

## Money is Not Enough: Social Capital and Microcredit

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*“The engine of the capitalist system is supposed to be fueled by greed . . . We must envision a world which has not only greedy people, but also people with strong feelings for their fellow human beings . . . Both types of people can be in the same market place, using the same tools and concepts of capitalism but pursuing completely different goals.”*

*-- Muhammad Yunus, Founder, Grameen Bank*

The United States, with its founding principle of egalitarianism, history of rugged individualism, and fascination with self-made success, has a troubled relationship with its own poor citizens. Because of this, anti-poverty programs face difficult and often conflicting criteria in gaining social and political acceptance. One approach that has met with wide-spread acceptance is microcredit – the idea of loaning very small amounts of money to the poor in order to promote entrepreneurial endeavors. Much of the popularity of this idea rests in microcredit’s utilization of social capital by organizing borrowers into small groups. “Social capital generally refers to trust, concern for one’s associates, a willingness to live by the norms of one’s community and to punish those who do not” (Bowles and Gintis 2000, 2). Social capital is exploited through “peer-lending,” in which borrowers operate with the lender through groups, with individual borrower status dependent upon the performance of all group members. Peer-lending-based microcredit began in Bangladesh where it has been touted as widely successful. This reputation for success has led to replication throughout the developing world and, eventually, attempts in the developed world, including the United States.

Several of these U. S. attempts will be examined in detail with each program’s level of success related to its use of social capital. Causes such as “cultural, ethnic, and market differences” have been blamed for the difficulty in translating microcredit’s success story to the developed world (Auwal 1996, 9). These differences are often examined as independent factors in microcredit application but indicate, in sum, differences in the amount of social capital that borrowers can bring to the program. It will be shown that programs in the United States suffered due to a lack of social capital among borrowers. This does not wholly negate the applicability of microcredit as an anti-poverty program in the United States, but it does invalidate one of its most appealing features, that of reducing program cost by relying on borrowers to screen one another and to enforce repayment.

### I. Poverty, as the United States Views It

From Roosevelt’s “New Deal” to Johnson’s “War on Poverty” to Clinton’s “Welfare Reform,” many ideas have been explored, implemented, adapted, abandoned, and revisited in the on-going attempt to address absolute poverty and economic inequality in the United States. The idea of citizens of one of the wealthiest nations on earth living in absolute poverty has been widely deplored since Michael Harrington’s seminal 1962 work The Other America which brought the poor to mainstream, middle-class America’s consciousness. Since then, little debate has existed on *whether* poverty should be addressed but debate has continued to rage over *how* to help America’s poor. Adding to the cacophony of deliberation has been the issue of inequality. Measures of both have fluctuated throughout U. S. history and a recent change in the pattern of positive correlation between inequality and absolute poverty has caused debate whether the increasing inequality of the 1993-2000 boom years is even a problem in light of the decrease of those living in absolute poverty from 15.1% to 11.3% during the same time period (U. S. Census Bureau 2003). Due to recession, these figures have since changed and again show a shift in correlation. The most recent U. S. Census Bureau figures show official measures of poverty increasing: the number of people living in poverty rose to 11.7% in 2001 and 12.1% in 2002. This occurred while several Census Bureau measures of income inequality either did not change or decreased. It may not be possible, without the benefit of significant hindsight, to determine if “rising inequality and falling poverty could well be an enduring feature of the New Economy” (Mandel 2002, 90). Regardless of

their connection, the attention and dispute devoted to both issues assures that methods for addressing them will continue to be much-debated.

The questions raised by these two issues lie at the heart of U. S. values. Founded on the idea that “all men are created equal,” U. S. citizens prefer to view economic inequality as a result of personal talent and effort, or lack thereof (Draut 2002, 6). This view of the poor as responsible for their own economic condition is contradicted by another well-known American axiom: “It takes money to make money.” The necessity of investment implied by this truism also illustrates two other features of American economic philosophy: capitalism and entrepreneurship. “Seed money,” the money required to begin a new capitalist enterprise, also called “capital,” “assets,” or “wealth” is generally agreed to be even *more* unequally distributed than income. In 1998, “88% of all stocks were held by the top third of households in terms of income” (Wolff 2001, 4). Thus the problems of inequality and poverty become mutually causative.

If the poor are defined by their lack of income and remain such through their lack of wealth, then two avenues for addressing poverty are presented: income transfers and asset redistribution. Income transfers are now a feature of the American economy, although the Welfare Reform Act of 1996 has addressed growing societal concern that simply providing the poor with monthly cash creates a cycle of dependency, undermining work incentive and corrupting the values of the poor. This opposition to income transfer has increased the possibility, and necessity, of asset redistribution. Simply seizing and “fairly” disbursing assets would never be tolerated in the United States and was shown to be ineffective in Eastern Europe and the former Soviet Union. It is also not sufficiently philosophically different from income transfers – an unearned gain is an unearned gain, despite its form.

Additionally, top-down federal approaches are also viewed suspiciously, leading to current support of community-based efforts. While 86% of Americans believe “...the government has a responsibility to do away with poverty in this country,” 49% of them also believe the government could not do so, *even if spending were no object* (Draut 2002, 7; emphasis added). A 1998 Gallop Poll showed Americans evenly split on governmental and non-governmental responses to inequality. Those less concerned with inequality strongly favored the private approach, indicating a greater interest in shrinking government than addressing societal disparity (Bowles & Gintis 2000, 17)

The strong and sometimes contradictory American values of assisting the poor, but only temporarily; of opposition to the dependence inherent in income transfers; of suspicion of large federal programs and preference for community-based ones; and an almost mythical admiration of the ability to “pull one’s self up by the bootstraps” through capitalistic entrepreneurship explain the political and societal popularity of redistributing assets through peer-lending-based microcredit. Often described as “a revolution,” microcredit has been touted as a program which “...reverses the conventional thinking about human rights, development, and capitalism” (Auwal 1996, 5). These ideas are indeed revolutionary but microcredit, despite reports of phenomenal successes in the developing world, has not proved to be the panacea for the twin U. S. economic ills of poverty and inequality that some had hoped it might be.

## II. Origin and Methods of Microcredit

Microcredit began in Bangladesh as the brainchild of economist Muhammad Yunus. After receiving his Ph.D. from Vanderbilt, this Fulbright scholar returned to his homeland to teach at Chittagong University (Yunus, *Banker to the Poor* 1999, 18-19). He was frustrated that the theories he was teaching did not seem to affect the lives of the people around him, who were still suffering greatly after the 1974 famine. Yunus could have remained within the walls of this isolated university, but he chose instead to explore the community around him in order to understand, firsthand, the lives of the poor. In his 17 July 1997 article “Grameen Bank Story,” published in *Dollars & Sense*, he tells of the experience that led him to pioneer microcredit:

I met a woman, Sophia, who made bamboo stools. She was extremely poor, and no wonder. She made only two cents a day making bamboo stools. Why so little? Because she did not have

the working capital to buy bamboo from the market for 20 cents. A trader lent her the money to buy the bamboo under the condition that she sell her stools to him at the price he decides. Now you can guess why she was extremely poor. (Yunus "Grameen Bank Story" 1997, 1)

Yunus began to loan out his own money, simply addressing the need without any thoughts for future expansion. As the article states, Yunus eventually realized that the real answer lay in on-going loans from commercial banks. It was then that he discovered why the poor had not attempted this themselves. Without collateral, they could not borrow. Also, most banks required that the borrowers be able to process paperwork. In a country with 75% illiteracy, this struck Yunus as a prohibitive requirement. The poor were considered too risky for loans and banks considered themselves a for-profit business, not a social service organization. Undaunted, Yunus co-signed commercial loans for the poor and began expanding his idea (Yunus, *Banker to the Poor* 1999, 52-54).

Yunus was convinced that small-scale self-employment was superior to large projects focused on creating wage employment. He saw independent self-employment as more family-friendly and, therefore, more likely to meet the needs of Bangladesh's poorest group, women. "People who experience the most cruel manifestations of poverty are the women from poor households" (Yunus, "First Decade" 1994, 31). Women with children can work from their homes, making self-employment more feasible than wage employment. He also saw women as potentially better credit risks because "They more desperately want a secure future for their children, their families and themselves" (Yunus, "First Decade" 1994, 31). Because women are bound by their children, "...no poor man is able to match the fervor of the poor woman in seizing the slightest opportunity to fight poverty" (Yunus, "First Decade" 1994, 31). Armed with these insights, Yunus began to develop an anti-poverty program that catered to women and revolved around readily available credit for entrepreneurial projects. After several years of informal experiments, Yunus realized that the lack of physical collateral among the poor could be successfully replaced by social capital and began operating the Grameen Bank in 1976 as a peer-lending institution (Grameen Foundation 2003).

The Grameen Bank ("Rural Bank" in Bangla) is a for-profit commercial bank which utilizes the idea of social capital by exclusively serving borrowers who join in self-organized, non-family groups of five which provide "peer pressure and peer support" for the process. After brief training in which potential borrowers come to understand the methods of the bank, a group is "recognized" and two members are issued small loans. (Yunus, "As I See It" 1994, 64-65). As the initial loans are successfully repaid, the number of members who may borrow and the amount of the loans increases. Loan default by a single group member makes the entire group ineligible to borrow subsequent funds and the small initial loan amounts make subsequent borrowing imperative. This creates strong incentive among group members to assure the others' business success and loyal repayment (Skousen 1999, 1). Thus poor people may bind together on a community basis and become self-regulating as well as self-sufficient, lessening the need for extensive borrower oversight and promoting shared knowledge that leads to entrepreneurial success. This decreases the cost of implementing a microlending program by shifting client screening and monitoring to the borrowers themselves.

### III. Appeal of Microcredit

This low-cost social capital approach led to rapid spread of the Grameen Bank in and outside of Bangladesh and to reports of incredible success, with repayment rates usually cited at almost 99% (Auwal 1996, 2). Yunus' 1987 visit to the U.S. captured media attention, culminating in a 1990 *Sixty Minutes* segment that continues to garner excitement (Yunus, *Banker to the Poor* 1999, 149). The numbers were seen as providing proof that the poor are "bankable" and that self-employment through microcredit was a viable method for addressing poverty, inequality, and development. Because the program had by then been successfully "replicated" in Malaysia, Indonesia, the Philippines, India, Nepal, and Vietnam, few at that time believed that its success was exclusively a result of specific cultural or economic aspects of Bangladesh or of the direct involvement of the charismatic Yunus (Getubig 2000, 1). The idea had also received the approval of the World

Bank, whose private-sector International Finance Corporation created The Foundation for International Community Assistance in 1984 to "...offer small loans and a savings program to those turned down by traditional banks, believing that even the poor have a right to financial services" (FINCA 2003). An anti-poverty program that was low-cost and self-sustaining through profit, which empowered the poor rather than fostering dependency, which relied on communitarian ideals of social collateral within the larger context of capitalism while promoting individualistic entrepreneurship was a possibility that captured the attention and devotion of many, in part due to the "...special charm in the idea that a rich country could learn something valuable about making wealth from a poor one..." (Taub 2003, 2). The spread of microcredit in the U. S. can be attributed to these basic attractions and to broad political support:

Grameen is a political chameleon: it has the ability to affirm beliefs that both conservatives and liberals hold dear. From the right Grameen can be seen as an entrepreneurial institution that makes the case for less government; from the left it appears to be an enlightened social-welfare program that argues for the value of government involvement. Some see Grameen as an example of reinvented government. Muhammad Yunus disagrees. He sees his bank as an example of reinvented capitalism. In fact, he calls it a 'socially conscious capitalist enterprise' (Bornstein, "Barefoot Bank" 1995, 45).

By 1994, microcredit organizations based on the Grameen social capital model numbered more than two dozen in the United States (Counts 1996, xviii). Although non-profit status is the norm in the United States, most groups hoped to attain self-sufficiency. According to their website, "Grameen Foundation USA was established in 1997 to provide financing, technical assistance and technology support to the growing numbers of grassroots institutions that are successfully replicating Grameen Bank's success..." The site lists 49 "programs that replicate the Grameen Bank approach" (Grameen Foundation 2003). Estimates made in 2002 put U. S. microcredit organizations at some 400 but it is difficult to know how many are using the peer-lending model (Bhatt and Tang 2002, 360). Despite this, there is no doubt that the social capital *model* of this appealing "socially conscious capitalist enterprise" is replicated in the United States but are branches replicating, as Grameen Foundation USA claims, its *success*?

#### IV. Success in Bangladesh

Determining the success of a microcredit credit program can be difficult. Different measures are used to quantify even obvious criteria, such as default rates and improvement of borrower living standards; these are further complicated by cross-country comparisons. Other criteria are even more ambiguous. Is borrower success determined by staying with the program or moving beyond it? Do small loans, indicating outreach, or large loans, indicating established borrowers, suggest a successful program? Should a program be judged by its growth, the clientele to whom it caters, or its dependency on financial subsidy or governmental support? Even answering the questions that are determined to be relevant is difficult. Most programs are reluctant to produce hard empirical evidence, partially because it is costly to do so and partially because it may counter the exciting and easily-cited anecdotal evidence (Morduch 1999, 1572).

The anecdotal evidence of the much-studied peer-lending model of the Grameen Bank does indicate that success came about through long-term trial and error in a socially and politically favorable climate (Morduch 1999, 1572). Group size and structure, loan schedules, organizational structure, and borrower profiles all developed gradually as Yunus was able to observe success and respond to failure (Yunus, *Banker to the Poor* 1999, 62-67). Yunus was also able to rely upon the results of a previous, similar experiment. Bangladesh had a history of government-sponsored credit cooperatives; the mistakes of which Yunus studiously avoided, most notably internal corruption (Bornstein, "Barefoot Bank" 1995, 44).

Yunus himself credits the social capital model with the Grameen Bank's success. In a section of his writing "Grameen Bank: As I See It" titled "What is Behind GB's Success?" Yunus observes:

The process of group formation itself contributes to the strength of GB. Usually it takes quite a bit of time for the members to identify each other and consult each other before they make an announcement that they wish to form a group. Many times members screen each other out before they arrive at the final five. Some drop out because of fear instilled in them by relatives and neighbors. Before negotiation with the bank even begins, the members have already gone through a process of understanding and mutual confidence-building (Yunus 1994, 65).

Social capital is not the only source of success, however. The Bank evolved in a culture where abject poverty and self-employment were both prevalent and connected, leading to readily available human capital in the form of entrepreneurial spirit. The level of desperation in Bangladesh, where many live in brutal poverty and starvation is common, offers powerful incentive to make the most of opportunity. "This is the life story of many a landless person" Yunus notes. "He is left only with his two hands. With those he does tidbits of odd jobs. He does something whenever he has an opportunity" (Yunus, "First Decade" 1994, 32). Opportunities found in widespread, if piece-meal, self-employment meant that borrowers were not as frequently "starting" new businesses as they were liberating their existing work from usurious money lenders or freeing themselves from exploitative contractors (Bornstein, *Price of a Dream* 1996, 17; Yunus, *Banker to the Poor* 1999, 49).

Grameen also benefited from heavy government support of Yunus' efforts. Although support was not immediate or easily obtained, Yunus was allowed to experiment for two years as a branch of the governmentally-backed Krishi Bank ("Agricultural Bank" in Bangla), a similar program exclusively targeting small farmers who, by virtue of their land holdings, are not Bangladesh's most impoverished. Following success in the experimental stage, Grameen officially opened as a government-owned bank backed by the Central Bank (Yunus, *Banker to the Poor* 1999, 90-96). Although now depositor-owned, Grameen continues to rely heavily on the Bangladesh Central Bank for subsidized loans and program expansion (Yunus, *Banker to the Poor* 1999, 120-28).

Grameen workers also contribute greatly to the success of the program. They are highly educated; a branch manager must have a Master's degree, a respected rarity in Bangladesh made more impressive by the managers' willingness to work in rural conditions (Yunus, "As I See It" 1994, 68). They are also devoted to the ideals of the bank and their role in it as "an elite brigade of poverty fighters" (Yunus, *Banker to the Poor* 1999, 101). They are trained to be "teachers," a much-respected profession in Bangladesh, helping the poor to recognize their own potential. This is an opportunity "...perfectly in tune with their inherent sense of social responsibility." Field workers below the management level are often attracted to the Bank because of the working environment, despite its difficulty (Yunus, "As I See It" 1994, 72-73). Jobs in Bangladesh are rare and Grameen offers something even more rare – an organization where corruption and bribery are frowned upon. "Here," one worker states, "you can be an honest person and it's possible to remain so" (Bornstein, *Price of a Dream* 1996, 167). This appeal leads to a very selective hiring process. Yunus estimates that only 1 in 10 applicants are hired, resulting in workers who are "...very cautious, eager to do a good job, and genuinely want to help the poor people" (Yunus, "As I See It" 1994, 74).

The honesty of the workers may impress local borrowers but the final question about the Grameen Bank's almost "too good to be true" success figures must be: Are they real? The Grameen Bank's often-touted 98 – 99% repayment rate is partially the result of non-standard, though transparent, accounting methods. Grameen calculates the value of overdue loans by dividing one-year-old amounts in arrears by the current portfolio. Because their portfolio has expanded so rapidly, it is much greater than the one that existed when these same loans first became "at risk." Correcting the denominator to the one-year-old portfolio, as done in standard banking practices, produces an average default rate of 7.8%, a figure still impressive for a development bank but not for a commercial bank. Additionally, grants from donors are counted as income. If income were defined strictly as resulting from interest and investments, as with regular commercial banks, Grameen Bank's 1985-1996 "profit" of \$1.5 million becomes a \$34 million dollar loss (Morduch 1999, 1590-91). This is without factoring in the main source of subsidy for Grameen: their ability to borrow at below-market rates from supportive governmental and non-governmental organizations. The International Monetary Fund has

approximated that “An additional implicit subsidy of \$47.3 million was received by Grameen through access to equity which was used to generate returns below opportunity costs” (Morduch 1999, 1591). The two sources of subsidy together, donations and soft loans, contributed \$81.3 million in black ink to Grameen Bank’s ledger sheet from 1985 to 1996.

These numbers and the social and political climate described above indicate the reality regarding the success of the Grameen Bank. The success was not immediate nor were structures for success immediately discovered by its founder. Social capital is an important contributing factor but it is present along with other social conditions. Bangladesh provided the Grameen Bank with desperate, entrepreneurial borrowers who were familiar with operating on credit under conditions far less favorable to themselves. The same culture also provided Grameen with workers devoted to pursuing the ideals of the Bank. Governmental support allowed for a slow trial-and-error approach and continues, along with non-governmental organizations and private donors, to be a strong financial component of the Grameen Bank. These conditions are not unique to Grameen, however; many other anti-poverty programs also rely upon the will of the recipients to succeed, the dedication of the program workers, and outside support. The presence of these conditions does not automatically reclassify Grameen as a “failure.” It may, however, indicate circumstances necessary for the type of success Grameen does enjoy. The fundamental question is therefore presented: Do these conditions, or sufficiently similar ones, exist in the U. S.?

## V. An Urban U.S. Replication

One of the earliest and most noted Grameen replications is the Chicago-based Women’s Self-Employment Project (WSEP) and its peer-lending program, the Full Circle Fund, which grew out of the South Shore Bank. South Shore was one of few commercial banks left in inner-cities in the 1980s. It had been purchased in the early 1970s by idealists determined to show that banks could succeed in poor neighborhoods. They had achieved this goal but were still puzzled by requests for very small commercial loans, not usually considered viable ventures. A founder of South Shore, Mary Houghton, visited Bangladesh in the early 1980s and returned with Yunus’ blessing to create the Women’s Self-Employment Project, designed as a non-profit, but otherwise based on the Grameen peer-lending model, including, as the name indicates, its focus on female borrowers (Counts 1996, xvi-xvii).

Replicating the “Rural Bank” in predominately black inner-city Chicago was not a one-to-one proposition. Grameen workers often had to overcome initial skepticism but in the United States program workers coped with mistrust born of racism – a situation unmet in homogenous Bangladesh. Prospective borrowers feared a scam and were suspicious of white Full Circle Fund employees (Counts 1996, xvii). Racism also meant that the poor to whom WSEP wished to cater faced disenfranchisement greater than that of poverty alone. Unlike in Bangladesh, few had any previous entrepreneurial experience. This meant that training programs were longer and more involved. Grameen simply introduced eager prospective borrowers to the way the Bank operated. WSEP had to convince community members of the possibility of success and offer training classes in accounting, marketing, and formulating and managing business plans (WSEP 2003).

Because of these hurdles, groups had to be formed within the program; there was simply not enough interest for borrowers to arrive in pre-arranged, self-selected groups of five (Counts 1996, 102). Although the *idea* of peer-lending remained it is difficult to consider groups formed during entrepreneurial training classes at the program and those consisting of previously-acquainted friends and neighbors as having the same social implications. Participants do share knowledge and ideas, and responsibility for each other’s repayments, but the strong pre-screening aspects of independently-formed groups, a key benefit for the Grameen Bank, are lost.

The aspect of Full Circle Fund that was most similar to the Grameen Bank, as Alex Counts illustrates throughout his book *Give Us Credit*, is the market place in which many of the Englewood, Chicago borrowers operated their businesses. The Maxwell Street Market in that neighborhood was an open-air collection of stalls, tables, and car trunks where goods “new, used, and very used” could be sold for almost negligible overhead. This opportunity for small-scale, low-investment marketing is “strongly reminiscent of Bangladesh” (Counts

1996, 121-22). In fact, Counts' book becomes the tale of attempts to save the Market from the encroaching University of Illinois.

The Market also illustrates another key difference in the U. S. and Bangladesh programs – government support. Although the neighborhood aspect of the Market meant it was a place where program members could take advantage of minority purchasing power, the city, hoping to profit from gentrification efforts, "...described the bazaar as dangerous and as a venue for criminals to sell stolen goods" (Counts 1996, 193-94). Roosevelt University (Chicago) economics professor Steven Balkin, the author of *Self-Employment for Low-Income People* and a Market advocate, is quoted by Bornstein regarding the policy contradictions facing the poor who comprise market dealers:

Governments like to spend money on expensive classroom-based self-employment training, yet at the same time they're squashing these markets. Street markets offer a low-cost way to start a business, interact with other vendors and customers, and build up trust in a community. And once you have trust, information flows, money flows, and deals can be made (Bornstein 1996, 336).

Although not explicitly stating it, Balkin was concerned not only with government defeat of entrepreneurial efforts but also with its direct attack on the community's source of social capital.

The eventual dismantling of the Market had serious repercussions for founding WSEP borrowers. By the end of the tale, the group followed in Counts' book was ineligible to borrow due to a default and none could be found among the member businesses currently listed on the WSEP website. The site does not offer program repayment statistics nor could any be located in current literature. At the time of publication, 1996, Counts noted that WSEP, because of recruitment and training requirements, was significantly more expensive to operate than Grameen. Administrative costs exceeded loan amounts and loan portfolio interest covered a fraction of institutional expenses (Counts 1996, 332). A default rate of 4.8% was "neither embarrassing nor overwhelming" and Counts is quick to note that the program was in its infancy at the time and Grameen also required time to develop a successful structure (Counts 1996, 335).

## VI. A Rural U.S. Replication

Could a successful structure that directly replicated the Grameen model be produced elsewhere in the U. S.? After all, it is the "Rural Bank;" perhaps Chicago is not the place for developed-world microcredit. The Arkadelphia, Arkansas-based Good Faith Fund was initiated by then-governor Clinton in 1988 to alleviate individual poverty and promote economic development. It is an example of a program which has, ultimately, replicated only one of Grameen Bank's ideas successfully – that of innovative adaptation.

Good Faith Fund was founded after a visit to Arkansas by Yunus and originally followed his model (Yunus, *Banker to the Poor* 1999, 177). Some of the suspicion of "outsiders" experienced by white workers in Chicago was also experienced by white workers in black rural Arkansas and was compounded by the fact that many of the early employees did not have rural backgrounds. The idea of credit at market interest rates as a "favor" to the poor also created suspicion. Misunderstanding increased when prospective borrowers discovered that a good idea was insufficient and that they were expected to produce business plans and financial prospectuses (Taub 2003, 5).

Arriving at the program door with four friends eager, and ready, to begin businesses was as problematic for Arkansas potential borrowers as it had been for those in Chicago. Again, groups had to be formed by program managers. These groups were even less cohesive than the ones at WSEP, where members did seem to encounter one another in the neighborhood and build a certain level of social capital through program participation. Program employees cited "groups falling apart" as one of their biggest problems (Taub 2003, 7). Group members reported that meetings were not a priority among their many responsibilities and expressed reluctance to tie their fortunes to those of strangers. One can imagine that transportation issues and the lack of

contact outside the program contributed to group members remaining “strangers.” Because of this complete absence of social capital, group responsibilities were not sufficient to prevent default, either, which reached rates as high as 48%. Background checks and physical collateral came to be required of borrowers. After these changes, defaults rates dramatically reduced to an average of 11%, annually (Taub 2003, 5). Eventually, the program was restructured so that group repayment rates no longer affected individual ability to borrow (Taub 2003, 7). Group pressure was simply not an effective repayment motivation in Arkansas and the only remaining aspects of group membership are moral support and “commonsense technical assistance” (Taub 2003, 7).

This need for assistance became a feature of U. S. programs not found in Bangladesh. The Good Faith Fund’s original hope of self-sufficiency was motivation to keep program costs low by limiting services but it soon became apparent that loans for enterprise start-up to those with no business experience would not produce a self-sufficient program, either. Borrowers must now complete a six week small business training program (Taub 2003, 5).

Training borrowers was not as much of a problem as simply recruiting them, a result of the very different demographics of rural Bangladesh and rural Arkansas. The most densely populated county served by the Good Faith Fund has 45 people per square mile; the least densely populated has 10. Bangladesh has more than 2100 people per square mile (Auwal 1996, 9). This has implications not just for availability of potential borrowers and their ability to exert group pressure on one another, it means there are few potential local buyers of any goods or services entrepreneurs may wish to offer. Because the small-scale operations that microcredit can effectively fund must be limited to local markets, Arkansas entrepreneurs were most successful when offering services (Taub 2003, 8). Although this improved the lives of the borrowers and their families, it does “... not generate new money or provide additional employment opportunities...” (Taub 2003, 8). Because of this, the Good Faith Fund’s goals of economic development were not achieved by its microlending arm. Although the microlending function remains on a very small scale, the program has largely been reorganized to provide large loans to existing companies in order to create wage employment, not self-employment (Taub 2003, 7).

A key problem in promoting self-employment for the poor in the U. S. is the very different reality of poverty in the developed world and in Bangladesh. Arkansas’ poverty rate was actually above the national average of 13% when the Good Faith Fund was implemented (U. S. Census Bureau 2003). The relative poverty of the 10% of Arkansans living below the official government poverty line is nothing like the abject poverty of much of the Bangladesh population, where miniscule amounts of money can be the difference in life and death by starvation. This is illustrated by the increase in immigrant labor in Arkansas to perform work that natives are no longer willing to do, such as poultry processing. If Arkansans are unwilling to take guaranteed wage work if it is unpleasant enough, why would they embrace the difficult and risky work of entrepreneurship? The amount of effort required to show some improvement in lifestyle in Arkansas is much greater than that required in Bangladesh (Taub 2003, 10). This provides disincentive for accepting business start-up loans and for repaying them, as well.

These disincentives are compounded by the social safety net in the U. S. The truly poor in U. S. have been surviving through welfare, an option not available in Bangladesh. Risking benefits for the unsure future of a small start-up business can be too great a deterrent. Because welfare benefits often include childcare and health care plans, the poorest are wise *not* to embrace microlending-supported entrepreneurship (Graham and Manning 2000, 30). Indeed, the Arkansas program was most often utilized by families that could afford some small risk, noticeably, those which had “...at least one moderately secure income” (Taub 2003, 11). By definition, the very poorest in the U. S. cannot risk indebtedness to microlenders. “Welfare Reform” has greatly altered this situation since these programs were implemented and its final impact on microcredit is as yet undetermined. The focus of welfare reform, however, has been on job training, not entrepreneurship.

## VII. Replication on the Pine Ridge Indian Reservation

This inability to target the truly impoverished was illustrated by another early U. S. attempt to replicate the Grameen model, that of the Circle Banking Project on the Pine Ridge Indian Reservation in southwestern South Dakota. Members of the Fund were deeply concerned about losing public assistance, which almost 50% of reservation households receive (Pickering and Mushinski 2001, 461). The program there also supported mostly supplemental endeavors, not full-scale businesses. High mobility, fostered by the lack of local wage work opportunities and the extreme isolation of the reservation, also contributed to the supplemental nature of the program.

This mobility had negative impact on group cohesion, as well, but was not the only problem in adapting the peer-lending aspect of the program (Pickering and Mushinski 2001, 464). Lakota concepts of family and their great mistrust of outsiders, even non-family members of the reservation, made adhering to the Grameen rule of non-family groups impossible. The Lakota expressed desire to work with members of extended family and this was eventually accepted with hope that family ties would provide strong incentive for repayment (Pickering and Mushinski 2001, 463). These societal views of any non-relatives as “outsiders” and “...intense negative feelings associated with admitting shortcomings in public...” meant that group members would *avoid* meetings if they were experiencing business or repayment problems (Pickering and Mushinski 2001, 463). Groups could not pressure absent members and the support aspect was lost completely. It was finally determined “...that the peer pressure among non-family members in Pine Ridge was actually too strong to make Circle Banking work” (Pickering and Mushinski 2001, 463). This profound difference in the understanding of what constitutes relevant community led to the formal termination of the program in 1998, just 10 years after it was implemented (Pickering and Mushinski 2001, 460). Pine Ridge is illustrative of the deepest misunderstanding of what social capital is and what it can do.

## VIII. “Social Capital and Community Governance”

Bowles and Gintis’ 2000 paper on “Social Capital and Community Governance” explores the governing power of social capital. “Community” they write, “better captures the aspects of good governance that explain social capital’s popularity, as it focuses attention on what groups *do* rather than what people *own*. By community we mean a group of people who interact directly, frequently and in multi-faceted ways” (Bowles and Gintis 2000, 3; original emphasis). This type of community was created by the Women’s Self-Employment Project through lending group membership, neighborhood proximity, and the activism efforts to preserve the Maxwell Street Market. Default rates were relatively low and usually caused by outside forces above and beyond simple “giving up” on behalf of the members. Lack of proximity or any interactions unrelated to the lending process kept community from developing among the “strangers” who were borrowers in the Good Faith Fund. Borrowers not only expressed reluctance to be responsible for others’ behavior, they were distressed at the idea of having to rely on another for their own needs (Taub 2003, 7). The peer-lending model was never truly effective there and was abandoned in favor of background checks and collateral. The definition of local community was misunderstood by Circle Banking program implementers. The Grameen model prohibits family members to form groups because of fear of collusion against the bank. The residents at Pine Ridge, however, could not think of non-family members as community. When this was finally accepted by the program, another issue arose. Bowles and Gintis find that community governance is strongest in neighborhoods with high levels of stability – usually indicated by home ownership and duration of residence (Bowles and Gintis 2000, 4). The Pine Ridge Reservation is characterized by instability as residents leave for wage work opportunities elsewhere (Pickering and Mushinski 2001, 464). Even without this alternative definition of community and high level of transience, Pine Ridge was doomed as a peer-lending attempt. The support and pressure concepts were something the Lakota simply would not share outside of family circles. This meant that, despite meeting the definitions of community through their multi-faceted interactions, the members were not privy to information about others that may have enabled them to determine a fellow group member’s willingness or ability to successfully engage in entrepreneurship or repay loans. Bowles and Gintis maintain

that the governing powers of social capital rest in the fact that "... [community] members, but not outsiders, have crucial information about other members' behaviors, capacities, and needs" (Bowles and Gintis 2000, 5).

Additionally, members of well-governing communities "...should own the fruits of their success or failure in solving the collective problems they face" (Bowles and Gintis 2000, 16). The failures of peer-lending group members are "owned" by all members in the form of losing credit eligibility but there is little scope for shared ownership of success. Beyond some shared knowledge of successfully implemented ideas and maintenance of current borrowing status, peer-lending group members do not seem to substantially benefit from one another's success. Perhaps the threat of collective punishment without the promise of collective reward is insufficient to promote community governance in the individualistic United States. Bowles and Gintis also find that economic inequality among group members hinders community governance. What does this mean for a single highly successful – or single exceedingly struggling – individual in an otherwise average group? Would some form of shared success be necessary to prevent the economic inequalities that microcredit is attempting to address from interfering with its basic premise?

## **IX. Was it Human Capital All Along?**

If social capital has been tenuous, absent, ineffective, or too strong to work in U. S. peer-lending microcredit programs, what has determined repayment? In a non-random sample of microcredit programs with detailed information, Bhatt and Tang found that, in the U. S., higher levels of education led to increased repayment rates (Bhatt and Tang 2002, 363). Education is indicative of human capital – the skills and knowledge of the workforce. Interestingly, physical proximity to the lending institution also increased rates of repayment. Bhatt and Tang speculate that this may be the result of reduced transaction costs for the microentrepreneur or of more effective oversight by the lending program. If it is the later, then peer groups are not as effective as the lending agency itself in monitoring borrowers. Supporting this speculation is the responses made by borrowers when asked "What do you think would happen if you did not repay the loan? ... *None* of the respondents ... mentioned public embarrassment as a cost of default..." (Bhatt and Tang 2002, 370; original emphasis). Further undermining the theory of social capital was the finding that group homogeneity, a substitute for shared norms, did not increase repayment rates. This suggests that "Where 'civicness' is present, it tends to persist; where it is not, it cannot be easily created" (Bhatt and Tang 2002, 370-71).

## **X. Conclusion – What Future for U. S. Microcredit?**

An "easily-created" program was the promise of microcredit. Social capital was believed to exist and would be effortlessly implemented in the United States as it had been in Bangladesh. Program costs would be low because borrowers themselves would perform screening and monitoring functions and because training would be unnecessary. This has been shown to be a false hope. Group members who are not previously associated do not have social capital to bring to the program and programs have not been able to readily create it. Peer monitoring does not seem to be a determinant of repayment. Education, the expensive investment in human capital that microcredit was supposed to circumvent, has proved necessary, at least in some amount. The peer-lending model of the Grameen Bank, *in and of itself*, is simply not sufficient to ensure a microcredit program's success.

The possibilities for implementing microcredit as an instrument against poverty and inequality in the United States are limited but not nonexistent. Access to credit in support of small-scale entrepreneurship may help some individuals to enjoy increased standards of living but will not produce results as a development plan. Neither will it help the most severely destitute who cannot risk the uncertainty of self-employment if it means losing health- and child-care benefits received through government assistance programs or forgoing the certainty of wage employment, however low those wages may be. Because of this, microcredit will be most effective when utilized by those already involved in entrepreneurial activities, rather than as a means of coaxing the uninitiated into self-employment.

The low-cost promise of a “for profit” anti-poverty program has been broken altogether. Even Grameen Bank, which still boasts of profits, is heavily dependent on grants and subsidies. Programs in the U. S., which are more expensive to implement due to the necessity of training functions, have no hope of attaining self-sufficiency through interest returns and loan portfolios. Microcredit must be subsidized by either the private or public sector. Because of the unrealistic, yet appealing, promises of microcredit, subsidy has been easily attained thus far. It remains to be seen if the limited beneficial effects of microcredit, in light of broken promises, will continue to garner support.

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