough that they may choose self-employment over a more secure or higher-paying wage job.

## **What Does the Research Tell Us?**

When the microenterprise field emerged in the United States, observers posed a basic set of questions: Can low-income people start businesses? Will these businesses survive? Will they be too small to make a difference? Will they help to raise household incomes? The body of research reviewed in this chapter captures a set of answers to these questions, at least in terms of the experiences of these microenterprise program clients. Low-income individuals can create small firms that survive and grow over time. Microenterprise can help some low-income individuals generate economic returns, in the form of both increased income and business assets, in a difficult marketplace. While the firms are small, they are not markedly different in terms of revenues and owners' draw from the large numbers of small firms owned by individuals who are not poor. And, while the returns these businesses generate are typically not large enough to bring a family into the middle class, they can be an important part of a household economic strategy that sustains many struggling families. Also, importantly for many individuals who engage in self-employment, there are non-economic benefits in the form of flexibility, and/or greater control and autonomy over their working lives. For these individuals, the benefits of business ownership provide a more rewarding work environment than a low-wage job.

While there is a great deal of richness to the studies conducted to date, important research questions remain. Some of these deal with ongoing questions about the long-term value and outcomes for those who engage in self-employment. Most importantly, it will be important to understand how the businesses fare over time: will they continue to survive; will they grow; and will their owners be better off financially? It will also be important to understand in more detail which low-income individuals do best in self-employment and which would do better to pursue wage employment or income patching. There is also a need for further study of the economic development impact of microenterprises: the extent to which they grow and generate jobs and their contribution to local economies.

One area where more research is needed is the role that microenterprise programs have played in producing the outcomes documented above. As is noted above, only one study of a microenterprise initiative has used an experimental design that can yield insights into program impacts. Therefore, further rigorous research on program impacts is needed.

However, it is important to note that some of the research that has been conducted suggests that programs do have at least some effect on the outcomes experienced by

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<sup>212</sup>Lisa J. Servon, "Microenterprise and Women: Entrepreneurship as Individual Empowerment," *Journal of Developmental Entrepreneurship* 1 (1996): 34-35.

their clients. First, as is noted in Chapter 3 of this report, the graduation rates of most microenterprise training programs are quite high, suggesting that programs do provide some value to their clients (who would otherwise drop out). Second, some of the above research asked clients directly whether the assistance they received from the microenterprise program was helpful. As Table 17 below indicates, in the WTW study, high percentages of business owners reported that specific skills learned in the microenterprise program helped them run their businesses.<sup>213</sup> Sherraden and others also found that more than 62 percent of the entrepreneurs they surveyed made a positive assessment of the assistance and support they received from the microenterprise program.<sup>214</sup> Third, as is also cited in Chapter 3, research by two microenterprise programs – Women’s Initiative for Self Employment and the Institute for Social and Economic Development – found a correlation between completion of business training and business outcomes or growth.<sup>215</sup> Additionally, the evaluation of the Self-Employment Allowance Program in three states found that participation in the program had had a large and statistically significant effect on their engagement in both self-employment and in their attachment to the labor market.<sup>216</sup>

**Table 17: Skills Learned at the Microenterprise Program That Helped Respondents Run Their Businesses**

<b>Skill Learned at the Program</b>	<b>Number and Percentage Reporting n=170</b>	<b>Skill Learned at the Program</b>	<b>Number and Percentage Reporting n=170</b>
Understanding costs	139 (82%)	Developing marketing strategies	129 (76%)
Identifying markets	137 (81%)	Pricing product	127 (75%)
Keeping business records	136 (80%)	Calculating cash flow	125 (74%)
Writing a business plan	132 (78%)	Personal budget and finance	124 (73%)
Instruction on making sales	133 (78%)	Making presentations	112 (66%)
Time management	132 (78%)	Financing the business	102 (60%)

There will continue to be an important role for research as the microenterprise field moves forward in search of more effective practice and policy. Research can play a role in many ways: in informing and illuminating practice, in further identifying the various

<sup>213</sup>Klein and others, 54.

<sup>214</sup>Sherraden and others, 83.

<sup>215</sup>Women’s Initiative for Self-Employment graduates from the core training were 40 percent more likely to experience business growth than those who did not complete the workshop. The Institute for Social and Economic Development (ISED) found that having a business outcome (a start, stabilization or expansion) after training completion correlated with a set of actions including: completing a business plan, making progress on securing needed financing, completing class assignments, and a high attendance rate. For more detail on their findings, see also their full research reports at <http://fieldus.org/li/pdf/ISED.pdf> and <http://fieldus.org/li/pdf/WI.pdf>; Internet. Note that these correlations do not necessarily imply causality.

<sup>216</sup>It is important to note that this study used a comparison group rather than a control group, so these findings are likely affected by self-selection. Kosanovich and Fleck, 81-83.

benefits and beneficiaries of microenterprise, and in quantifying the costs and benefits of investment in microenterprise programs. Moreover, this research can be of many kinds, depending on the nature of the questions at hand: from practitioner-directed efforts to capture data on their performance and outcomes, to qualitative research into the non-financial benefits of microenterprise, to rigorous impact studies.

## Conclusion

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**A**s we look toward the future of microenterprise in this country, it is important to understand where this strategy connects to some of the key challenges facing our nation. The challenges of poverty and economic dislocation are complex and defy simple and sweeping solutions. As our nation looks to provide opportunities for individuals and communities that are struggling economically, microenterprise offers value in three important ways:

- ▶ **Microenterprise offers opportunity to the segment of low-income individuals for whom self-employment is a necessary, and in some cases, the best source of employment and income.** Our current economic environment is a very difficult one for those at the lower end of the labor market and those who face job loss due to technological changes and/or outsourcing. As Chapter 1 documented, in that environment there are a number of demographic and economic trends – including fewer solid middle-class jobs, the aging of the population, an increase in work among mothers, continuing immigration, and changes in welfare and public assistance programs – which continue to both push and pull individuals toward self-employment. Microenterprise programs work with the most disadvantaged of these individuals to help them take advantage of what may be their best – or indeed, their only – economic option.

As the data in this chapter reveal, low-income individuals can use and benefit from microenterprise in different ways. Some use self-employment to create jobs for themselves and increase their family incomes. Some appear to use it to increase their resiliency in the workplace – in other words, to lower the amount of time spent out of work, and/or to tide themselves over between wage jobs. Others use it to balance demands between work and family or to create a work setting that is better than that of a low-wage job. In terms of the benefits of self-employment, owners of a set of “high performing” microenterprises are able to do quite well. Others use their self-employment income – often in tandem with other income sources – to move out of poverty, although they still struggle to afford key needs, such as health insurance. In other cases, the businesses are quite small, providing a small piece of the family’s total income. Whatever the specific role of the business, however, what is common about these individuals is that they use the microenterprise as a tool to cope with the difficult economic challenges they face.

► **Microenterprise opens wealth and ownership opportunities to individuals who have been excluded from our economy.** Researchers and grassroots organizations are increasingly focusing on the role that asset ownership and wealth play in combating poverty. However, recent economic trends have increased the disparities in wealth in our nation. As Chapter 3 of this paper documents, microenterprise programs clearly have succeeded in reaching out to individuals who have faced exclusion and discrimination in our economy: ethnic and racial minorities, women, individuals with disabilities, and low-income individuals. They are unique in that they offer individuals the opportunity not only to generate income, but also to build assets and to serve as owners, not just workers. The data in this paper begin to demonstrate that microenterprise is, in fact, a successful strategy for building ownership among these disadvantaged groups. Program clients are able to start and grow businesses that survive over time and grow in terms of revenues and assets. There is also evidence that these low-income entrepreneurs save and that they become more engaged in community and leadership roles after engagement in a microenterprise program.

► **Microenterprises can play a role in the revitalization of local economies.** In the face of lagging economic growth and the overseas migration of firms and jobs, many communities are focusing today on building a local culture and business environment that is supportive of entrepreneurship. Entrepreneurship is seen as key to local economies, because it creates jobs, retains locally-generated profits, and broadens the distribution of wealth. As the data in this chapter indicates, while the majority of microenterprises are quite small, some do grow to become much more substantial in terms of revenues and employment. And, in some areas, such as the rural communities described in Chapter 1, microenterprise and self-employment may be a critical source of new job growth.

Microenterprise programs have demonstrated their effectiveness in reaching entrepreneurs who are not served by other enterprise support programs and whose potential might otherwise not be realized. This is important in creating or rebuilding an entrepreneurial culture among disadvantaged individuals or communities. As noted above, targeting the most disadvantaged communities and individuals broadens ownership and opportunity. From the perspective of local politicians and policy makers, broadening the base is important, as when the benefits of public economic development investments are widely shared, they are more likely to receive broad public and political support.

Given our country's need to find effective strategies that can better connect struggling families and communities to the economy and what has been learned to date about the outcomes for entrepreneurs, it is our assessment that it makes sense to provide continued support – both public and private – for microenterprise. Part of this support should be in the form of funding for microenterprise programs. While it is true that the research conducted to date does not definitively show that such investments yield net positive benefits, it does show that many of the program clients experienced positive outcomes, and that they ascribe some of their success to program services. As we at FIELD have conducted and observed this research, we are convinced that microenterprise programs can and do make a positive difference for their clients.

Furthermore, as the field continues to learn more about what makes for effective programs, this learning raises the prospect for increasing the benefits that programs can offer to their clients and to society as a whole. Thus, while additional, more rigorous research is needed, and while programs must work to improve their reach, impact and cost-effectiveness, we believe that continued funding support is clearly warranted and is, in fact, vital given the persistent challenges faced by low-income individuals and struggling communities.

We also believe that the microenterprise field, as well as funders and policy makers, should look more broadly at ways to support microenterprise development. Low-income emerging entrepreneurs clearly want access to business expertise and capital. They also face challenges with affording health insurance, negotiating business regulatory requirements, and obtaining financial services. There may well be ways – either through microenterprise programs or via policies aimed directly at microentrepreneurs – to cost-effectively assist large numbers of microentrepreneurs to meet these challenges as well.

In sum, we believe that support for microenterprise development, and microenterprise programs, continues to hold promise in the United States. At the same time, the context in which microenterprise programs operate, as well as the field's knowledge of what works and what its clients need, have changed dramatically during the past 20 years. These changes and developments require that programs operate in new ways. Chapter 5, which follows, provides a set of recommended directions and areas for exploration that can help the field, and our country, make the most of that promise for the future.



Significant changes affecting the context in which microenterprise programs operate have set the stage for transformation and restructuring within the microenterprise field. In this chapter we both describe the context for change and detail eight important directions the field should embrace in order to better position itself for long-term growth and stability.

# Charting the Future of the Microenterprise Industry in the United States

**T**he 20 years of the microenterprise industry's experience seem relatively brief when compared to those of other, more established development fields, such as affordable housing and workforce development. At the same time, however, these 20 years have brought vast changes in financial markets and the overall economic context that shapes how programs operate in the funding environment and in the field's own understanding of the market it seeks to serve and the strategies and approaches that may be most effective in doing so. These changes present critical challenges to the current structure and operations of the microenterprise field, challenges that demand a response if the field is to remain and grow as a source of support for low-income entrepreneurs. This chapter, therefore, presents the key challenges that are driving change within the industry and a set of recommended directions that over time, we believe, will lead to a stronger and more vital microenterprise field.

## Key Challenges

To understand why and how the microenterprise field must change, it is necessary to understand the critical challenges that face it today. As is discussed below, the four key challenges facing the industry are: dramatic shifts in the market for microenterprise products and services, an extremely challenging funding environment, the current scale of service delivery, and the unevenness of program quality and performance.

### THE CHANGING MARKET

The market for services, and the field's understanding of that market, have shifted dramatically during the past 20 years. Changes in the "supply side" of the market for credit products and services have been particularly marked, as the financial industry in this country has restructured and new players and products have emerged. Two key forces are the use of credit scoring, which has broadened access to bank loans and credit cards, and the emergence of new "alternative" lenders. Thus, although it was presumed initially that microentrepreneurs had few alternatives for business financing, today there is anecdotal evidence that they are accessing a variety of sources for their businesses. While practitioners applaud the movement of banks toward this market, there is concern that the more likely alternative sources of financing – credit cards, payday loans, moneylenders – are less positive for microentrepreneurs, because of either their high costs or the potential for clients to take on more debt than is advisable. These shifts in the market demand a response. Given the dynamic nature of the financial industry, future shifts in the market are also inevitable. One pending change is proposed revision

to the Community Reinvestment Act, which may reduce the level of investment by traditional banks in microenterprise loans and/or programs.

New players are also beginning to emerge on the training and technical assistance side of the market as well – although these are much less significant at this time. Some private companies that provide services to the small-business market – including eBay, Verizon, and American Express – are beginning to provide on-line business assistance and education to their customers, presumably as a means to build and develop this market segment. While their services apparently are targeted to larger, more established businesses and may lack the individualized, in-person features of most microenterprise services, they may prove valuable to some microentrepreneurs. As such, they bear watching as the field seeks to enhance and refine its product and service mix.

While the supply side of the market is changing, so is the field's understanding of the demand side of its market. Many of the early assumptions regarding the field need to be revised based upon experience and the changed context in which the industry operates. Initially, it was assumed that the market demanded a core set of services: training on business plan development, some technical assistance, and access to small-term loans. We now know there are many sub-markets of microentrepreneurs: individuals who start very small businesses as a supplement to a wage or other income sources (income-patchers), growth-oriented entrepreneurs, very poor individuals who face challenges to self-sufficiency that require a broader range of services, refugees, individuals with disabilities, and so forth. Each type of client may demand different products and services. In addition, the market is learning that some microentrepreneurs have unexpected characteristics, such as poor credit histories<sup>217</sup> and/or a strong aversion to debt, which pose challenges in developing the appropriate products and services.

It was also presumed that microentrepreneurs would eagerly grasp services under any terms that programs offered. However, some practitioners have reported “buyer resistance” to loans.<sup>218</sup> Research has identified a range of potential costs – interest rates that are perceived to be high, fees, required training and technical assistance, travel, and other transaction costs – that borrowers may incur in program participation that might lead applicants to think twice.<sup>219</sup> Similarly, on the training and technical assistance side, programs have struggled with the challenge of how to meet the needs of clients who say that they want additional services to help grow their business, but have difficulty finding the time to participate in program offerings. In fact, the “if we build it, they will come” approach has proved insufficient in attracting high numbers of clients.

Like all markets, the market for microenterprise services will continue to change and evolve over time. The challenge to the microenterprise field, then, is to change and grow in ways that remain relevant to the market.

## A DIFFICULT FUNDING ENVIRONMENT

The funding environment that microenterprise programs face today is extremely difficult. The challenging context is partly due to a set of macro-level trends that affect

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<sup>217</sup>While poor credit histories may be due to poor past management of credit, others may be due to the absence of past credit (a “thin” file) or a financial crisis (such as an illness that resulted in high medical bills). Currently, many microlenders use their underwriting process on evaluating the reasons for a poor credit history, and whether the low credit score should preclude a loan to the applicant.

<sup>218</sup>Edgcomb and others. *Scaling up Microenterprise Services*, 11.

<sup>219</sup>Caroline E. Glackin, “What Does it Take to Borrow?,” *Journal of Microfinance* 4, no. 1 (Spring 2002): 115-135.

all U.S. nonprofits. On the national level, tax cuts have led to reduced federal revenues. The accompanying desire to cut domestic spending has and will continue to affect discretionary spending at the federal level for at least the next several years. The recession and initially slow recovery have affected state budget levels; some states are now faring better, but others continue to face significant challenges. Moreover, the lagging stock market has affected some private foundation giving as well.

The scarcity of funds is exacerbated by concerns among funders regarding the scale, impact and performance of this field. Donors are asking a set of critical questions about the field: Is it big enough to make a difference in our efforts against poverty? Does it have real impacts? Are programs well run? These concerns are not surprising; when funding resources are scarce, there is greater scrutiny of the value and performance of different strategies. As we noted in the conclusion to Chapter 4, we believe microenterprise development has impact and value, particularly in the difficult economic context facing low-income individuals and many rural and distressed communities. Nevertheless, programs must recognize that in the current funding climate, they will continually be pressed to demonstrate that they run high-quality, high-value programs. This will require that programs track information on their performance, understand how that performance relates to the industry nationwide, and educate their donors about how to identify and support high performance.

Within this overall funding context, there are differing impacts at the program level. Funding streams and, therefore, microenterprise programs targeted to low-income individuals have been particularly affected. On the other hand, states and local communities seeking to deal with economic recession and the offshore movement of jobs are refocusing on entrepreneurship. Within the broad range of entrepreneurship and business creation strategies, microenterprise is of interest when focused in communities or neighborhoods where self-employment or small-scale enterprise makes sense (i.e., rural and inner-city neighborhoods) or where residents are those who are typically not served by other entrepreneurship strategies (immigrants and refugees, low-income, etc.). However, while areas of opportunity do exist, the overall result is that raising funds, never easy, is more difficult and time-consuming than in past years.

## **THE SCALE OF SERVICE DELIVERY**

In Chapter 1, we estimated that there are approximately 10 million entrepreneurs within the overall target markets defined by the microenterprise field. As noted in that chapter, this is an estimate of the overall market. Given that some entrepreneurs may not want or need services and that there are other providers in the marketplace, it is unreasonable to assume that programs should be serving this entire market. However, even if one were to estimate that the field should achieve market penetration of 10 to 20 percent – or one to two million entrepreneurs – the field is currently only reaching between 7.5 and 17 percent of even that number.<sup>220</sup>

The mismatch between the estimated size of the potential market and the current scale of the industry is due to a variety of factors. Two of these factors relate directly to challenges noted above. The scarcity of resources to subsidize the expansion of services has played a role, as programs seeking to expand in scale have lacked the resources necessary to do so. Changing market conditions and the lack of detailed knowledge of

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<sup>220</sup>As is noted in Chapter 2, FIELD estimates that in 2000, the field served an estimated 150,000 to 170,000 individuals.

client demands have also limited the attractiveness of microenterprise products and services to some clients. In addition, as noted in Chapter 2, there is disparity in the geographic spread of programs across the United States. This has left many markets with limited availability of microenterprise services. Finally, some organizations come to microenterprise with a mission that focuses on a specific target market, such as refugees, or geographic region; for these organizations, growth or “scaling up” are not key issues of concern.

As a result, the microenterprise field currently comprises hundreds of modest-sized programs – with an average of four to five staff persons each – punctuated by an occasional large-scale and high-volume organization. This is not surprising given the field’s grassroots origins. The microenterprise industry is not alone in this profile; for example, the community development finance industry shares this same characteristic.<sup>221</sup> Many other industries have also been created and developed by a few industry leaders.<sup>222</sup>

In addition to the few large-scale programs that exist, the current structure also contains some small- and medium-size program models that have achieved important outcomes and levels of performance. For example, there are microlending programs integrated within CDFIs (credit unions and larger loan funds), that have succeeded in making between 100 and 200 microloans per year at high levels of efficiency and self-sufficiency. Because these organizations offer financing products and services beyond microloans, they are able to spread costs across various products and realize certain efficiencies. In addition, their clients can benefit by gaining access to a range of financial services. On the other hand, many of these integrated lenders operate in fairly limited geographic markets, and they face other constraints (including concerns on the part of regulators regarding the risk of microlending) that limit their interest in and ability to grow.

Similarly, on the training and technical assistance side, some relatively small-scale microenterprise programs show strong outcomes on measures of client success, such as the percent of clients that are in business and changes in client household income. Their success lies in part on the strength of relationships built between program staff and clients – relationships that go beyond business advice to help in securing child care, troubleshooting various personal challenges, and overall moral support. While rigorous evaluations are required to establish whether these organizations truly have a positive cost-benefit impact, they do, at least, suggest that microenterprise programs might achieve positive impact without reaching large numbers of individuals.

However, despite the effectiveness of some models, the present composition of the field has led to real constraints in achieving scale, in realizing efficiencies, and in developing the capacities needed to offer more sophisticated services. Although the issue of organizational size may have different ramifications for credit-led and training-led institutions, the fact of the matter is that the small size and independent operation of most programs have left them challenged to incorporate technologies to increase efficiencies and to purchase skills and expertise needed to develop services that respond to market demand. The small scale of most lenders presents an especially acute

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<sup>221</sup>Within the CDFI industry, a small number of institutions “hold a substantial portion of the field’s total assets. The largest five CDFIs control 39 percent of the sample’s assets, and the largest 10 control 50 percent.” CDFI Data Project, *Community Development Financial Institutions: Providing Capital, Building Communities, Creating Impact*. Fiscal Year 2002 (Philadelphia: CDFI Data Project/National Community Capital Association, 2004).

<sup>222</sup>Kirsten S. Moy, “New Pathways to Scale in Community Development Finance,” *Profitwise News and Views* Chicago Federal Reserve (December 2004): 2-23.

challenge, as they expend more on operations than the value of the loan portfolios. This is untenable for the long term. Even the largest, most efficient lenders, which have achieved higher levels of self-sufficiency than the industry as a whole and demonstrated significant economies of scale, report being constrained by fund-raising challenges in their efforts to scale-up.

Finally, the limited reach of microenterprise service delivery is a challenge, because some donors – both public and private – may look at scale as a proxy for the impact data that programs lack. Thus, in times when both private and public funders face tight budgets, the sustainability of smaller-scale programs is challenged, regardless of their other merits.

If the microenterprise field is to survive and grow over time, it must address the challenge of expanding the scale of its reach. This is important both in terms of demonstrating its relevance to the market and in making its case to the donors.

### **UNEVEN PROGRAM QUALITY**

As discussed in Chapter 2, the performance data that is available on the microenterprise field demonstrate that some microenterprise programs have achieved high levels of performance on key measures: reaching high percentages of minority and women clients; serving several hundred or even thousands of clients annually; achieving loan loss rates between 1 and 5 percent and rates of training completion above 75 percent; and demonstrating increasing levels of cost recovery, particularly among credit-led programs. These leading programs illustrate that microenterprise programs can achieve solid levels of performance. At the same time, FIELD's experience in collecting performance and outcomes data also reveals that there are many other programs that suffer from limited resources, inadequate staffing for the types of program services they want to offer, and diseconomies of scale that limit their performance.

The reasons for the uneven quality of program performance are many. It is important to note at the start that what these programs seek to do is difficult; owning a business is a challenge for most individuals and low-income individuals face additional obstacles, both in accessing markets and resources and in overcoming personal and family factors that often contribute to their poverty. Furthermore, microenterprise lending emerged because private banks rarely made microenterprise loans due to the high costs and risks involved. In addition, the market continues to change over time, pressing programs to innovate and change.

Yet, while the challenge that programs take on is a difficult one, much has been learned over time about effective performance and best practice. Nevertheless, spreading those lessons and raising the level of performance broadly are not easy tasks. While more research publications and training opportunities on best practices are available, the decentralized nature of the field means that some programs continue to function largely in isolation from their peers. Programs find it difficult to find the resources necessary to hire and retain skilled and experienced staff, so turnover and staff development are a common challenge. Many programs lack the internal management and data collection systems required to capture and analyze their performance over time.

As the field moves into a very tight funding situation, the low performance of some programs undermines the ability of the field to argue its value. Even in times when funding is less constrained, support for these programs means that subsidy dollars – both public and private – are invested inefficiently. Thus, the field must expand its efforts to measure and improve performance.

## Future Directions

Together the four challenges detailed above set the stage for transformation, shakeout and restructuring within the microenterprise field. Periods of transformation and restructuring happen in all industries – as original entities emerge and grow, areas of overlap or inefficiency clearly appear, and there is a period of restructuring, mergers and so forth. Periods of restructuring also result as fields encounter downturns in funding, which are inherent in our political and economic system. It is important to acknowledge that these times of restructuring are difficult. However, they can also offer an incentive to change. Within the microenterprise field, we believe that there is a base of experience, knowledge and capacity that can be built upon to expand the level of service delivery and the depth of impact that programs have. *With the appropriate focus of resources, use of learning to date, and rededication of effort, this time of challenge can set the stage for the next level of development and impact for the field.*

The remainder of this chapter, therefore, sets forth eight directions that the microenterprise field must look toward as it seeks to move through this period of restructuring and transformation. While ideally this final section would set out a detailed vision for the future and a road map for how to get there, at this point the path forward is not fully clear. Our goal is to be as clear and specific as possible in suggesting how the field can use this time of challenge to strengthen itself and to grow. Toward that end, the discussion of each direction provides examples of initiatives that represent important steps forward and show how some in the industry are already advancing. It is now time for more practitioners, and the support organizations, donors, and other stakeholders that assist them, to embrace them as well. Finally, the discussion also includes a box that describes the roles that each of three key players in the field – practitioners, support organizations and donors – can play in support of these new directions.

### New Roles for Future Directions

Moving forward in pursuit of greater scale, impact and sustainability will require that each of the three key actors in the microenterprise field take on new roles. The text boxes in the following sections will relate the key roles that must be taken by:

**Microenterprise Practitioners** – organizations that provide direct services and products to microentrepreneurs.

**Microenterprise Support Organizations** – state and national trade associations, research and policy organizations, and technical assistance providers that provide information and other key resources to practitioners.

**Donors** – public and private funders who provide financial resources in the form of grants and investments to microenterprise practitioners.

### DIRECTION 1: IMPROVE UNDERSTANDING OF THE MARKET

If the microenterprise field is to increase its scale and define its role for the future, it must begin with a stronger and more detailed understanding of the market – in terms of both supply and demand. On the demand side, this involves research into the level of

actual demand for microenterprise products and services and the characteristics and preferences of potential customers. On the supply side, it involves mapping out the competitive marketplace to identify the products it is offering and the segments of the market it is serving.

While there has been recent research helping identify the number of microenterprises that exist in the United States, there has been much less attention to market research. In order to gauge the size and nature of demand, the field needs to know how many microentrepreneurs want financing and business development services and are unable to access them. Then, within this potential market for microenterprise services, the field must understand in greater detail the characteristics of potential customers (such as their credit histories and stages of business development), their product and service preferences, the marketing messages that resonate with them, and the communications or distribution channels best positioned to reach them.

Some microenterprise programs have begun to focus on market research as a key to increasing scale and improving their products. For example, between 2000 and 2002, a set of FIELD grantees undertook a range of market research.<sup>223</sup> Their efforts included:

- ▶ The development of in-house systems to capture key marketing and contact information toward the goal of identifying the most effective marketing channels and techniques.
- ▶ The use of geographic information systems to identify the potential scope of demand in various neighborhoods.
- ▶ Client focus groups and customer surveys geared toward providing feedback on specific program products and services.

These efforts demonstrated the value of these investments to program expansion, as they allowed programs to refine their marketing efforts, as well as to improve their products and make them more attractive to clients.

However, undertaking research on market demand is not an easy task. Given their size and the fact that they are often home-based, microenterprises are not captured in many databases and are often difficult to locate, increasing the cost and complexity of survey research. Most microenterprise programs have limited resources and limited expertise to conduct this type of research on their own. And, funders have traditionally neither understood nor supported the need for market research, making it a challenge to find the resources to support these inquiries.

Research into the issue of market supply is in an even more nascent stage. Microenterprise programs that have been conducting market research are beginning to hear that potential clients are accessing credit from other sources: credit cards, payday lenders, etc. There are also some data suggesting that banks may be making more small loans (i.e., less than \$35,000) through the Small Business Administration's 7(a) and Community Express programs.<sup>224</sup> On the training side, there are indications, as noted above, that private companies are beginning to provide business management

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<sup>223</sup>Elaine Edgcomb, *FIELD Forum Issue 13: Marketing Strategies for Scale-Up: FIELD Grantees Share their Experiences* (Washington DC: The Aspen Institute/Field, March 2002); Edgcomb and others, *Scaling up Microenterprise Services*.

<sup>224</sup>The 7(a) loan program provides guarantees to banks for loans made to small businesses. Community Express is a component of the 7(a) program that seeks to increase loans in underserved areas. In 2004, more than 22,000, or 27.5 percent of all 7(a) loans were in amounts less than \$25,000, while more than 3,500, or 86.5 percent, of Community Express loans were in amounts less than \$25,000. Small Business Administration data, provided to FIELD by AEO, February 15, 2005.

information to their customers, but it is unclear to what extent they are targeting, or accessible to, the microenterprise market.

Because many of these changes have occurred only within the past few years, little if any work has been done to try to map the key players moving to serve the microenterprise market and to determine which are, indeed, competitors, and which are potential collaborators in the quest to ensure that more microentrepreneurs get the services that can best contribute to their business goals. Yet, this type of research will be critical if the microenterprise field is to carve out its role in the marketplace. Although it is most likely that there will continue to be some entrepreneurs that private providers will not reach, at least for the foreseeable future, it may be that the field is best able to reach some entrepreneurs through partnerships or collaborations with the private sector. Examples of some ongoing initiatives to partner with private-sector lending organizations include:

- ▶ Partnerships between several microenterprise organizations and Circle Lending, an Internet-based firm that facilitates loans between family members and friends.
- ▶ A partnership between ACCION New Mexico and several area banks, in which the banks market, originate and close loans made by ACCION New Mexico. In this relationship, the partnership reduces ACCION New Mexico's transaction costs and allows the banks to provide customers (or potential customers) with access to loans they cannot themselves make.
- ▶ An automated sourcing agreement between the CDC of Long Island and several area banks, in which the banks automatically refer all applicants who are turned down to the CDC.

In order to identify the niches of the microenterprise market that it can serve directly or to identify potential partners and the potential benefits to collaboration, microenterprise programs must understand the supply side of the market. Building this understanding will require market research – review of marketing materials, industry sources (trade press and trade associations), and interviews with staff from these companies or those who follow them – to obtain information regarding their services, market focus and market penetration.

## Roles in Understanding the Market

### Microenterprise Practitioners:

- ▶ Conduct market research as a means of defining and designing new products.
- ▶ Look to develop internal systems, such as contact management systems, that can provide market information on clients.
- ▶ Explore joint ventures or collaborations with private lenders active in the local market (banks and alternative lenders) in areas such as customer referrals (automated sourcing), information exchange on client characteristics, and joint services.

### Microenterprise Support Organizations:

- ▶ Develop new and better tools for practitioners to use in conducting market research.

- ▶ Conduct and disseminate general market research that can support and inform individual program efforts. This could include survey and focus group research on key market issues, such as the demand among specific sub-groups (informal entrepreneurs and growth-oriented clients), and the type of language or messages that are most effective in reaching microentrepreneurs.

**Donors:**

- ▶ Assist practitioners to gain a deeper understanding of the changing marketplace by supporting opportunities to learn about market trends and general research as noted above.
- ▶ Fund market research to understand demand in specific marketplaces – including both quantitative (what is the size of demand) and qualitative (what are the characteristics and preferences of potential customers) research.
- ▶ Fund supply-side research and initiatives to map the competitive marketplace and identify areas of greater collaboration with banks and other lenders.
- ▶ Consider requiring practitioners that request funding to support new or expanded products and services to conduct market research to inform product design and delivery.

## **DIRECTION 2: DIFFERENTIATE AND BROADEN PRODUCTS AND SERVICES**

As the field gains a better understanding of its market, this will lead to a broader and more differentiated set of products and services. As we noted previously, there are a number of sub-markets within the microenterprise market that require different products and services. Developing and offering new products to meet these needs will lead to increased scale as new clients are attracted and existing clients continue to look to programs for needed services. It can also lead to greater efficiencies as staff resources are invested in offering tailored products that customers demand, rather than in one-size-fits-all offerings.

As an example, the field has two clear sub-markets in income patchers (part-time business owners) and growth-oriented firms. Most practitioners currently offer clients of both types the same set of services, typically centered around a core training program that focuses on the development of a business plan. While this product may make sense for the start-up that is seeking to become a full-time enterprise, it is not necessarily the right product for a supplemental or part-time business. From the client's perspective, it may be hard to invest significant time in training if he or she is also working in a wage job and the business represents a relatively small, although perhaps important, component of family income. From the program's perspective, it is important to consider whether it is worthwhile to invest the industry average of \$2,416 (median, \$1,750)<sup>225</sup> in clients whose businesses yield a few hundred or thousand dollars per year with limited prospects for growth.<sup>226</sup> This is not to say that programs should not serve part-time businesses. In fact, as Chapter 4 discusses, the research to date shows that among low-income entrepreneurs, income patchers may have the highest overall

<sup>225</sup>MicroTest Fiscal Year 2003 data, based on 63 organizations submitting data.

<sup>226</sup>Income patchers in the WTW study drew an average of \$4,591 from their businesses, representing 11 percent of total household income. Klein and others, 28. Part-time business owners in the Ms. Foundation study drew an average of \$2,305, or 6 percent of household income. Black, *Enhancing Economic Opportunity Through Entrepreneurship*, 5. It is important to note that these are average rather than median figures. Because typically a few business owners will show very strong business performance, median owners' draw is typically lower than average figures.

household incomes. Rather, the point is that programs should be strategic about what they offer and how much they invest.

On the other hand, clients whose businesses have growth potential typically seek services beyond core training – assistance that can help them expand their markets, manage their growing finances, and manage the addition of employees. Yet, it has been the experience of many programs to “lose” their clients after entry-level training services or one to two loans are completed. FIELD research has identified the value of providing services for at least 12 to 24 months after core training is completed, as the development of businesses demands the use of increasingly more challenging skills. Keeping clients with growth goals requires the development of services that are demand-driven and customized to specific needs. These services must offer both broad and deep knowledge and be provided in one-on-one and group settings. Table 18 below shares some of the lessons that FIELD has gleaned to date about the specific products and services demanded by both part-time and growth-oriented firms.

**Table 18: Product Features for Growth vs. Part-time Microenterprises**

Growth-Oriented Firms	Part-time or “Patchers”
<ul style="list-style-type: none"> <li>▶ <b>“Sector-sensitive” services:</b> information, guidance, market connections and product-development support that is based on a deep understanding of specific business sectors in which microentrepreneurs are engaged. One example is MicroMentor, which connects protégés with mentors across the nation using an on-line matching system.</li> <li>▶ <b>Sector-specific programs</b> that combine assistance in basic business skills with specialized services or training focused on a particular industry, such as child care, crafts, apparel, specialty foods and home construction.</li> <li>▶ <b>Assistance in technology integration.</b> Technology can support clients’ bookkeeping, accounting, branding, marketing, learning and networking.<sup>227</sup> While experience in this area is recent, some programs have taken the lead in providing these services. This area presents an opportunity for partnership with the private sector.</li> <li>▶ <b>Larger-scale loans and patient capital for expansion.</b> Many microenterprise programs have increased their loan sizes to support the financing needs of their larger and growing customers. A few have begun to develop “microequity” products that seek to provide a source of patient capital to help firms with growth potential to finance expansion.</li> </ul>	<ul style="list-style-type: none"> <li>▶ <b>Feasibility assessment</b> designed to help owners determine the income-generating potential of their business ideas, as well as its potential for growth.</li> <li>▶ <b>Focused training</b> on key topics such as pricing, cost management and marketing that can help increase the amount of income derived from the business.</li> <li>▶ Training on how to <b>transfer entrepreneurial skills and experience to better jobs</b> in the formal labor market.</li> <li>▶ <b>Assistance in accessing and maximizing Earned Income Tax Credit (EITC) claims.</b> Many low-income patchers who use self-employment to supplement low-wage work are not aware that income earned from self-employment (and even though bartered services) can be used toward an EITC claim. Programs can provide or connect clients to expertise that will allow them to maximize the value of these claims.</li> <li>▶ <b>Financial services.</b> Demand for loans appears lower among part-time business owners, but access to affordable financial services, including savings mechanisms and health insurance, would likely enhance the stability of the business and family.</li> </ul>

<sup>227</sup>For more information on technology services for entrepreneurs, see Karen Doyle Grossman and others, *FIELD Best Practice Guide: Volume 5 Business First: Using Technology to Advance Microenterprise Development* (Washington, DC: The Aspen Institute/FIELD, August 2003).

Other sub-groups of microentrepreneurs also demand products and services with specific features. For examples, entrepreneurs who are risk averse or those with poor credit histories require specialized financial products and services. Some of these focus on providing equity rather than debt. For example, the field has invested a great deal of effort in the development of Individual Development Accounts (IDAs) as tools for building equity; likewise the Trickle-Up program provides small cash grants. More work and investment is needed if these approaches are to be accessible to and appropriate for larger numbers of entrepreneurs, but they represent important steps forward. ACCION USA recently began offering small credit repair loans to customers – some with businesses; some without – who are seeking to improve their credit scores.

Of course, offering and developing new products entail costs, which raise the additional challenges of achieving both cost-efficiency and some cost recovery. As programs begin to offer new products, they must simultaneously focus on differentiation and efficiency. This will require tracking the incremental costs of offering new products and the benefits – in the forms of new clients, improved outcomes and increased revenues – that accrue to them. It will also involve moving away from one-size-fits-all approaches to invest resources and target products to the clients that can best use them. Finally, practitioners must continue the growing trend of charging clients fees – both as a means of recovering costs and of demonstrating product value. As an example, several leading programs have experimented with membership based models with fees-for-service and offering an array of benefits – technical, marketing and financial – to attract and serve more advanced, growth-oriented clients.<sup>228</sup> As most fees will remain modest, given the financial situation of program clients and their businesses, practitioners will still struggle with the sustainability of services. However, a focus on efficiency and cost recovery will enable the field to stretch scarce resources as far as possible.

## Roles for Differentiating and Broadening Products

### Microenterprise Practitioners:

- ▶ Implement screening and assessment techniques that identify the specific product and service needs of individual clients.
- ▶ Restructure product offerings to offer distinct products to different types of clients.
- ▶ Implement management systems and processes that can track the growth, impact, efficiency and cost recovery of new products and services.
- ▶ Look to charge client fees and focus on cost recovery in evaluating new product offerings.

### Microenterprise Support Organizations:

- ▶ Continue to document the emergence of new microenterprise products and services.
- ▶ Develop and provide technical support and information to practitioners on how to evaluate the feasibility and monitor the effectiveness of new products and services.

<sup>228</sup>More on these models can be found in: Nelson, *Staying Connected* and Elaine Edgcomb and Erika Malm, *FIELD Best Practice Guide: Volume 4 Keeping it Personalized: Consulting, Coaching and Mentoring for Microentrepreneurs* (Washington, DC: The Aspen Institute, August 2002); available from <http://fieldus.org/publications/primevol4.pdf>; Internet.

**Donors:**

- ▶ Provide grants and investment capital for the development and roll-out of new products.
- ▶ Recognize that new product development entails longer-term investment in management structures and systems development, as well as in direct service delivery to clients.
- ▶ Eliminate grant restrictions that prevent programs from charging clients fees.

**DIRECTION 3: RESTRUCTURING THE INDUSTRY FOR GREATER SCALE AND DEPTH**

Better understanding the market and developing new products and services will be important if the industry is to move toward greater scale and impact. However, the industry's current structure, in which most programs are relatively modest in size, is also a key factor that inhibits its ability to achieve greater scale and limits the breadth and depth of services that can be provided to clients. Thus, the field must look to reorganize and restructure if it is to enhance and expand its reach.

It is essential to note here that this does not mean that all microenterprise programs must grow bigger. The localness of microenterprise programs has been part of the field's strength, as programs have been able to develop strong personal connections with clients, tap local sources of funds, and tailor their services to local conditions. However, it is also clear that there are economies of scale in some aspects of program delivery and operations, and that the field must find ways to realize these cost savings. Furthermore, even small-scale programs must find ways to offer a broader range of services and expertise than can be provided by a handful of staff. What we envision, therefore, is the development of a number of large regional and national organizations that offer specialized microenterprise products and services to and through the existing network of microenterprise programs, as well as a set of new relationships among programs at the local level.

There are a number of ways in which new structures could offer efficiencies and broaden product offerings for microenterprise lenders. For example, large-scale national or regional lenders can both lend directly and offer credit products through local microenterprise programs. Larger-scale lenders are able to reduce costs by spreading the expense of certain lending functions (servicing, systems development and so forth) across a large number of loans. Local programs partnering with these lenders could focus on outreach and origination and put a local name and face on loan products, reducing the amount spent on lending functions and, at the same time, offering a better product for their customers. Circle Lending and Count Me In are two organizations offering loan products and services via the Internet. ACCION USA has created a national structure to offer loans in a number of cities across the country. Importantly, in looking to develop and partner with national and regional providers that can offer new products and services, programs should look to for-profit as well as nonprofit providers. For example, Circle Lending is a for-profit firm. It may be that the field can achieve scale as much by helping private sector firms to reach its market, as by expanding the scope of services of nonprofit practitioners.

Smaller microlenders should also look to realize efficiencies by centralizing and outsourcing some functions, such as servicing and portfolio management. These elements of the lending process are areas where considerable economies of scale exist,

and the fact that small-scale programs currently replicate these functions hundreds of times over leads to inefficiencies – either because programs are paying more than they should to perform these services or, in other cases, because they underinvest in these activities. The latter then leads to poor information, which, in turn, leads to higher costs in the form of loan losses or more staff time spent on problem loans. Some outsourcing is already beginning to occur. For example, Alternatives Federal Credit Union currently operates a community lending program in which local nonprofits deposit their loan funds at Alternatives, which, in turn, offers to match the deposit amount with funds available for lending, assists in the development of underwriting criteria (although the nonprofit has final say in the loan parameters), and originates and services the loans. Two experienced lenders are currently exploring the feasibility of providing loan servicing to microlenders and other loan funds across the United States.<sup>229</sup> These efforts are an important first step in this direction and will expand as the industry moves logically in response to the weaknesses in current lending models.

There is room for similar efforts among providers of business training and technical assistance, as well. Particularly as practitioners look to expand the breadth and depth of services they provide, there will be a need to offer expertise beyond the capacities of an organization with a few staff members. National or regional providers – again paired with local practitioners who can give the products a local face, may provide a solution. As examples, Accelerator Online already has the capacity to offer distance learning on business planning across the country. MicroMentor, a project of FIELD, matches mentors with strong industry-based experience to protégés with no regard to geography, linking them by e-mail and phone. As a national organization, MicroMentor’s potential advantage lies in part in its ability to recruit mentors broadly, enhancing its ability to identify individuals whose industry and business experiences more closely match those of the protégé. It can also invest in technology platforms and services that enhance the matching and mentoring process – for example, by allowing the mentor and protégé to “meet” on-line in a manner and at a time that works well for busy individuals. These national efforts and others are necessary to deliver scarce technical content and financial services more directly and efficiently.

We also believe that, in some cases, mergers and partnerships between microenterprise programs will yield important benefits in terms of efficiency and a broader set of product offerings. Within recent years, several microenterprise organizations have completed mergers. These include the merger of ACCION USA and Working Capital and that between PaceWorks and Colorado Microcredit, which formed MicroBusiness Development Corporation in Colorado.<sup>230</sup> Mergers of these sorts make sense in areas where market demand may be limited or in cases where different organizations offer complementary products that may be more efficiently or effectively provided by one entity. In considering ways to realize efficiencies or broaden product offerings, practitioners should look beyond other microenterprise programs to different types of organizations that serve a similar target market. For example, microenterprise programs should look at partnerships with credit unions – even those that may not

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<sup>229</sup>In late 2004, Mary Matthews and Kathy Keeley sent a survey to microlenders and other CDFIs to determine their interests in outsourcing loan servicing to another entity.

<sup>230</sup>For more information on these mergers, see AEO, “Microenterprise Mergers: Industry Trend Towards Scale? Part 1,” (*AEO Exchange*) Issue 5 (January-March 2002) and AEO, “Microenterprise Mergers: Industry Trend Towards Scale? Part 2: The ACCION-Working Capital Merger,” (*AEO Exchange*) Issue 6 (April-June 2002).

currently engage in microlending – that might provide lending functions or services, and/or might also be a source of needed financial services for their clients. Community colleges, which are increasingly offering courses in entrepreneurship education and business management and are one of the primary providers of training for low-income individuals, may also be strong potential partners for microenterprise training programs.

In sum, as the microenterprise field looks to increase its scale, efficiency and range of products, it would benefit from looking at some of the strategies the corporate sector uses to achieve these same goals. Outsourcing some functions; co-branding and distributing products offered by other national, regional or local players; mergers and acquisitions; and strategic alliances all present potential opportunities for building an industry or field-wide structure that can have greater market relevance and impact.

## Roles for Restructuring the Industry

### Microenterprise Practitioners:

- Look to mergers, alliances or partnerships with local, regional and national players as means to offer new products, increase scale and realize operating efficiencies.

### Microenterprise Support Organizations:

- Educate practitioners about the need for industry restructuring; provide examples of how to engage in the restructuring process.
- Assist the emergence of new national and regional structures for service delivery through dialogue with donors, research and other support for institutional development.
- Reach out to potential national and regional partners – both for-profit and nonprofit – to identify potential areas for partnership with the field.

### Donors:

- Invest in the growth of institutions that have demonstrated the potential for greater scale.
- Recognize that "scaling up" requires significant, long-term investments in market research, product development, new technologies, staff capacity and appropriate capital structures.
- Find ways to strengthen small-scale, "retail" service providers through matching them with national- or regional-level specialized services that can increase efficiency or enhance product offerings.
- Encourage small, local programs to look at outsourcing, co-branding, strategic alliances, and mergers and acquisitions.

## DIRECTION 4: USE TECHNOLOGY TO TRANSFORM OPERATIONS

Technology will be one of the field's key tools as it seeks to expand, restructure and offer new products. New technologies have driven and supported the transformation of many of our nation's industries, from financial services to manufacturing to health care. Similarly, new management information technologies played a key role in the dramatic expansion of the microfinance industry in developing countries. It makes sense that technology will play a critical role in the U.S. microenterprise field as well, and, in fact, one of the advantages that the field has in this country, relative to its

counterparts in developing nations, is that we are a nation with superior technological infrastructure and know-how.

The microenterprise field has already begun to incorporate new technologies. A few lenders, including Count Me In, have developed on-line application and decisioning systems for microloans; it also uses its Web site to offer on-line courses and business assistance to its borrowers. ACCION USA has invested in the development of a sophisticated contact management system that provides staff with valuable data on where its clients come from and how they progress through their services, enabling them to identify which marketing channels are most effective and at what points in the process clients drop out of their system. The Northeast Entrepreneur Fund in Minnesota enables customers to register for its in-person Core Four business plan training course on its Web site, as well as offers both an “Introduction to Business Planning” workshop and the full Core Four course on-line. The Jefferson Economic Development Institute in California has used video conferencing to include participants in remote locations in training classes. And, as noted above, MicroMentor has developed a technology platform that matches mentors and protégés; its Web site applications and automatic follow-up e-mails also capture data on clients and the services they receive that generate needed performance data for its donors.

Moving forward, these and other aspects of technology hold promise. Improved management information systems (MIS) will be essential for capturing data that can be used for marketing and market research purposes. In addition, strong management information systems are critical to the development of data necessary to incorporate credit scoring, another technology that can enhance efficiency and improve risk management for lenders.<sup>231</sup> On-line and other distance learning technologies will likely be key to the ability of training organizations to expand their line of training and technical assistance offerings. Additionally, communications and MIS technologies have the potential to assist organizations operating in rural areas to operate more efficiently or to cover larger geographic areas.

In an important step, the Hewlett Packard Company has provided support to a number of programs to integrate new technologies into their operations and client offerings. Its leadership and the lessons from its funding efforts will help to highlight the role that technology can play within programs. However, it is important for programs to recognize that investments in technology can be expensive, and they can fall short of their intended value if they are not selected and implemented appropriately. To maximize the value of these investments, programs must selectively enhance strategic parts of their operations – not simply mimic investments or technology choices made by other programs – and these choices must be based on a technology plan that examines their alternatives in relationship to their programmatic goals, that takes into account the “total cost of ownership” of new technologies, and that fully recognizes the need for staff development to support the technologies being implemented.<sup>232</sup> As the following box describes, practitioners, support organizations and donors all have critical roles to play in realizing the potential of technology to enhance the operations of the microenterprise field.

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<sup>231</sup>As we note in the following section, improved MIS systems are also critical to the expanded collection and use of program performance data.

<sup>232</sup>See Grossman and others, 16-29. The “total cost of ownership” of any new technology includes not only the purchase and installation of hardware and software, but also the training, technical support, replacement costs and Internet charges that are associated with ongoing use and maintenance.

## Roles for Increasing the Use of Technology

### Microenterprise Practitioners:

- Look to incorporate new technologies that can enhance operations, either by partnering with other providers that can provide access to their benefits, if possible, or by implementing them directly.
- Approach investments in technology strategically, recognizing that they will require accompanying investments in staff knowledge and capacity, and ongoing maintenance costs.

### Microenterprise Support Organizations:

- Work with vendors and donors to develop and expand new technologies and technology infrastructures that can support the field (e.g., improved management information systems and credit scoring models).
- Provide training and information to practitioners about how to identify and implement appropriate investments in technology.

### Donors:

- Lend institutional expertise in the implementation and use of technology to improve operations. (Note: This is particularly relevant to corporate donors, particularly those in the technology and financial industries.)
- Support investments in technology, recognizing that implementing them requires accompanying investments in other organizational and staff capacities.

## DIRECTION 5: MEASURE AND IMPROVE PERFORMANCE THROUGHOUT THE INDUSTRY

Better market information, new and differentiated product offerings, and a more efficient industry structure are the keys to enhancing the scale, market relevance and impact of the microenterprise field. Yet, it will not be enough for a few leading practitioners to adopt these approaches. Furthermore, exploring all of these tactics will involve costs, yet not all partnerships, or new products, will bear fruit in the form of new clients, reduced costs, or greater impact at the client level. In order to identify which new approaches truly add value, programs, and the support organizations that work with them, will need to monitor the costs, outputs and outcomes associated with them. And, if the field as a whole is to respond and grow in response to the challenges it faces, it must ensure that improvements in practice and performance are spread widely and not limited to a few industry leaders.

In other words, the field as a whole must dedicate itself to the discipline of pushing on the issues of scale, efficiency and cost recovery, as well as to improving program outcomes. In a constrained funding environment, this discipline is essential to the long-term growth and effectiveness of every program, even those that cannot by themselves reach large scale or full self-sufficiency. Every program needs to make wise choices about where to invest its resources. To do so, programs need tools and systems for measuring performance. They also need to face incentives for higher performance.

There is already a drive to improve performance in the microenterprise field, led by FIELD's MicroTest program and AEO's Standards and Accreditation project.<sup>233</sup> In the former, FIELD has worked during the past six years to develop a set of common

<sup>233</sup>For more information on the MicroTest project, see [www.microtest.org](http://www.microtest.org); Internet. For information on AEO's work on standards and accreditation, see <http://www.microenterpriseworks.org/projects/msap/index.htm>; Internet.

measures by which program performance can be measured and to provide MicroTest member programs with tools and assistance in gathering, interpreting and using data on these measures as part of their ongoing operations. AEO's standards project is working to identify a set of practice and numeric standards that define minimally acceptable program performance.

It is important to note that these efforts must grow and change over time in three important ways. First, they must grow to reach large numbers of programs within the field. Both MicroTest and AEO's standards project envision such expansion; MicroTest is currently engaged in efforts to expand the number of members substantially. AEO plans to obtain broad industry compliance through education and a voluntary accreditation process. Second, they must also be refined over time, both to reflect the diversity within the field and to ensure that the way the field measures performance evolves along with the changes that must occur within it. In measuring and determining performance, it is important to reflect the varying goals that programs pursue and the varying local contexts in which they operate. For example, the critical outcome measures for organizations pursuing microenterprise from a self-sufficiency perspective may be different from the measures used by those seeking economic development outcomes. Third, to be truly effective, they need to go beyond helping programs to identify their strengths and weaknesses to helping them figure out how to improve. This means providing, or linking programs with, sources of information and technical assistance that can help managers address specific challenges and issues.

In order for these efforts to expand and grow, donors can play a key role in supporting the use of performance measures and standards and in rewarding improvements in performance. In part, this will involve supporting the organizational capacities – such as staffing and management information systems – that microenterprise programs need in order to generate and use performance data in a sophisticated manner. One of the factors that has limited participation in existing measurement efforts, such as MicroTest, is that programs simply lack the resources they require.

Donors can also help to lead the drive toward higher performance by increasingly structuring their financial support in ways that reinforce or reward improvement in performance. Such incentive structures will vary depending on the type of funder: whether they are public or private, and local, statewide or national in scope. At the local level, funders that support one or perhaps a few microenterprise programs can work with their grantees to identify areas of strength and weakness relative to national norms and support investments in capacity that can raise the level of performance. At the state and national levels, donors that fund substantial numbers of microenterprise programs can require reporting on measures that go beyond descriptive data or program outputs to more sophisticated measures of efficiency, cost effectiveness and program outcomes. In addition, these donors can create incentives for recipients to move to higher levels of performance. Greater use and support of performance measurement will be particularly important for public donors as a means to ensure accountability and that their resources are allocated to the organizations that can use them most effectively and efficiently.

Moving to a greater and more concerted use of performance measurement among donors may be challenging, but is highly desirable. The field's funders are highly decentralized. And funders do vary in the goals they seek to achieve by investing in microenterprise programs; as a result, they look toward different performance metrics.

For example, some donors are primarily concerned with serving particular target groups of clients and in helping them achieve greater economic self-sufficiency. Other funders are more concerned about how assisted businesses fare and whether these businesses provide jobs in the local community. Yet, while it is important to capture information on these and other outcomes of interest to specific donors, if donors also support a more comprehensive use of standardized performance measures, the field will more quickly improve performance on a wide scale.

In moving forward, then, practitioners and the field's support organizations will need to work to educate funders about the importance of using a set of broad and consistent performance measures. Several private donors and one state agency have already moved in this direction, funding their grantees' participation in the MicroTest program.<sup>234</sup> Additional progress might be facilitated by the development of an affinity group or other collaborative efforts among those who fund microenterprise development that could explore how donors can support and expand the use of performance measurement and standards within the microenterprise field and the donor community.

## Roles for Raising Performance

### Microenterprise Practitioners:

- Connect to national efforts – such as MicroTest and the AEO Standards and Accreditation process – that support and enhance performance.
- Invest in the systems and processes required to collect, reflect and act on data regarding program performance. This includes data collection processes; hardware and software to store, aggregate and organize data for analysis; and processes for reviewing and responding to performance information with program staff and board members.

### Microenterprise Support Organizations:

- Continue to support and expand national efforts such as MicroTest and the AEO Standards and Accreditation process.
- Refine these existing efforts to ensure that they can appropriately reflect differences in program goals and local contexts.
- Educate and work with donors on the creation of performance incentives within key funding streams that support microenterprise programs.
- Recognize that because the field and its donors are so decentralized, state-level support organizations, such as state microenterprise associations, will have a particularly important role in helping both practitioners and funders to increase their focus on performance.

<sup>234</sup>These donors include the Ms. Foundation for Women's Collaborative Fund for Women's Economic Development, the Hewlett Packard Company, JP Morgan Chase, and the Maine Department of Economic and Community Development. The Charles Stewart Mott Foundation also provides grant funding to support the operating costs of the MicroTest program and has also supported AEO's Microenterprise Standards and Accreditation Project, as has the Ford Foundation in the past.

**Donors:**

- ▶ Develop systems for performance-based grantmaking for microenterprise programs:
  - Adopt industry measures and standards (e.g., MicroTest and AEO Standards) to guide grantmaking.
  - Encourage consistent approaches to performance measurement by donors – both public and private – especially in donor affinity groups or collaboratives.
- ▶ Reward performance through grantmaking:
  - Emphasize performance targets; expect grantees to maintain the discipline of pushing to achieve higher scale, effectiveness, efficiency and cost recovery as they work to achieve good business and client outcomes.
  - Require reporting on critical performance measures.
  - Structure grant awards to reward improvements in or higher levels of performance.
- ▶ Invest in building the capacity to measure and improve performance:
  - Support investments in management information systems and other capacities that grantees require to measure and enhance performance.
  - Support the further development and expansion of national systems and tools for measuring performance.

**DIRECTION 6: DEVELOP AND SUPPORT POLICIES THAT DIRECTLY BENEFIT MICROENTREPRENEURS**

Providing products and services to microentrepreneurs is clearly one means of assisting them to start and grow their businesses. However, another means to reach these entrepreneurs is through policy tools that can support them directly – whether or not they enter a microenterprise program. In fact, such policy tools may have the potential to affect much larger numbers of microentrepreneurs.

The microenterprise industry has always recognized that policy is important. To that end, the industry has advocated for the launch and expansion of major funding initiatives at federal and state levels to increase services. These policy efforts have been central to the growth that the field has enjoyed to date. Maintaining these funding sources in the long term will be critical if the field is to move in new and more expansive directions.

However, there are also areas where new policy initiatives, particularly those aimed at supporting microentrepreneurs themselves, could play a key role in supporting the growth of both microenterprises and the programs that serve them. These initiatives cover a variety of areas: programs that support various disadvantaged individuals, efforts to support asset development and access to financial services, health insurance, immigration policy, and local regulatory policies.

***The Role of Self-Employment in Social Welfare Policy***

From its inception, the microenterprise field has advocated that federal and state efforts to integrate disadvantaged individuals into the economy should recognize the value of self- as well as wage employment. The most notable example of this is around welfare policy, now embodied at the federal level in the Temporary Assistance for Needy

Families (TANF) program.<sup>235</sup> However, there are many other types of individuals targeted by welfare and job readiness programs, including: dislocated workers and the unemployed, the working poor, individuals with disabilities, and ex-offenders. It will be important to examine the particular policy barriers faced by each of these groups and to identify ways in which these can be addressed.

### Microenterprise for Welfare Recipients

The microenterprise field's initial efforts to support self-employment for welfare recipients began in the late 1980s with the Self-Employment Investment Demonstration (SEID). Sponsored by the Corporation for Enterprise Development, the demonstration tested self-employment programming with recipients of Aid to Families with Dependent Children (AFDC) in five states. CFED's efforts also focused on efforts to change what were then the key policy barriers facing welfare recipients who started businesses. These related to the program's income and asset rules – for example, those that allowed recipients to own no more than \$2,000 in assets – which caused many individuals to lose benefits early on in the business start-up phase.

With the advent of the TANF program, states had flexibility to create their own income and asset rules, and many chose to create policies that were more supportive of self-employment. However, other policy barriers emerged. For example, the federal statute governing the TANF program does not mention self-employment. Therefore, while careful reading of the law reveals that states can, in fact, allow recipients to count self-employment training activities, as well as self-employment itself, as a work activity, and fund self-employment services, many states are not aware of this option. Furthermore, the “work first” orientation that underlies the TANF program can also create barriers. For more information on the barriers in current TANF policy, as well as a set of recommendations for how the TANF program could be more supportive of self-employment, see: [http://fieldus.org/li/welfare\\_policy.htm](http://fieldus.org/li/welfare_policy.htm).

To ensure that workforce and public assistance programs support self-employment, four types of policy change are needed. First, self-employment must be allowed, or supported, as one of the work activities that can be pursued by recipients of assistance. This often involves broadening definitions of what constitutes “work” to include self-employment. Second, various program rules, such as those regarding the treatment of earned income and assets or those relating to the performance measures used in measuring outcomes, must be adjusted to relate to the specific circumstances of self-employed individuals. Third, the rules regarding the use of funding streams must allow expenditures toward self-employment services, as well as other forms of employment assistance. Finally, work supports – such as child care, transportation and health insurance – that are made available to those engaging in wage employment should also be extended to the self-employed.

<sup>235</sup>The Charles Stewart Mott Foundation funded a demonstration program in which 10 microenterprise programs provided services to TANF recipients. FIELD conducted the evaluation of this demonstration program with assistance from the Center for Law and Social Policy (CLASP). Research findings and policy recommendations resulting from the demonstration can be found at [www.fieldus.org/](http://www.fieldus.org/); Internet. CFED also sponsored several efforts in support of self-employment for welfare recipients; for information on these see [www.cfed.org/](http://www.cfed.org/); Internet.

Recommendations already have been developed for changes to the TANF program that would better support self-employment; as Congress considers reauthorization of TANF, microenterprise support organizations should take the lead in educating policy makers and working with practitioners to advance these recommendations. There has been a significant body of policy work that has enabled individuals with disabilities to more easily pursue self-employment; practitioners who want to target this market can connect to these efforts.<sup>236</sup> In addition, other areas of social welfare policy need to be examined in greater depth. This process must begin with research and policy development to identify the barriers that exist and feasible solutions to these problems. Such work has been led in the past by national policy, research and trade organizations, such as CFED, AEO, FIELD and others; these organizations and others like them should continue to explore ways to open the self-employment option to those who could usefully pursue it.

### *Microenterprise and Asset Policy*

One of the newest and most rapidly growing areas of social welfare policy is asset development. Early on, the proponents and researchers of asset policies for the poor identified self-employment strategies as a key asset-building policy,<sup>237</sup> and the microenterprise field has been a key collaborator in the creation of Individual Development Accounts (IDA), as well as advocate for the broad implementation of this tool through tax policy.

The ability to build savings will be important to the spread and success of microenterprise. One of the constraints to demand faced by microlenders is that some microentrepreneurs – particularly those who are the most low-income, have poor credit histories, or are in the earliest stages of business operations – likely need equity rather than debt financing. Savings can be a key tool to build this equity. While IDA programs have proliferated within the microenterprise community, program staff has identified limitations of these accounts as key sources of business capital. First, the fact that the accounts exist outside the business create an incentive for entrepreneurs to pull income from their business (so that it can be deposited in the IDA and receive matching funds), when it might be better left in the enterprise as working capital. Second, while prospective entrepreneurs can work to build savings in their IDA while planning their business, it may not make sense for those who are ready to start, or are poised to expand their business, to wait for several months or years to build up savings in an IDA. In such cases, other forms of equity will allow for faster progress. As an example, the Trickle-Up Program provides small grants to entrepreneurs in recognition of “sweat equity.” In another approach, some microenterprise programs have helped emerging entrepreneurs file for EITC claims that are then used to finance business start-up or operations.<sup>238</sup>

Those working in the microenterprise and asset-building fields are still working to develop and refine asset-building tools that support business development. This is an area where continuing research and development is needed. What is clear is that the

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<sup>236</sup>For example, The Abilities Fund works extensively with both individuals with disabilities and with rehabilitation professionals and agencies to provide services and create policies in support of self-employment. For more information, see [www.abilitiesfund.org](http://www.abilitiesfund.org); Internet.

<sup>237</sup>See Michael Sherraden, *Assets and the Poor* (New York: M.E. Sharpe, Inc., 1991), 251-257.

<sup>238</sup>In some cases, these EITC payments have also been deposited in IDA accounts, in which case the level of equity available to the business owner is increased.

availability of savings and other forms of equity will be key to the growth and success of microenterprises. The microenterprise field must continue to partner with and support those engaged in designing and advocating for asset-building policy.

### *Access to Financial Services and Health Insurance*

One of the reasons that the poor often stay poor is that they lack a cushion against financial shocks and hardships – illness, a death in the family, and the breakdown of a car. Interviews with entrepreneurs reveal that these events hinder businesses in two ways: by keeping the owner from working or by causing them to pull scarce working capital out of the business in order to meet these personal expenses. Financial services, such as savings and insurance, are tools that middle-income families use to protect themselves against the impact of such financial shocks. However, low-income families generally either cannot access affordable services or must make do with expensive substitutes. Furthermore, all microentrepreneurs – low-income or not – face the special challenges of the self-employed in accessing affordable health insurance.

The microenterprise industry has invested in the development of IDAs as a tool for long-term savings. However, other savings and financial service products – such as low-cost savings accounts and affordable consumer and personal loans for short-term needs, such as car purchases and repair – will also be key to the long-term economic health and self-sufficiency of entrepreneurs who are low-income. Fortunately, there is an emerging body of work in this country on financial services for low-income individuals. Microenterprise practitioners should explore partnering with those offering these products to help entrepreneurs increase their ability to mitigate risk.

Perhaps most importantly, the microenterprise field recognizes that health insurance is a critical issue facing not only its clients, but also millions of microentrepreneurs. There have been some efforts on the part of practitioners and other organizations to try to provide entrepreneurs with access to policies that are at least somewhat more affordable.<sup>239</sup> Making headway on this issue has been difficult, because the question of health care policy is a critical one facing many in our nation and involves many interests beyond those of the microenterprise community. However, the field must weigh in on this issue. The lead role here is for state and national support organizations, which should track the status of key health policy initiatives and ensure that as policy proposals emerge they are responsive to the particular needs of the low-income self-employed.

### *Policy Incentives for Business Formalization*

FIELD's research on the informal economy identified a set of policy and regulatory issues that constrain microentrepreneurs from formalizing their businesses and, in some cases, from growth. These areas include: tax policy, immigration policy that affects undocumented entrepreneurs, policies that constrict categories of businesses and licenses that can be accessed by ex-offenders, and state and local industry regulations that govern licensing and location of specific businesses. While there are often valid concerns underlying specific policies or regulations – health and safety, as prime examples – there are also areas where more openness or the creation of incentives, such as graduated licensing or tax policies, could help many microentrepreneurs improve their livelihoods, even without walking in the doors of a microenterprise program.

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<sup>239</sup>See the FIELD Web site at <http://fieldus.org/li/HealthInsurance.htm> for information and materials regarding initiatives in support of health insurance for low-income entrepreneurs.

The fact is that the informal economy is a significant and growing force in the United States, and that many communities have survived and, in some instances, experienced revitalization and development through informal economic activities. In light of this fact, it might well be beneficial to both the public at large and to microentrepreneurs to revisit some of these existing policies. As an example, there are, of course, entrepreneurs who do not pay taxes, because they believe their competitive advantage lies in the ability to offer their product or service at lower cost. However, there are others who do not pay income taxes, because the initial lump sum of income and social security tax payments – which they often fail to plan for – is unmanageable. The latter set of business owners might well choose to formalize if provided with information and planning assistance and, perhaps, incentives in the form of some sort of amnesty and/or tax credit for first-time filers. Similarly, local zoning or health and safety regulations can pose a significant challenge to microentrepreneurs. If local officials can take a proactive approach to helping them move toward compliance, this may smooth the path toward growth and formalization.<sup>240</sup>

Microenterprise programs have the knowledge and perspective to help both clients and policy makers. They can provide entrepreneurs with information, tools and assistance to come into compliance with regulations, tax policies and other legal requirements. They can also help policy makers see the positive contributions that these enterprises can make, and help identify approaches that accommodate legitimate state concerns, while reducing onerous requirements. Achieving greater scale and impact in the United States may come not only from expanding direct service delivery, but also from enhancing the prospects for entrepreneurial activity through changes in the legal and regulatory environments that surround it.<sup>241</sup>

## Roles for Policy Development

### Microenterprise Practitioners:

- ▶ Assist state and national organizations, as necessary, by identifying local resources that can inform their policy development efforts (i.e., state or local policy makers or public employees who have developed supportive policies, and local advocacy organizations).
- ▶ Engage in advocacy in support of public policies that can support program clients and other local entrepreneurs.

### Microenterprise Support Organizations:

- ▶ Take a lead role in research and development of policies in the areas of social welfare policy, asset policy, and tax and regulatory policy.
- ▶ Educate members of Congress and support advocacy for changes in the TANF program in support of self-employment.
- ▶ Work with organizations and policy makers in the forefront of health care policy to ensure that policy proposals aimed at increasing health insurance coverage reflect the needs of microentrepreneurs.

<sup>240</sup>For an example of such a proactive approach, see Shirk and Wadia, 57-60.

<sup>241</sup>Examples of organizations that are working on policy issues can be found in Tamra Therford and Elaine Edgcomb, *FIELD Forum Issue 15: Microenterprises in the U.S. Informal Economy: Summary Research Findings* (Washington, DC: The Aspen Institute/FIELD, July 2004); available from [http://fieldus.org/publications/Field\\_Forum15.pdf](http://fieldus.org/publications/Field_Forum15.pdf); Internet.

- ▶ Continue to build and expand relationships with policy, research and advocacy organizations in other fields that can inform or support policy initiatives relating to self-employment.

**Donors:**

- ▶ Provide funding in support of policy development and research on new policies that can support emerging and low-income entrepreneurs.
- ▶ Seek ways to connect the organization's funding and grantees in these other policy areas – asset building, health insurance and health care, immigration policy – with microenterprise support organizations and the microenterprise field.

## **DIRECTION 7: DEVELOP NEW STRATEGIES TO STABILIZE AND SUSTAIN PROGRAMS**

One of the clear lessons the microenterprise field has learned is that achieving self-sufficiency – fully covering program costs through fees charged to clients – will be difficult for microenterprise credit programs and clearly unfeasible for institutions that focus on training. This is a difficult lesson to learn, as relying on donor funds always introduces uncertainty (although it is a misconception to believe that private firms do not face uncertainty, as shifting market conditions and other factors can clearly impact their ability to attract customers and generate revenues). The current funding environment, where donor resources are more scarce and much of the funding that is available provides only single-year support, increases the challenges that programs face in trying to raise funds and invest in the capacities required to grow and innovate.

In order to make progress toward growing and sustaining itself, the field must move in three key directions: demonstrating the value of microenterprise programs, developing strategies for sustainability that combine greater revenue generation with external support, and developing sources of multiyear funds that can enable greater stability and better position programs for growth.

In order to justify subsidy by public and private donors, the field needs to demonstrate its value – in other words, to show that investments in microenterprise yield benefits in excess of their costs. To do so, the field needs more rigorous evaluations that use experimental research designs. Designing and implementing high-quality evaluations will not be easy; they require significant resources in themselves, and there remain challenging design and technical issues to be resolved. For example, it is difficult to track low-income individuals over time and to obtain accurate business information from them. Yet, engaging in long-term follow-up will be required, as the benefits of business ownership should ideally be measured over the long term (e.g., five years). Furthermore, selecting the appropriate programs for study will be a challenge. Should the field select a random sample of programs, so that the studies show the impact of “average” or “representative” programs? Or, should they focus on programs that have achieved the highest levels of performance, so that the evaluation reveals the potential impact of programs? However, despite the challenges involved in producing solid research on this issue, the time for rigorous evaluation is now.

Secondly, while most programs should not anticipate achieving total self-sufficiency, they must continue to explore avenues for increased cost recovery. Focusing on cost recovery is key if programs are to invest their resources efficiently. It is also important if programs are to achieve a more balanced mix of revenues and demonstrate that their services provide value to clients. Thus, programs are increasingly moving to charge fees to their clients, while recognizing that most clients do have limited resources. This trend must continue and it must be supported by donors, who should reduce restrictions on the ability of their grantees to charge fees.

Programs also are looking to increase their levels of cost recovery and/or to diversify their revenue streams by operating businesses or business activities that generate new revenue streams. These initiatives range from kitchen incubators to retail stores that sell the clients' products, to printing or coffee shops that provide services to local customers and also provide business experience to program clients who have the opportunity to work in the enterprise. While these enterprises have the potential to bring in new sources of revenue, they do require management expertise, investment of resources, and knowledge of the local market and industry. Such ventures can be a source of new revenues, but they also can divert organizational resources and capacity away from a microenterprise program's core business. There is an emerging body of knowledge around what it takes to successfully launch and operate these "social enterprises;" practitioners should look to these sources as they explore whether this type of venture could contribute to their program's overall sustainability.<sup>242</sup>

Finally, programs that have demonstrated stronger levels of performance need funding that can stabilize them and position them for growth and change. With the preponderance of funding being distributed as one-year grants, programs spend too many of their resources – important, high-level management and leadership time – in the continuous pursuit of funds to sustain their operations. In this situation, it is difficult to dedicate the time that is required to plan and build the capacity for growth. Moreover, programs become reluctant to invest in growth or in new products and services, if it is unclear that they can be sustained over the longer term. Donors that want to help take the field to the next level of development, should consider providing capital in new ways. Specifically, programs will need access to multiyear funding commitments that support and build the key management and organizational capacities that provide long-term stability to the programs and help to position them to invest in growth and new product development.

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<sup>242</sup>For more on this, see the Social Enterprise Alliance, <http://www.se-alliance.org>; Internet.

## Roles for Enhancing Stability and Sustainability

### Microenterprise Practitioners:

- ▶ Place a continued focus on cost recovery in evaluating existing programs, as well as newly proposed products and services.
- ▶ Explore new opportunities for cost recovery (client fees) and revenue generation (social enterprises).

### Microenterprise Support Organizations:

- ▶ Document and support learning among programs regarding successful cost recovery and revenue generation strategies.

### Donors:

- ▶ Support research that uses an experimental design to document the impact of microenterprise programs – as a means to demonstrate the value of the strategy to public and private funders.
- ▶ Help programs pursue new cost recovery mechanisms by removing restrictions on client fees and encouraging graduated fee schedules and fee-based programs for clients.
- ▶ Provide feasibility study and testing money for new approaches to cost recovery.
- ▶ Provide longer-term, more substantial funding to programs that have demonstrated progress and the potential for high impact.

## DIRECTION 8: REPOSITIONING THE MICROENTERPRISE FIELD

One of the key factors limiting the microenterprise field may be its name – and how that name is perceived by both its primary market and potential funders. One clear finding from the market research conducted to date is that the field’s target population does not use the term “microenterprise” or recognize itself in that language. Programs typically do not use that term in their marketing materials, instead asking clients, “Do you want to start a business?” or “Do you need cash for your business?”

The field came to its current name for several reasons. First, the term was in broad use in the developing world, in programs that targeted small-scale, informal enterprises. As noted in Chapter 2, the origins of the U.S. field come in part from these international models, and in the early years, the press generated by leading organizations from overseas – such as the Grameen Bank – helped to create some resonance among the U.S. public for the programs emerging here at home. Furthermore, when the field originated in the United States, there was already an existing infrastructure of programs that worked with small businesses: Small Business Development Centers, Small Business Investment Companies, and business revolving loan funds. The term “microenterprise” served to differentiate these new programs and their target market from these existing initiatives.

However, the term microenterprise also has significant limitations in the United States setting. First, it describes the field in terms of the size of the businesses that it serves, instead of the characteristics of its owners, their aspirations or their goals. Although it is the case that the large majority of “microenterprises” are very small, some of them have the potential and the desire to grow, and very few think of themselves as

being “micro” in scale. Therefore, many programs do not use the word “microenterprise” when marketing their products and services to clients.

Second, the term microenterprise also fails to resonate with some potential donors and supporters. Funders who approach microenterprise with the goal of poverty alleviation have less difficulty with the term, as many of them are familiar with and have, in some cases, funded programs overseas, which are targeted toward the poor. However, for donors who are interested in enterprise development from an economic development perspective, the name implies that the strategy focuses solely on very tiny businesses, which lack the potential to grow and contribute to the local economy. As we noted previously, while most microenterprises stay small, some do grow and provide jobs for others; a few such businesses have the potential to make an important impact in a declining community or neighborhood. Thus, the name appears to belie the value of this strategy in some settings.

In a similar vein, the commonly used definition of microenterprise – a business with five or fewer employees that requires \$35,000 or less in start-up capital and that does not have access to the traditional commercial banking sector – is also misleading or limiting in some ways. It suggests that the primary focus of microenterprise programs is to provide credit, when the experience in the field to date is that most clients come to programs in support of business skills and information. It also again implies that the businesses assisted are only those that are small – not those that begin small and may or may not grow larger over time. There was a logic to this definition when it emerged: first, it was believed that most clients would require and seek capital; and second, the qualifiers that they were small and could not access traditional capital was a proxy for the fact that their owners faced barriers to traditional sources of business assistance, due to income, discrimination or other factors. While the field continues to define its market as those who cannot or do not receive assistance through other channels, this definition is now confusing to many who are trying to understand the field.

Repositioning the field will require action in three areas: creating language and messages that better convey the field’s purpose, targets and outcomes; better documenting the outcomes and impacts of microenterprise from an economic development perspective; and strengthening connections to the broader economic and enterprise development communities. In the first area, the field needs to engage in a communications effort to craft language that is more accurate and effective. Although this effort must engage practitioners, it should be initiated and led at the national level, in order to assure its consistency and use across the broader field. In the second area, as we noted previously, research on the economic development effects of microenterprise is clearly needed and will be the role of research organizations, hopefully joined by academics with an interest in microenterprise development. Better connections to the economic development and enterprise community will need to be forged both at the national and local levels. They will be most important at the local level, as programs find ways to develop effective relationships and partnership with other business development programs and with policy makers in their areas, so that they can integrate themselves into local enterprise systems. However, their local partners often turn to national organizations (such as trade associations) for information and guidance, so partnerships at the national level will also be important.

## Roles for Repositioning the Field

### Microenterprise Practitioners:

- ▶ Seek to build new or strengthen relationships with the local enterprise and economic development communities, as appropriate to the organization's mission.
- ▶ Provide input into national efforts to craft a new language for the field.

### Microenterprise Support Organizations:

- ▶ Engage in a national communications effort to craft a more accurate and effective language and message for the field.
- ▶ Conduct research focusing on the economic development outcomes and impacts of microenterprise programs.
- ▶ Develop partnerships with national economic and enterprise development organizations.

### Donors:

- ▶ Provide funding in support of a communications effort and for research into the economic development effects of microenterprise.
- ▶ Connect microenterprise grantees (at the national, state and local levels) with other grantees in the economic and enterprise development fields.

## Conclusion

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**S**mall-scale enterprise has a long history in the United States, and it is clear that it has an important role to play in our current economy. Microenterprise programs have emerged during the past 20 years as a means to extend the option and benefits of business ownership to individuals who have traditionally not been the targets of business development policy. In an economic environment where too many families and communities are struggling, microenterprise programs add value by opening and supporting an additional option in the workplace, broadening opportunities to own and build assets, and ensuring that economic development policies support the full range of entrepreneurial activities.

The microenterprise field has enjoyed rapid growth in this country, fueled by many forces: the lure of stories about successful entrepreneurs, interest in its unique ability to bring together social welfare and economic development approaches, and the need to create new economic opportunities in many communities. It has learned as it has grown. Some lessons have reaffirmed the value of the microenterprise strategy: programs have found that low-income individuals can start and operate businesses and that their businesses can grow. They also have learned that they can lend to emerging businesses and achieve high rates of repayment. Some of the lessons also have been difficult: for example, the realization that the road to scale and sustainability will be far more challenging than in developing countries where the microenterprise market is much larger and more visible.

As the industry moves into its next decade, it must continue to learn, innovate and stretch its capacity. If the field is to meet the demands of the market that appear to exist, as well as the expectations of its funders and supporters, it must find ways to expand the size and breadth of its services. This requires developing a much more sophisticated understanding of the microenterprise market, creating new products and delivery structures that tap into true demand and allow for large-scale delivery, and ensuring that programs across the field achieve high levels of performance and impact. Practitioners, working in tandem with new partners in both the private and nonprofit sectors, must play a key role in developing new approaches and in seeking efficiencies in their current work. Funders and intermediaries will play a key role, both in providing the funding necessary to innovate and grow and in pushing practitioners to higher levels of performance. Moreover, policy change will continue to be critical, both in removing barriers that face low-income business owners and in creating structures that provide the financial tools that can help these entrepreneurs to achieve higher levels of success and economic security.

In today's economy, low-income individuals need the microenterprise option. The microenterprise field has opened it to some; now is the time to take the steps to ensure that it is available to many.



## Estimating the Scope of Self-Employment and Microenterprise in the United States

This appendix presents a detailed discussion of the estimated size of the microenterprise sector and the estimated potential market for the targeted services offered by microenterprise programs, as discussed in Chapter 1 of this paper.

### Microenterprise and Self-Employment in the National Economy

A number of national data sources are useful in estimating the number of microenterprises in the United States. The Association for Enterprise Opportunity (AEO), the trade association of microenterprise programs in the United States, estimated that, in 2001, there were 20.7 million microenterprises in the United States. This estimate includes all businesses with fewer than five employees and is based on data from the U.S. Census Bureau's Non-Employer Statistics combined with data from County Business Patterns, published by the U.S. Department of Commerce.<sup>243</sup> Based on this data, AEO also estimated that these microenterprises together employed a total of slightly more than 27 million individuals, including the business owners.<sup>244</sup> These workers accounted for 16.6 percent of total private non-farm employment in 2001. In addition, FIELD calculates that, based on this methodology, microenterprises represent 86.4 percent of all enterprises in the United States.<sup>245</sup>

Another general estimate of the number of microenterprises can be determined by examining the number of sole proprietorships. A sole proprietorship is an unincorporated business that is owned by one individual. According to the IRS, there were 20,378,335 non-farm sole proprietorships in 2001.<sup>246</sup> This represents a steady increase since 1995, when there were fewer than 18.4 million sole proprietorships. It is important to note that some sole proprietorships have employees, and, thus, some of the firms included in this estimate may be larger than microenterprises.

ACCION USA, one of the major microenterprise programs operating in the United States,<sup>247</sup> conducted market research in 1999 to try to determine the size of the U.S. market for microenterprise loans. Their research, which drew on both a range of secondary sources as well as random enumeration studies in nine markets, estimated that there were 13.1 million microentrepreneurs in the United States, of whom 82

<sup>243</sup>The methodology used by AEO was developed by James C. McConnon, Jr. and Thomas Allen of the University of Maine. For more information, see [http://www.microenterpriseworks.org/services/policy/mees/us\\_sheet.htm](http://www.microenterpriseworks.org/services/policy/mees/us_sheet.htm); Internet.

<sup>244</sup>Estimates from the AEO Web site; see [http://www.microenterpriseworks.org/services/policy/mees/us\\_sheet.htm](http://www.microenterpriseworks.org/services/policy/mees/us_sheet.htm); Internet.

<sup>245</sup>Calculations by FIELD, based on the methodology used in the AEO estimates.

<sup>246</sup>See <http://www.irs.gov/pub/irs-soi/01sp10si.xls>; Internet.

<sup>247</sup>ACCION USA provides assistance to a network of five separate microenterprise organizations in the U.S. and also directly operates microenterprise lending programs in three cities: Miami, Atlanta and the Boston area.

percent had not previously received a bank loan and 45 percent had never even considered one.<sup>248</sup>

Data regarding self-employment is derived from yet another source, the Current Population Survey (CPS) of the U.S. Census Bureau. According to the CPS, in 2003, there were 9.34 million unincorporated self-employed workers; these individuals represented 6.9 percent of the total nonagricultural labor force.<sup>249</sup> In addition, there were 4.8 million incorporated self-employed individuals who represented an additional 3.6 percent of non-farm workers.<sup>250</sup>

It is important to recognize, however, that only individuals who identify self-employment as their *primary* source of employment are included in the self-employment figures. Thus, individuals who engage primarily in wage employment and operate a business on the side are not included in this statistic. In fact, the U.S. Census Bureau reported that there were 16.9 million non-employer firms (firms without employees) in 2001.<sup>251</sup> This figure is 72 percent higher than that of the number of self-employed workers for that year, suggesting that there are a significant number of individuals who own businesses without employees, yet who are not counted as self-employed.<sup>252</sup> It may well be that many of these firms are what one might call “sideline” businesses – firms operated by individuals and used to supplement their primary employment in a wage job. Based on data from the Current Population Survey, in 2003 1.5<sup>253</sup> million U.S. workers were classified as second-job entrepreneurs. It is probably also the case that some self-employed individuals operate more than one business (although it is unclear how many), and that this may contribute to the fact that there are more non-employer firms than there are self-employed individuals.

Finally, it is important to recognize that the above statistics do not include the many individuals who operate businesses in the informal economy<sup>254</sup> – defined as firms that are engaged in licit business activities, but fail to comply with the business reporting or licensing practices that would cause them to be included in the above statistics.<sup>255</sup> Some individuals who work in the informal economy are in fact wage employees, working for businesses that choose not to report their employment. Others, however, operate their own enterprises.

There are some estimates of the scope of the informal sector in the United States, although most of these are many years old. In 1983, a study by the Joint Economy Committee of the U.S. Congress estimated that 27.1 percent of men and 13.5 percent of women were engaged in the informal economy.<sup>256</sup> More recently, other research has

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<sup>248</sup>ACCION International, *The Microlending Market in the United States, Executive Summary* (September 1999).

<sup>249</sup>Hipple, 14.

<sup>250</sup>Hipple, 15.

<sup>251</sup>Internal Revenue Service, <http://www.census.gov/epcd/nonemployer/pdf.html>; Internet.

<sup>252</sup>There were 9,826,000 self-employed workers in 2001 and 16,938,220 non-employer businesses in that same year.

<sup>253</sup>Hipple, 20.

<sup>254</sup>For a more detailed discussion of the informal economy and microenterprise in the United States, see Erika T. Malm, *FIELD Forum* Issue 14: *The Informal Economy and Microenterprise in the United States* (Washington, DC: The Aspen Institute, March 2003).

<sup>255</sup>We distinguish here between the informal economy, which does not comply with required reporting and tax filing requirements, and the underground economy, which involves business activity that is illicit in nature – such as drug dealing and money laundering.

<sup>256</sup>D. O'Neill, *Growth of the Underground Economy, 1950-81: Some evidence from the Current Population Survey*, Joint Economic Committee, Congress of the United States (Washington, DC: U.S. Government Printing Office, 1983).

suggested that this finding may have underestimated the engagement of women in the informal economy, by indicating that female-dominated occupations are those most likely to be associated with non-payment of social security taxes. Other estimates of the size of the informal sector have estimated that it may range in size between 15 and 25 percent of GNP.<sup>257</sup>

Based on the above figures, it is reasonable to infer that there are at least 20 million microenterprises in the United States, and that this figure is likely an underestimate given the lack of data on the number of businesses operating in the informal sector.

## Microenterprises as a Percent of Total Business Establishments

In estimating the number of microenterprises in the United States, AEO adds the number of non-employer establishments (data from Nonemployer Statistics, Census Bureau) and the number of establishments with fewer than 5 employees (data from County Business Patterns, Census Bureau). The data that is currently available on the Census Bureau Web site is slightly different from that used in the AEO estimate; this could be due to revisions to the data after the reports were published.

	Establishments With No Employees	Establishments With Employees		
		1 to 4 Employees	5 and More Employees	Total
Updated numbers	16,979,498	3,817,930	3,277,372	7,095,302
Original numbers from AEO	16,938,220	3,807,856	–	–

Based on these figures, FIELD estimates the number and percent of microenterprises as follows:

Total number of establishments = 16,979,498 + 7,095,302 = 24,074,800.

Number of microenterprises = 16,979,498 + 3,817,930 = 20,797,428.

Percent of microenterprises = (20,797,428 / 24,074,800)\*100% = **86.4 percent.**

## Estimates of the Number of Microenterprises in Specific Target Groups

The above estimates describe the overall scope of the microenterprise sector within the U.S. economy. However, the microenterprise industry defines itself primarily as providing services to individuals who face barriers in accessing traditional business development services. The following discussion presents estimates of the number of microentrepreneurs within the key target groups that are the focus of most microenterprise programs.

<sup>257</sup>Richard B. McKenzie and Dwight R. Lee, "Government in Retreat," *NCPA Policy Report* No. 97 (1991).

**Low-Income Entrepreneurs.** Many of the databases that capture information on business ownership and self-employment do not focus specifically on the family income levels of those individuals. This makes it a challenge to estimate the extent to which low-income individuals are engaged in microenterprises. However, some figures are available. For example, in 2002, 1.7 million self-employed individuals (or 17.9 percent of the self-employed) had family incomes below 150 percent of the federal poverty thresholds.<sup>258</sup>

Again, the self-employed represent only some of the business owners in the United States. The last year for which income data are available on the owners of business enterprises is 1992, and these statistics provide data on only the personal income of the owner – not the family income. According to these figures, more than 4.3 million of the 16.2 million business owners operating in 1992 – or 26 percent – had personal incomes less than \$10,000.

**Microenterprises with Difficulty Accessing Bank Financing.** Estimate from market study conducted by ACCION International in 1999.<sup>259</sup>

**Women Microentrepreneurs.** The vast majority of women-owned firms have fewer than five employees. Data from the 1997 Economic Census allows us to characterize the size of women-owned firms. These data indicate that of the slightly more than 5.4 million women-owned firms that existed in that year, almost 5.13 million had fewer than five employees.<sup>260</sup>

**Racial and Ethnic Minorities.** The figures in the table are based on slight upward revisions of data from the 1992 SMOBE (as cited in a study by Robert Fairlie). Although these data are somewhat dated, they do include sideline as well as primary businesses. The study by Fairlie also includes 1998 data from the Current Population Survey, although these data include only primary businesses (i.e., those for individuals whose primary form of employment is self-employment.)<sup>261</sup> The figures for each are as follows:

Number of Minority-Owned Firms		
	SMOBE, 1992	CPS, 1998
African American	620,912	393,000
Hispanic	771,708	675,000
Asian	606,426	475,000
Native American	n/a	75,000

The ACCION market research study estimated there were 1.2 million Hispanic microentrepreneurs and 1.2 million African American microentrepreneurs in 1999. In addition, the First Nations Development Institute estimated that there were 170,083

<sup>258</sup>U.S. Department of Commerce, Bureau of the Census, Current Population Survey, March Supplement, March 2002, and FIELD calculations based on data downloaded from <http://ferret.bls.census.gov/cgi-bin/ferret>; Internet.

<sup>259</sup>ACCION International, *The Microlending Market in the United States, Executive Summary*.

<sup>260</sup>U.S. Bureau of the Census, *Women Owned Business Enterprises*, 1997 Economic Census, Table 7; available from <http://www.census.gov/prod/ec97/e97cs-2.pdf>; Internet. Note that these figures include firms with no paid employees.

<sup>261</sup>Robert W. Fairlie, *Recent Trends in Ethnic and Racial Self-Employment* (Department of Economics, University of California Santa Cruz, Joint Center for Poverty Research Northwestern University, and University of Chicago, November 2000); available from <http://econ.ucsc.edu/~fairlie/papers/recent13.pdf>; Internet.

Native American-owned microenterprises in 2000.<sup>262</sup> Based on these combined findings, we believe that the estimates in Table 1 are a reasonable (and somewhat conservative) estimate of the number of minority-owned firms.

**Individuals with Disabilities.** Individuals with disabilities also comprise a substantial potential market for microenterprise programs. Of the 49.7 million people who reported themselves as having a disability on the 2000 census, 30,553,796 are non-institutionalized working age adults between 21 and 64 years of age.<sup>263</sup> As noted in Chapter 1, U.S. Census data from 1983 found that individuals with disabilities were almost twice as likely to engage in self-employment as those without – 14.7 percent vs. 8 percent.<sup>264</sup> Similarly, researchers with the U.S. Department of Labor found that women with disabilities were 1.5 times more likely to engage in self-employment than those without, and that men with disabilities were 1.3 times more likely to engage in self-employment.<sup>265</sup> FIELD estimated a potential rate of self-employment among disabled individuals by applying a factor of 1.5 times the self-employment rate for all workers of 6.8 percent in 2000,<sup>266</sup> yielding a self-employment rate of 10.2 percent for disabled individuals. Applied to the total number of working-age individuals with disabilities in 2000,<sup>267</sup> this yields an estimated 3.12 million individuals who would be self-employed.

**Welfare Recipients.** The National Survey of America's Families (NSAF), conducted by the Urban Institute, includes a component that collects data on TANF leavers (individuals who are former recipients of TANF assistance). NSAF findings indicate that, in 1997, 6.8 percent of TANF leavers sampled were self-employed.<sup>268</sup> In Fiscal Year 2002, the TANF caseload averaged 2,064,373;<sup>269</sup> FIELD multiplied this figure by the 7 percent from the NSAF study to achieve an estimate of 140,377 who would become self-employed.

**Unemployed Individuals.** The loss of a job has always been one force that has “pushed” individuals to pursue self-employment. While clearly self-employment is not for all unemployed workers, there are those who will choose to pursue it – either because of a long-standing interest in working for themselves or a lack of other job opportunities in the local labor market.

For many years, federal policy that governed unemployment benefits created disincentives to unemployed individuals seeking to pursue working for themselves. To qualify for benefits, individuals were required to be “looking for work,” which effectively prevented them from investing time in planning and starting a business. Beginning in the late 1980s, the U.S. Department of Labor sponsored a demonstration program that examined, in two states, the potential and value of self-employment for some unemployed individuals. The demonstration efforts provided both business start-up

<sup>262</sup>First Nations Development Institute, *Native American Entrepreneurship Report* (Fredericksburg, VA: First Nations Development Institute, 2002). Unpublished study.

<sup>263</sup>Andrew Houtenville, *Disability & Employment in the USA: National Overview Based on the 2000 Census* (RRTC, 2002).

<sup>264</sup>Seekins, *Rural and Urban Employment Patterns*.

<sup>265</sup>Messenger and Stettner, 57.

<sup>266</sup>Hipple, 14.

<sup>267</sup>Of the 49.7 million people who reported themselves as having a disability on the 2000 census, 30,553,796 were non-institutionalized working age adults between 21 and 64 years of age. Houtenville.

<sup>268</sup>Loprest, 13.

<sup>269</sup>This figure is for the average number of families that received assistance in 2002. See <http://www.acf.dhhs.gov/news/stats/newstat2.shtml>; Internet.

services and financial assistance (in one state, an ongoing payment of bi-weekly unemployment benefits; in the second, regular bi-weekly payments were accompanied by eligibility for a lump-sum payment).

The evaluation of the demonstration, which used a classical experimental design, found that between 2 percent and 4 percent of new unemployment insurance claimants chose to pursue self-employment when offered the opportunity.<sup>270</sup> Using the midpoint figure of 3 percent and applying this to the 8,378,000 individuals who were unemployed in 2002<sup>271</sup> provides an estimate of 251,430 unemployed individuals who would pursue self-employment.

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<sup>270</sup>Benus and others, iv–v.

<sup>271</sup>See the series for 1948-2003:

[http://data.bls.gov/servlet/SurveyOutputServlet?data\\_tool=latest\\_numbers&series\\_id=LNU03000000&years\\_option=all\\_years&periods\\_option=specific\\_periods&periods=Annual+Data](http://data.bls.gov/servlet/SurveyOutputServlet?data_tool=latest_numbers&series_id=LNU03000000&years_option=all_years&periods_option=specific_periods&periods=Annual+Data); Internet.

## Calculation of Costs and Benefits

Chapter 3 presents a preliminary analysis of the costs and benefits associated with microenterprise program services. The analysis is based on cost and outcomes data provided by 17 member programs that participated in MicroTest's outcomes tracking process in 2004. These 17 programs were part of the first cohort of MicroTest members to apply new protocols for collecting uniform outcomes data across the industry. All MicroTest programs were eligible to participate in this data collection initiative, and a subset of 22 chose to do so. However, only the data from 17 of those 22 could be used for this analysis due to a set of issues that emerged during the analysis and will be described below.

The 17 organizations included the following: ACCION New Mexico (N.M.), Goodwill Industries of North Georgia (Ga.), Jefferson Economic Development Institute (Calif.), PPEP Microbusiness and Housing Development Corp. (Ariz.), Center for Rural Affairs (Neb.), Washington Community Alliance for Self-Help (Calif.), Women Entrepreneurs of Baltimore (Md.), West Company (Calif.), Women's Economic Ventures of Santa Barbara (Calif.), Women's Initiative for Self-Employment (Calif.), Women's Rural Entrepreneurial Network (N.H.), Community Financial Resource Center (Calif.), Acre Family Day Care (Mass.), Cobb Microenterprise Center (Ga.), Good Faith Fund (Ark.), Native Americans for Community Action (Ariz.), and Justine Petersen Housing and Reinvestment Corporation (Mo.).

These programs have important characteristics that distinguish them from the industry as a whole. The participating programs were more likely to offer credit than the overall industry (76 percent offered credit versus 64 percent of those organizations that reported data on their methodology for the *2002 Directory of U.S. Microenterprise Programs* (198 of 308 programs). More than a third of clients responding had loans. The participating programs were somewhat more mature than the field as a whole. As of Fiscal Year 2000, the mean and median ages of the participating programs were 7.5 and 7.4 years, respectively. The mean and median ages of the programs in the industry in Fiscal Year 2000 were 7 and 5 years, respectively. Compared to the MicroTest organizations as a whole, the programs participating in the outcomes survey were more likely to be training-led (76 percent vs. 46 percent) and serve a higher percentage of women (76 percent vs. 56 percent). The programs participating in the outcomes survey were also more likely to serve clients who were pre-business at intake than the full MicroTest group (49 percent vs. 34 percent) and somewhat less likely to serve clients with start-up businesses at program entry (22 percent vs. 28 percent).

### The Data Collection Process

The process these organizations followed consisted of guided collection of outcomes data from a sample of program clients, using protocols and tools developed by MicroTest. All participating programs received training by MicroTest staff and drew a random sample of their clients. The sample was drawn from clients who received

program services during Fiscal Year 2002. Clients in the sample were interviewed in the first quarter of 2004 and asked to report if they were in business during 2003 and to provide data regarding business sales, owners' draw, employment and household income, and other points of interest. Clients also indicated if they were still in business at the time of the survey.

The size of the sample was based on program size. Programs with fewer than 100 clients attempted to survey all of them. Programs with 100 clients or more attempted to survey a sample of 100. All interviews were conducted by phone or in person.

## **Data Analysis**

The data were submitted to Aspen and then cleaned and analyzed by Aspen staff. During the first phase of analysis, five programs' data were deleted from the data set for the following reasons.

One organization's data were eliminated because the organization collected data on only a very limited and special subcomponent of their program in response to donor needs. This component, focused on a prison population, is unrepresentative of their overall program and very small. Three others were eliminated due to two factors: they had low response rates (between 17 percent and 52 percent) *and* they did not provide intake data on all those they attempted to survey, thereby making a respondent analysis impossible. A fifth institution's data were eliminated because of a limited response rate, 35 percent, and the presence of bias in the data revealed by a visual inspection. (The business status of 60 percent of the clients in the original sample was not known. Thirty-nine percent were ongoing businesses and one percent were start-ups. The interviewed group, however, consisted almost exclusively (94 percent) of ongoing businesses.

Among the remaining 17 programs, three were included even though they did not submit sufficient intake data to conduct a respondent analysis. In two of the cases, they succeeded in interviewing 100 percent of their sample, obviating the concern. In the third case, the response rate was 66 percent, which, we decided, was sufficiently high to include in the analysis group.

A respondent analysis was then completed on the 14 programs that provided adequate intake data on all members of their sample. For these programs, the following test was performed. The last row of the table on page 117 presents the percentage distribution of the categories in the original sample that the programs attempted to interview. We would expect the interviewed group to have the same kind of distribution for the sample to be unbiased with respect to this characteristic. For example, we would expect there to be 25.7 percent start-ups in the interviewed sample. Since the programs interviewed 671 clients, there should be 172.4 start-ups in the final data set (25.7 percent of 671).

<b>Business Status at Intake</b>						
		<b>Start-up</b>	<b>Ongoing</b>	<b>No Business</b>	<b>Unknown</b>	<b>Total</b>
Not Interviewed	Count	133	152	184	39	508
	%	26.2%	29.9%	36.2%	7.7%	100%
Interviewed	Count	170	259	190	52	671
	%	25.3%	38.6%	28.3%	7.7%	100%
Total	Count	303	411	374	91	1179
	%	25.7%	34.9%	31.7%	7.7%	100%

Using the same logic, the “expected” numbers for each category were calculated. These then were juxtaposed against what we actually observed in the interviewed group, as follows:

	<b>Observed (n)</b>	<b>Expected (n)</b>	<b>Residual</b>
Start-up	170	172.4	-2.4
Ongoing	259	234.2	24.8
No Business	190	212.7	-22.7
Unknown	52	51.7	0.3
Total	671		

As can be seen, the actual proportions of categories are not very different from what they would be expected to be. This is confirmed by the formal Chi-square test: the interviewed group is not statistically different from the original sample with respect to the business status at intake.

<b>Chi-Square Test</b>	
<b>Business Status at Intake</b>	
Chi-Square	5.092
df	3
Asymp. Sig	0.165

Similarly, for the group of 14 programs, the analysis found no significant differences between the respondents and non-respondents in terms of the average household income at intake. As the tables below show, the t-test for equality of means ( $t = 1.640$  because Levene’s test indicates equality of variances) indicates that statistically there are no significant differences between the two group means.

<b>Group Statistics</b>					
		<b>n</b>	<b>Mean</b>	<b>Std. Dev.</b>	<b>Std. Error</b>
HH Income at Intake	Interviewed	610	29505.77	20446.082	827.838
	Not Interviewed	433	27310.55	22465.434	1079.620

		Levene's Test for Equality of Variances		t-test for Equality of Means				
		F	Sig.	t	df	Sig. (2-tailed)	Mean Difference	Std. Error Difference
HH Income at Intake	Equal Variances Assumed	0.002	0.962	1.640	1041	.101	2195.22	1388.944
	Equal Variances not Assumed			1.614	874.81	.107	2195.22	1360.476

With these results for 14 programs and the 100 percent response rates achieved by two other programs, it was concluded that the aggregate data on respondents from these 16 programs is representative of the entire (“attempted”) sample with respect to the business status and household income at intake. The overall response rate for the group of 17 is 60 percent.

After this examination of the representativeness of the sample, a set of calculations and estimates were made to determine costs and benefits, as are described below.

### Cost per Business Outcome

The cost per business outcome for these 17 programs was calculated and used as the basis for a comparison with other workforce development initiatives. For this analysis, a respondent was deemed to have a business outcome if they were in business at the time of the survey (conducted in first quarter of 2004). It is reasonable to assume that individuals who achieved a business outcome would be more likely to respond to the survey than those who did not start a business. However, some of this potential upward bias may be offset by the use of a conservative definition of a business outcome, as respondents who reported that they were in business in 2003, but who were no longer in business at the time of the survey were not counted as achieving a business outcome.

To estimate the total number of clients in the 17 programs who achieved business outcomes, the percent of the survey sample found to be in business at the time of the survey was applied to the total number of clients served by the programs. The 17 programs served a total of 3,740 clients in Fiscal Year 2002. In the random sample, 80 percent of the clients have businesses. Constructing a 95 percent confidence interval for the true proportion of clients who have businesses results in the following:

$$0.80 - 1.96 * \left( \sqrt{\frac{0.80 * 0.20}{813}} \right) \left( \sqrt{\frac{3740 - 813}{3740 - 1}} \right) < \theta < 0.80 + 1.96 * \left( \sqrt{\frac{0.80 * 0.20}{813}} \right) \left( \sqrt{\frac{3740 - 813}{3740 - 1}} \right)$$

Simplified this is  $0.776 < \theta < 0.824$ .

So, with a 95 percent certainty, we can state that the true proportion of clients with businesses is between 78 percent and 82 percent, that is, between 2,917 and 3,067 businesses.

Program costs were determined using total microenterprise program expenses, as reported to MicroTest. Because the average years of service received by the surveyed clients through the end of 2003 was 2.6 years, 2.6 years of program costs were added together to

represent the total value invested in producing these business outcomes. For the 17 programs, this amounted to \$22,756,429 for Fiscal Years 2000 through 2002. This figure includes not only the costs of providing all services to current business owners, but also the total costs associated with anyone who participated in program services in some way during the period, whether they started a business or not. It was assumed that services provided to those who were not in business at the time of the survey were part of the cost involved in producing the business outcomes that existed at the time of the survey.

Finally, total costs were divided by the estimated number of business owners (\$22,756,429/2,917 and \$22,756,429/3,067) for a cost per business outcome of between \$7,420 and \$7,801.

This cost per business outcome was then compared to the costs of producing job outcomes in other workforce development strategies – defined as job placements and jobs retained for at least 90 days. The costs for job placement ranged between \$4,825 and \$17,141, and between \$4,260 and \$21,697 per job retained for the set of programs on which Aspen collected data. Other studies reported cost per job figures from \$1,906 to \$50,580 with both the low and high ends referring to various tax incentive packages. These cost analyses also refer to a range of jobs with varying job quality and which were designed for individuals of varying disadvantage.<sup>272</sup>

## Comparison of Costs and Benefits

To answer the question as to whether this level of investment was justified based on the economic benefits produced, data from 10 of the microenterprise programs were analyzed. This smaller sample was used because only 10 programs were able to provide both intake and follow-up data on three key variables: business ownership, owners' draw (the amount of money a business owner reported drawing from the business in the form of salary or lump sums for personal or household uses) and employment in the business.

The same procedure outlined above was used to calculate the cost per business outcome for these 10 programs. The percent of respondents with businesses in the sample of 10 was also found to be 80 percent. Constructing a 95 percent confidence interval, as above, results in a finding that the true proportion of business outcomes among their overall client population was between 77 percent and 83 percent. For this group of 10 programs, this means that among a total of 2,779 clients, the true number of businesses is likely to be between 2,140 and 2,307. The average time of program participation for respondents in this group was 2.3 years. Total costs for the programs for 2.3 years were \$15,180,779. Dividing these total costs by the estimated number of business owners (\$15,180,779/2,140 and \$15,180,779/2,307) results in a cost per business outcome of between \$6,580 and \$7,094.

The change in owners' draw was calculated as follows. A total of 226 business owners reported their earnings both at intake and survey. The mean draw at intake was \$10,431. The total dollar value of the earnings for these 226 businesses at intake was \$2,357,406 (226 times \$10,431). At survey, the average draw was \$14,114. So the total dollar value of earnings at the time of survey was \$3,189,764 (226 times \$14,114).

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<sup>272</sup>Ida Rademacher and others, 70. Anne Inserra and others, 73. Maureen Conway and Marshall Bear, 58. Jeffery W. Thompson and others, 55. Amy K. Glasmeier and others, 58. Kirby, Hill and others, 49 (Table V.3 for costs of program services and supports) and 62 (Table VI.5 for placement rates of four programs). Servon and Doshna, 183-208. Bartik, 1992, 102-110. R. Burchell, 1997. H.B. Milward and H. Newman, 1989, 203-222. Bartik, 2001, 226-229.

In addition, at the time of survey, 87 new businesses reported an average draw of \$7,732. The total dollar value of earnings produced by these businesses, then, was \$672,684 (87 times \$7,732).

Adding the dollar value of owners' draw produced by ongoing and new businesses results in a total draw of \$3,862,448 ( $\$3,189,764 + \$672,684 = \$3,862,448$ ). This represents an increase in earnings from intake to survey of \$1,505,042. (Survey earnings less intake earnings =  $\$3,862,448 - \$2,357,406 = \$1,505,042$ .) The average increase (per business) in earnings from intake to survey was then calculated by dividing the change in total earnings by the total number of businesses that reported on owners' draw at the time of the survey, that is,  $\$1,505,042 / (226 + 87) = \$1,505,042 / 313 = \$4,808$ .

These clients also reported the number of paid full- and part-time employees at intake and at the time of the survey. At intake, 277 respondents reported that they employed 106 full-time employees and 168 part-time employees. Estimating each part-time business as half time, it was calculated that the businesses were responsible for 190 FTEs, apart from the owner. At the time of the survey, these same 277 businesses, plus an additional 114 businesses started after intake, reported that they employed 167 full-time individuals and 388 part time. Estimating each part-time business at half time, it was calculated that these clients were responsible for 361 FTEs. The increase in employment between intake and survey was calculated by subtracting 190 from 361 for 171 net jobs. Divided by 391 businesses, the net increase from intake is .44 jobs per business.

The value of the increased wages paid to these employees was then estimated using the assumption that full-time employees were paid the minimum wage and worked 40 hours per week for 50 weeks. Assuming \$10,300 in annual wages per FTE ( $\$5.15$  times 40 hours per week times 50 weeks), an increase of .44 FTEs equals \$4,532.

Thus, the total benefit per business is equal to the \$4,808 increase in owners' draw, plus the \$4,532 in increased wages paid to employees, for a total of \$9,340. With an investment of between \$6,580 and \$7,094 per business outcome by these programs, it is estimated that the initial economic return is between 1.3 and 1.4 times the investment.

In considering this return, it is important to keep several factors in mind. First, there are several economic benefits of the businesses – such as taxes paid, reduction in welfare benefits paid to the business owners, and increased circulation of money in local communities – that are not included here; valuing those benefits would presumably increase the returns above. Second, the analysis only considers benefits that accrued in the one-year period prior to the survey. It does not capture any benefit that respondents who were multiyear clients may have reported after previous years of program participation. Furthermore, as other research has shown that most of the businesses of microenterprise clients survive for several years, the return on the investment would increase as the value of future benefits is included.

On the other hand, however, because the process of collecting the outcomes data did not include a control group, the above estimate captures the gross effects of the clients' participation in these programs. It could be that some of the positive changes in owners' draw and employment would have occurred even if these businesses had not received services from the programs; thus, analysis of the net benefits of program participation would be a more accurate representation of program benefits.

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### **IN THE WORKS:**

During 2005 and 2006, FIELD will create several additional publications and products designed to build on the ideas and recommendations contained in *Opening Opportunities, Building Ownership; Fulfilling the Promise of Microenterprise in the United States*. For instance, we plan to produce a funder's guide, designed to help public and private funders identify opportunities for investment and understand how their investments can positively impact the microenterprise field.

For practitioners, plans are underway to create an on-line resource guide that will link to helpful tools and information about market research, product development, organizational restructuring, etc. In addition, a special area of the FIELD Web site will be dedicated to helping practitioners digest the eight recommendations contained in *Opening Opportunities, Building Ownership* and begin working on implementation strategies. We envision a dynamic site where practitioners will be able to post information on their own efforts, and request ideas and advice from others as they move forward.

Finally, we anticipate creating a piece for policy makers that will recommend ways microenterprise development can be used as a tool to meet economic development needs, and identify specific ways policy makers can support the microenterprise industry.

To stay abreast of these and other developments, we recommend bookmarking our Web site: [www.fieldus.org](http://www.fieldus.org).

### **PRODUCTION CREDITS:**

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“ This publication is an essential read for anyone interested in understanding the evolution of the microenterprise field and its current status. Edgcomb and Klein, two of the field’s leading voices, present an objective and most insightful analysis of the growth, impact and performance of the many organizations that support microenterprise. They also succinctly set the agenda for the future, posing a series of what some will consider are controversial challenges. I believe the future success and existence of the microenterprise field in the United States will depend on its ability to meet these challenges. We all owe a debt of gratitude to the authors for pointing us in the right direction.”

**William W. Burrus**, *President and CEO, ACCION USA*

“ This publication powerfully reminds us of the thousands of entrepreneurs who rely on the efficiency of our services and on our ability to sustain our work far into the future. Moreover, it articulates our collective charge as funders, practitioners and policy makers to realign our efforts towards the realization of economic self-sufficiency for all.”

**Sara K. Gould**, *President and CEO, Ms. Foundation for Women*

“ This timely and important report makes a compelling case for expanding microenterprise strategies for our nation’s poor, showing that – if offered the opportunity – the poor can, indeed, become part of the ‘ownership society.’ ”

**Ray Boshara**, *Director, Asset Building Program, New America Foundation*



**THE ASPEN INSTITUTE**  
ONE DUPONT CIRCLE, NW  
SUITE 700  
WASHINGTON, DC 20036

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