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Extension Demonstration: Grameen Microfinance Methods and Capital Access for Low-Income Female Entrepreneurs

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Abstract

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Keywords

cultural diversity, poverty reduction, financial management education, entrepreneurship, microfinance

Disciplines

Economics | Entrepreneurial and Small Business Operations | Inequality and Stratification

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Strategies for reducing income equality have been raised as discussion topics in recent presidential campaigns. While income guarantees may be efficient for income redistribution, redistribution alone or financial training alone does not assure opportunity for practice of financial management best practices by diverse low-income populations when institutional, market, or cultural barriers exist. Furthermore, payday loans with predatory terms may quickly negate the gains from financial training, hard work, and savings for emergencies. Yet, access to basic training, small loans for practice, savings for emergencies, and regular meetings with peers and coaches coupled with appropriate group and individual incentives provide an important theoretical pathway for improved finances as well as personal, family, and community development.

Review of Literature

Community “Free Spaces” are often regarded as a necessary condition for successful Extension education programs on personal and public policy topics that are sensitive for culturally diverse populations. Extension designs programs to build leadership skills and public policy education capacity for solving local problems. A critical success factor in working with culturally diverse target populations is the identification of “free spaces.” A free space occurs in a setting for which people can meet to talk publically and actively contribute to solving public problems. It's characterized by several major components: a sense of shared bonds, a comfortable physical, social, and cultural setting, a social network, engaging discussion, a participatory environment, and potential for forming new networks and shared vision. One might add a politically neutral, non-threatening and safe place without those who are predisposed to cause harm or report individuals to others who may cause harm. If a free space exists, participants can learn group identity, self-respect, public skills, and the value of cooperation (King & Hustedde, 1993).

Historically, the black community often viewed their churches as free spaces. Church leaders organized the civil rights movement. Churches played an impactful role in developing a sense of aspiration and public skills for members and the larger black community. During the early 20th century, women gathered in homes because that was one of the few female free spaces where they could discuss civic vision and action. These physical free spaces often used interactive learning techniques and room arrangements to facilitate group bonding, debate, and empowerment (King & Hustedde, 1993).

Extension in some states during the 1940s, 50s, and 60 facilitated Extension Homemaker Units that provided “free space” with similar attributes: meeting in homes, social network development, discussion of relevant topics related to personal development, family living, and community issues. Unit members met

monthly for a one to two hour meeting that included educational demonstrations, and seminars and social discussions on food preparation, nutrition, family health, child development, gardening and other relevant topics. Impacts of the homemaker units were measured as part of a 1964 study of Extension's impacts in Jefferson County, Kansas. The study authors compared the institutional mechanism results to previous data and observed that the social networks created by homemaker units often developed bonds that lasted for decades with similar age cohorts. However, participation declined as younger women entered the workforce (Ragle, Baker, and Johnson, 1967).

Peer-group lending methods were developed by Professor Muhammad Yunus in Bangladesh beginning in 1976. Yunus was an economist who observed Bangladeshi women in extreme poverty making handmade items to increase incomes--but failing in their efforts. Bangladesh was one of the world's most poverty stricken nations in the late 1970s and early 1980s following a 1974 famine in which 26,000 people died due to starvation. Yunus observed that groups of entrepreneurial women were financing and buying inputs and selling outputs to the same entities that were using confiscatory pricing terms. With his own funds, Yunus began to experiment in loan-making in the homes of poor women who knew each other, had income generating activities, and expressed common goals in seeking a better life for themselves and their families. Loans were made without requiring collateral. Working with the groups of poor women, Yunus identified several "de facto" policy barriers and worked with the women to overcome several hurdles presented by religious, community, and cultural institutions. The Grameen Bank was founded in 1983 following initial peer-group lending methodological successes and the pervasive Bangladeshi need for poverty reduction strategies and economic development (Yunus, 1999).

Since 1983, Grameen peer-group microfinance methods have been adopted by affiliates in more than 64 low-income countries worldwide. For his efforts in development and deployment of Grameen methods globally, Yunus received the World Food Prize in 1994, Nobel Peace Prize in 2006, U.S. Congressional Gold Medal in 2010, and many other honors. In 2008, Grameen America was formed as an affiliate to organize microfinance projects in the United States. Initially, U.S. projects were organized in eight large metro areas with local multi-million dollar donors for each project. As of 2019, Grameen America reported 14 large U.S. metropolitan communities had disbursed over \$1.24 billion in loans to over 120,000 low-income women (Grameen America, 2019). While similar concepts such as lending circles mimic Grameen methods, none have reported 98% loan repayment rates or the scale reported by Grameen affiliates.

Domestic access barriers to conventional loans and savings are wide ranging for low-income populations. A 2017 survey of 35,000 households by FDIC and U.S. Census Bureau found that 6.5 percent of households in the United States were *unbanked* (FDIC, 2018). This proportion represents approximately 8.4 million households did not have an account at an insured institution. An additional 18.7

percent of U.S. households (24.2 million) were *underbanked*, meaning the household had a checking or savings account but obtained other financial products or services outside the banking system during the previous 12 months.

Low-income entrepreneurs have difficulty in accessing loans from conventional financial institutions due in part to loan underwriting standards. Conventional lenders typically require (a) a written business plan with financial statements and positive cash flow projections, (b) an acceptable credit history, and (c) collateral and/or loan guarantors with net worth. Entrepreneurs who are part of new resident populations are often unable to provide one or more of the underwriting requirements when they want to start a business enterprise. New resident entrepreneurs may also face language barriers, may not understand institutional procedures, and may be unaware of cultural norms that contribute to conventional loan approvals. Not all financial institutions are interested in making small business loans of less than \$50,000 (Edelman, 1915). Some lenders may not have culturally competent staff or staff with underwriting expertise for unique industry startups. For some lending institutions, decisions for startup market participation can be far removed from local loan officers. Portfolio decisions affecting loan approval are sometimes made by a higher authority at corporate headquarters far removed from the local loan client and loan officer.

While numerous studies point out that low-income households can save, others have identified institutional and public policy factors that might impede low- to moderate-income households' ability to save (Beverly & Sherraden, 1999). Having access to checking, savings, or credit accounts has been found to be related to savings behavior. Turnham (2010) found a number of factors that prevented or reduced the ability to save, including inadequate income, lack of access to savings programs, lack of financial knowledge, spending behaviors, feelings of discouragement when events disrupted savings, and lack of trust in institutions. Income instability also appears to be a barrier to savings.

Financial knowledge has been found to be associated with "positive" financial behaviors (Hilgert, Hogarth, & Beverly, 2003; Osteen, Muske, & Jones, 2007). Other characteristics associated with individuals who perceived they could and could not save included age, presence of child under 18 years of age, and gender (Mauldin, Bowen, & Cheang, 2013). Having no money left over, being late on bills and/or credit card payments, being under- or unemployed and having been affected by a natural disaster were associated with perception of whether one could save. These circumstances and characteristics may often be present with culturally diverse, low-income female entrepreneurs.

Gap Analysis and Institutional Development Planning

In January 2012, a community investment officer for a large bank in the Des Moines market organized a delegation visit to a Grameen America project in an

out-of-state large metro community. At that time, there were no conventional lenders or nonprofits that were providing loans of less than \$5,000 in Des Moines. The delegation included the bank's community investment officer and representatives from university extension and two nonprofit microenterprise development and training organizations. The delegation visited one of the first eight projects organized by Grameen America as it had disbursed small loans to 1,800 low-income women in less than four years.

The University Extension representative was previously impressed after reading *Banker to the Poor* (Yunus, 1999) and was leading an Extension initiative designed to revitalize a nascent nonprofit called Iowa Community Capital (ICC). ICC was a Community Development Financial Institution (CDFI) certified by the U.S. Treasury for access to the CDFI fund. ICC was Iowa's only CDFI with a statewide mission to provide business technical assistance and financial capital to benefit low-income populations and underserved areas. On the return trip from visiting the Grameen Project, the bank's community investment officer and University Extension representative agreed to explore the feasibility of bootstrapping a smaller project using Grameen methods. University Administration sanctioned Extension involvement in nonprofit leadership under two conditions: Extension and University staff (a) would not represent a majority of the nonprofit board and (b) would not participate in the loan decisions.

The bank's community investment officer was part of the Des Moines Latino Leadership Forum network, which studied various lending circle alternatives and recommended a Grameen-style lending program to a communitywide planning process called Capital Crossroads as a strategy to stimulate incomes and economic activity in low-income areas of the urban core. The Community Crossroads agenda was subsequently used for shaping priorities for philanthropic giving and grant making by the Community Foundation of Greater Des Moines. A market study and target low-income population focus group was organized by a third party to discuss the need for small loans, loan terms, repayment amounts and meeting participation requirements. Contact was made with Grameen America to discuss and determine interest and willingness to share methodology and advise a small project located in a small metro area.

The University Extension initiative led development of ICC's business plan for an initial 3-year project and fund raising budget with goals to reach 300 clients and to replicate client performance metrics reported by Grameen America projects. The plan included a collaboration agreement with a second nonprofit, Iowa Microloan, to provide back-office loan administration, payroll and fiscal accounting. ICC called the new program Solidarity Microfinance (Solidarity Microfinance, 2019). The bank's CEO made the first three-year financial commitment. In spring 2013, community development leaders from Chicago's Federal Reserve Bank hosted a Solidarity workshop for nonprofits and bank compliance officers in the Des Moines market. Featured presentations included

the CEO's initial funding commitment, the market study client need testimonials, collaborating nonprofit loan administrator experience, and goals for the business plan and funds raised for the 3-year pilot. ICC's budget targets were sufficiently met by Spring 2014 to launch the Solidarity Microfinance program and the bank's community investment officer joined the ICC Board.

Demonstration Project Training, Policy, and Program Implementation

Solidarity Microfinance has been the first and only program launched by the ICC nonprofit following its reorganization. First steps included hiring a staff. For Coordinator, ICC looked for someone possessing familiarity with local low-income population networks, openness to training and guidance on Grameen methods, leadership skills necessary for arranging the office, ability to create media presence, and skills to organize a launch ceremony attractive to community stakeholders as well as potential client networks. ICC remained in contact with Grameen America for methodology training. A consultant was identified with 30 years experience in Grameen methods, experience at various Grameen positions in accounting and management, and Grameen experience in organizing successful startup projects including Central America—in Spanish.

A week of training for the ICC Board and staff occurred in August 2014. Another training week was conducted in October in conjunction with the Solidarity Program launch—which attracted 80 community leaders and potential clients. The Coordinator organized the initial two beta-test loan groups in November. The Consultant arranged a visit Grameen America Project to provide the Coordinator and ICC Board leaders with an opportunity to observe and discuss Grameen methods and procedures in detail. One initial beta-test loan group failed before the end of 2014. As a result, the ICC Board concluded that training alone would not be sufficient for program success. So, the Grameen Consultant was engaged fulltime onsite as Solidarity Program Director in Des Moines beginning March 9, 2015 and he has led the Solidarity program since that time.

What makes Grameen methodology and the Solidarity Microfinance structure unique and different from conventional loan underwriting? No written business plan is required. No collateral or conventional loan guarantee is required. No credit score or credit history is required. Solidarity loan decisions are made by peers and staff based on character, trust, behavior and repayment performance.

To be eligible for the Solidarity Program, a person must be low-income, age 18 or older, and have lived in the community for two years. The first element in the formation of a peer group is that five women must know and trust each other and have interest in developing an income generating activity. The group members participate in five one-hour orientation sessions to become familiar with program rules and expectations for weekly or bi-weekly meeting participation, loan payments, savings deposits, and support for each other's enterprises. During

orientation, group members and staff meet in client homes, verify eligibility, member willingness to trust other group members. If all potential members and staff are in agreement, the loan group is approved. The loan group elects officers and group meetings begin either weekly or every other week at client leader's home. The loan group meetings are typically one-hour and may involve multiple loan groups in a neighborhood Center meeting with two to six loan groups that meet together. Group and Center leaders and a staff person facilitate collection and passbook procedures for half of the hour meeting. The remainder of the meeting time is allocated to group activities and mentoring discussions involving client enterprises, business challenges, or family and community topics of interest to the clients.

Before loans are considered, each Solidarity group member describes their income generating activity and explains the intended use of their loan to other group members. Typically each member of a group initially starts with a \$1,000 loan and makes installment payments over a six-month loan term. Loan group members and two staff discuss each loan proposal and will either approve, reduce the amount, or deny each loan. If a client maintains a good record of meeting participation and loan payments, they are eligible for a \$500 increase in loan amount every six months. If a group member does not repay their loan during the six-month term, no one in the group is eligible for future Solidarity loans until all loans in the group are repaid.

The interest rate on all Solidarity loans is 15 percent. However since all loans are for six-month terms, the loan amounts grow as the enterprise repayment capacity grows. The total combined interest paid over a two-year period on Solidarity loans is significantly less than interest payments on a single market rate conventional two-year loan that covers an equivalent amount for the combined Solidarity loans over two-years. Thus Solidarity client payments go more to Solidarity loan principal and less to Solidarity interest in the two-year comparison. Recently, the ICC Board approved raising the maximum loan amount from \$6000 to \$8000 for clients with the longest participation record.

All Solidarity clients are required to establish a savings account at a local bank. Each Solidarity client allocates a designated portion of each meeting payment for deposit into the savings account. ICC and the Solidarity Program maintain a custodial relationship with the bank and each client. Each savings account remains in the client's name. The savings can only be withdrawn for approved emergencies during the first three years of program participation.

Seminars on special topics of interest to the clients are organized periodically. Attendance is not mandatory. These educational opportunities are typically held quarterly and involve local resource persons who cover topics such as legal matters, accounting, taxes, credit scores, and physical abuse.

Assessment after Five Years of Solidarity Microfinance Operation

The Solidarity Microfinance program demonstrated consistent growth during the first five years of operation. However the program did not achieve the 3-year goal of attracting 300 low-income clients by the end of the fifth year (Table 1). Many factors were perceived to influence slower than expected growth, included improving economic conditions and lower unemployment rates, increasing risks and uncertainties created for diverse new resident target populations by immigration policy actions, staffing and resource limitations.

Table 1. Solidarity Microfinance Participation July 1, 2014 to June 30, 2019.

June 30 Fiscal Year End	FY2015	FY2016	FY2017	FY2018	FY2019
Active Loan Clients	50	97	122	150	152
Cumulative Clients	50	118	179	253	284

Source: Solidarity Microfinance Director's Report, July 18, 2019.

The diversity of the low-income new resident populations attracted to the Solidarity program at the end of the fifth year is described in Table 2. Center meetings for Hispanic clients were conducted in Spanish.

Table 2. Solidarity Microfinance Client Demographic Indicators on June 30, 2019.

	Hispanic	Black	Caucasian	Female	Male
Percent (%)	82%	17%	1%	99%	1%

Source: Solidarity Microfinance Director's Report, July 18, 2019.

The age and educational attainment of the target population attracted to Solidarity Microfinance are reported in Table 3. The income generating activities of the Solidarity clients typically encompassed a wide variety of part-time, home based enterprises such as hair products and services, jewelry and clothing sales, cleaning products and services, health and beauty products, child and senior care, food and catering, and crafts.

Table 3. Respondent Characteristics of Solidarity Clients Serviced FY2019.

Age Category	Respondent Age Distribution		Educational Category	Educational Distribution
18-24	6%		Less than High School	31%
25-34	29%		High School or Equivalent	48%
35-44	39%		Some College Assoc. Degree	16%
45-64	26%		Bachelor's Degree	5%

Source: Solidarity Microfinance Director's Report, July 18, 2019.

During the first five years of the Solidarity Microfinance, ICC conducted program operations primarily with two full-time equivalent staff positions: a director and a coordinator. The staff organized 48 loan groups into 18 centers, disbursed \$1,958,599 in loans to clients, and deposited \$74,714 into individual savings accounts for clients. The loan balance outstanding for Solidarity clients was \$213,715 on June 30, 2019. Average loan disbursements to Solidarity clients and fiscal year end loan and savings balance averages are reported in Table 4.

Table 4. Solidarity Microfinance Client Balances at Fiscal Year End, 2015- 2019.

End of FY: June 30	FY2015	FY2016	FY2017	FY2018	FY2019
Average Loan Disbursed	\$ 1,114	\$ 1,399	\$ 1,894	\$ 2,255	\$ 2,600
Average Loan Balance	\$ 803	\$ 896	\$ 1,155	\$ 1,303	\$ 1,455
Average Savings Balance	\$24	\$101	\$131	\$150	\$ 233

Source: Solidarity Microfinance Program Data, 2015-2019.

Analysis of Program Performance Metrics and Impacts

The ICC Board and Solidarity Microfinance Director established four program goals in 2014. First, ICC desired to demonstrate whether or not the 98% loan repayment rate reported by Grameen projects could be replicated by a non-Grameen microfinance institution. The Solidarity loan repayment rate exceeded the goal and was calculated to be 99.7 percent for the five years of operations. This metric is calculated from loan administration accounting records. One factor in loan repayment success appears to be related to the short six-month loan term, which allows clients facing issues to quit within a short period after loans are paid. Another factor is the pressure and support provided by peer groups when a group member experiences repayment difficulty. Finally, clients who leave a group with unpaid obligations may face stigma from their cultural and social networks in the community.

A second program goal was for indicators of Solidarity client income to increase by \$2,400 annually (\$200 per month or more). The 2018 Solidarity Annual Report indicates average client income increased by \$6,777 annually. The Solidarity Program conducts a client survey as part of the loan payoff procedure at the end of each loan and the client business income change is calculated from the survey responses for the most recent sample in 2018.

A third program goal was for Solidarity clients to achieve \$150 in savings for emergencies. As part of its custodial relationship, monthly statements from savings accounts for the clients are reported to Solidarity and compiled. Table 4 reports the average savings account balance was \$233 for active clients on June 30, 2019. Therefore, the clients surpassed the Solidarity program savings goal.

A final program goal was for Solidarity to provide clients with an opportunity to establish or increase their credit scores. Solidarity loans and payments are

reported monthly to the major credit bureaus through Credit Builders Alliance. ICC requested credit reports for Solidarity clients every six months as part of the client loan request and payoff until 2018. Credit scores were tabulated for the 108 credit reports were received for Solidarity clients during 2017. FICO scores ranged from 443 to 781. Not all Solidarity clients had prior credit scores for comparison indicating that a new credit score was being established by Solidarity loans. A sub-sample of ten Solidarity clients without previous credit scores achieved an average FICO score of 670 during the initial six-month loan period. The remaining sub-sample of Solidarity clients with beginning and ending credit scores for 2017 showed an average FICO score increase of 10 points. This modest increase average reflects the possibility of client credit issues external to the Solidarity program as well as the potential for credit bureau algorithms that generate higher reporting errors for clients using ITINs for identification as has been documented by others (Acevedo, 2016).

Solidarity evaluation surveys conducted with each client during loan payoff procedure collected data participant attitudes and performance. Client surveys for 2018 were translated by third-party interpreters and evaluators external to the staff. The 2018 report indicated 79 out of 83 clients, or 95% of survey respondents provided comments indicating the Solidarity program assisted them in some manner, while 5% identified weaknesses or areas for improvement. Selected comments included: “Helped me grow my business”, “Raises income”, “Easy getting a loan and easy payment”, “Helps me to invest more wisely in my business”, “Appreciate interaction with other people”, “Learning from each other”, “Opportunity to start a business”, “Provides opportunity to improve self”, “Opportunity for family to get ahead”, “Being able to make money in business”, “Helps in becoming more responsible”, “Helps repair credit”, “Helps women to make own decisions”, “Helps in getting to a better life”, “Helps in learning how to use earnings”, “Helps with discipline”, “Helps in meeting people”, “Very good help for women who need help”, “Easy loans and low payments”, “Like the flexibility and honesty”, “Helps create mutual trust”, “Helps in treating others as equals”, “Creates more unity and commitment among those in the group”, “Learn teamwork”, and “Helps each other to grow assets.” The unfavorable comments were related to staff transitions and conflicts within some loan groups regarding discipline and member responsibilities.

Two program adjustments and innovations were implemented due in part to client feedback. First, Solidarity moved from weekly loan group meetings to meetings scheduled every other week in 2017. This change nearly doubled the size of each loan installment payment. However, the program time scheduling requirements for each client to participation was reduced. The change was observed to have little impact on loan repayment rates. Solidarity staff time was released to perform other functions or serve additional loan groups.

Second, the Solidarity savings program was a priority for funders interested in addressing the issues of “under-banked” and “unbanked” populations. The traditional Solidarity savings program was adjusted to make deposits to individual accounts once during each loan term instead of small weekly deposits. This adjustment was made to avoid transaction fees before a pending policy change by the host financial institution. The savings amount total for the six-month period was added to the loan amount but deducted and deposited in savings at the time of loan disbursement. The clients continued to make payments weekly or every other week without significant change in cash flow.

Sustainability and Community Impacts are related. Nonprofits focusing solely on client microfinance assistance tend to require significant philanthropic efforts for sustainability. The reason conventional financial institutions avoid low-income microfinance is that little or no profit margins exist. Also microfinance products for low-income target populations may come with additional costs and risks related to underwriting, language and culture. Solidarity program annual interest earnings in FY2019 are sufficient to support about 15 percent of the cost of Solidarity operations. A 50 percent self-sustainable program would be easier to promote to donors compare to a 15 percent self-sustainable program. While larger scale economies may allow greater efficiencies by sharing administrative overhead among multiple projects in multiple communities, full sustainability appears to be infeasible without continuous philanthropic commitments. Internal ICC debates over strategic next steps emerged. One extreme plan would narrow ICC focus to serving needs of one culture and one community. An alternative plan would diversify programs to add communities and add more lucrative financial products and economic development services to support Solidarity.

Continuous philanthropic commitment is unlikely without ability to demonstrate community impacts. In the case of Solidarity, active clients used their access to capital in FY2019 to generate an estimated combined incremental increase in earned income of over \$1 million. When compared to the net operating budget requirements for the Solidarity program, each \$1 of philanthropic support generated over \$6.60 of increased client income in the community, without considering the value of individual empowerment, skills and social capacity.

Summary of Findings and Implications in a Changing Policy Context

Solidarity case study results demonstrated that outcome metrics promoted by Grameen projects can be replicated and that the methods can be successfully applied in a small metro area with similar results for low-income women entrepreneurs of diverse cultures. Expectations for client loan repayment, income increase, and savings were exceeded. While average client credit history improved only modestly for those with prior credit score issues, however a respectable FICO score average of 670 was established for clients without a prior credit score. Client surveys indicated found favorable attitudes relating to

Individual financial literacy and management skills, problem-solving skills, confidence, leadership, business investment, marketing networks, access to capital, teamwork, and improved outcomes for their businesses and families.

Sustainability for Solidarity Microfinance in a small metro community remains inconclusive due to a relatively low sustainability ratio of 15 percent in 2019, even though a philanthropic case of community impact can be articulated: for each \$1 donated, more than \$6 of incremental earned income is generated by clients from the low-income target populations. Changes in the policy context also have implications for sustainability of Solidarity. Charitable giving from corporate and individual donors is expected to decline as marginal tax rates decline following recent tax policy reforms. Community Reinvestment Act and regulatory context reforms for banks are factors in philanthropic support of CDFI nonprofits like ICC. Income disparity more broadly appears to have increased in deference to initiatives for economic inclusion. Divisions and debate over immigration policy generate uncertainty and affect philanthropic giving as well as the level of program participation by target populations. Key factors in Extension's role in sustainability include perceptions about the mission for Extension and perceived role of Extension professionals beyond subject matter and process to inclusion of client practice opportunities, technical assistance coaching, and nonprofit affiliation and support when the mission is aligned with Extension. A final key factor is the relative priority of importance that Extension decision-makers place on outreach to target low-income populations with diverse cultures and limited access to capital for personal, family and community economic development.

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