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News

Microlending offers hand up asset ladder
By Sue Kirchhoff, USA TODAY
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PORTLAND, Ore. — Sherrita Myers has overcome many challenges to create a thriving child care center in her home. They've ranged from minor headaches (Play-Doh down the garbage disposal, Barbies in the plumbing) to major hurdles, such as a lack of capital and business experience.

Myers' success is a tribute to her tenacity and the city of Portland's intensive efforts to help low-income workers build assets.

"Without them, I think I would have been shut down long ago; I wouldn't own my house," says Myers, 28, who has increased her monthly earnings to $5,000 from $1,000 several years ago. She's now saving for future needs, with each dollar she deposits in a special account matched two to one.

Fed banks step in to boost asset creation
On March 14, the Kansas City Fed will host the next in a series of forums on asset building, focusing on underserved groups.

The San Francisco Fed, which held its meeting last year, is now working with the city of San Francisco to open savings accounts for 10,000 people.

"Asset creation does appear to be a good way to address poverty," says Jack Richards of the San Francisco Fed.

Oregon, one of the first states to adopt Individual Development Accounts (IDAs), which offer a one-to-one, two-to-one or better match for every dollar saved, is considering a new program focused on savings accounts for children. The state, which funds its IDAs through a tax credit, funded 260 accounts last year and hopes to reach 1,500 to 2,000 a year.

But on the federal level, legislation to create a nationwide system of IDAs is stymied. Portland faces cuts in the federal funding it uses for its programs.

Myers is part of an expanding effort, including a new push by the Federal Reserve, to help low-income workers build wealth. The idea is to help people move out of poverty or up the financial ladder by starting a business, buying a home or accumulating savings.

Asset-building strategies include no-closing-fee home loans, financial education, ATM-type stored-value cards and support for microenterprises — firms with five or fewer workers needing $35,000 or less in capital, which often don't have access to commercial banks. Individual Development Accounts (IDAs), offering a one-to-one, two-to-one or better match for every dollar saved, also hold promise. Matches can come from government or private sources.

The drive for assets is as old as the nation, but the issue has a new urgency. The personal savings rate has plunged into negative territory. Government welfare programs have been cut. Financial holdings remain tightly concentrated. The top 1% of the population has about a third of the nation's wealth, while the bottom half owns less than 3%.

New Fed data show some signs the wealth gap is growing: the median net worth (gross assets minus liabilities) of non-Hispanic white families rose 6% to $136,000 between 2001-2004 but was basically flat for African-Americans at $20,000. Research has shown that African-American and Hispanic families have lower rates of homeownership and hold fewer financial assets, such as stocks. At least 10 million people have no bank account, including many Hispanics.

Central bank officials are so concerned that the 12 regional Fed banks have launched a joint effort with Washington non-profit CFED, (originally the Corporation for Enterprise Development) to develop strategies for asset building. Regional Fed banks are hosting meetings around the country, bringing together such big names as Citigroup, Bank of America, Harvard and the Ford Foundation and smaller non-profits and firms.

Two sessions have been held, with three more planned this year, including a meeting at Fed headquarters in Washington, D.C.

"As Americans, we believe in the fundamental concepts of savings, homeownership, higher education for our children, and a comfortable retirement ... but for many people — especially those with low or moderate incomes — these are luxuries, abstract and unattainable," Philadelphia Fed President Anthony Santomero told a December forum sponsored by the New York, Philadelphia and Boston Fed banks.

Financial security certainly seemed out of reach for Judith Pothier of Springfield, Ore., who hit bottom several years ago, disabled and dependent on federal aid.

Pothier is now launching a business making coverlets for people who are in wheelchairs or spend a lot of time outdoors, such as hunters and sports fans. Her enterprise has been financed partly with an IDA and other aid via the non-profit Lane MicroBusiness.

"To me, even $25 makes a difference in, 'Oh, I can eat something different than rice and beans this week.' When you're already low on the totem pole, you can just go up," says Pothier, who made her first substantial sale to a Japanese firm.

Building assets is key

Financial assets — savings, checking or retirement accounts, stocks and bonds — and non-financial assets — a car, home or business — can spell the difference between security and drift. Assets mean access to college education, the ability to open a business, buy a house, have a secure retirement and a hedge against job loss.

"People do not thrive for long without assets. They may have a good job and a good income, but if they don't have assets" they are at risk, says David Foster, policy strategist at Oregon Housing and Community Services.

Despite a history of entrepreneurs and such asset-building laws as the 1862 Homestead Act and 1944 GI bill, U.S. wealth remains concentrated by income and race.

Andrea Levere, president of CFED points out that many tax breaks for savings and retirement go mainly to the well-off. Low-income workers are denied access to social programs if their assets are above certain thresholds.

A study by the Pew Hispanic Center found that in 2002, Hispanic households' median net wealth was just 9% that of non-Hispanic white households. Recent Fed research shows that about 20% of black families had no type of non-financial asset in 2004. While that's an improvement from 24% in 2001, it compares with less than 5% of non-Hispanic white families.

At the same time, the median net worth of black families with business assets was about $174,000 in 2004, more than eight times the median for all black families, Fed Vice Chairman Roger Ferguson said in a speech on the data.

Average net worth of blacks rose faster than for whites in the period, as the number owning homes and businesses rose. Because the ownership is relatively narrow, the median didn't change, Ferguson said.

Valerie Plummer, executive director of the Oregon Microenterprise Network, says asset development is not just about alleviating poverty, but also about economic development. About 17% of U.S. businesses meet the definition of a microenterprise. Many business owners have skills but lack capital.

Ron Tate, 52, runs Tate Insurance Services in a Portland office with a shelf of trophies from youth football teams he has coached. After working for another insurance firm, he expanded his business several years ago with $3,000 from Mercy Corps Northwest microloan program. "My credit score wasn't that good; I knew I wasn't going to get (money)" from a bank, says Tate, who has paid off his loan. "Things took off pretty well for me. I might have some needs coming up," he says. Still, given his firm's small size, he adds, "I'm not sure whether a regular bank will help."

Does it work?
The asset development movement has been quietly expanding since the 1980s. Today, there are hundreds of IDA programs around the country, serving tens of thousands of borrowers, predominantly women and minorities. More than 500 microenterprise programs provide counseling and capital to a quarter of a million people a year.

While the programs serve a tiny slice of the population, there is evidence they make a difference. Portland officials work with local businesses and other institutions to provide health care, legal aid, insurance, and financial aid and counseling to people making 50% or less of the area's median income ($33,950 for a family of four). The goal was to raise business revenue by at least 25% over three years. In the past 16 months, revenue at 268 microbusinesses is up more than 50%.

"Few cities across the country right now have a poverty-reduction program. ... Most are hung up on the trickle-down economic approach," says Lynn Knox of Portland's Bureau of Housing and Community Development, who says the economy is rigged against the poor.

A study by the non-profit Aspen Institute found more than 72% of low-wealth entrepreneurs increased income in five years. Rates on Mercy Corps microenterprise loans average 11%; the default rate is about 10%. The higher interest rate reflects the riskier loans.

Banks are becoming more engaged in IDA and microlending. One reason: The efforts help them meet legal obligations to lend to underserved areas. In Oregon, Plummer has been meeting with private banks to create a rural loan fund for microentrepeneurs.

Businesses are also stepping up. The Association for Enterprise Opportunity is working with the eBay Foundation on a pilot program to help individuals who want to start online businesses. It also has projects with other major firms.

Still, the San Francisco Fed, in an asset development publication, notes a large number of savers dropped out of an IDA demonstration project or couldn't save more than $100. Many who did save set aside about $25 to $35 a month, not enough for a home down payment or major purchase.

The programs are expensive to operate, with IDAs costing as much as $850 to $2,000 per participant. The overhead costs of administering the loans, including training for recipients and other services, are high and, so far, hard to recover.

As the asset-building movement has grown, there has been a surge in payday lenders, check-cashing firms and high-cost subprime lenders. More capital is available in low-income areas, but it's often found in pricey loans that strip assets, Alfreda Norman, community affairs officer at the Dallas Fed, says.

"There are people who are poor because of discrimination, both in the labor market and in the credit market, and for those people, this (asset development) undoubtedly would work," says

William Spriggs, chairman of Howard University's economics department. "Given what the Fed has power over, a more effective strategy that might affect more people would be to combat discrimination in credit in general," he says.

While the Fed is interested in using asset development programs partly to combat poverty, a number of clients served by microlenders don't fit the profile of the long-term poor. In Portland, some of the most successful people using the Mercy Corps program have college educations or professional backgrounds but were unable to get help from a commercial bank. That means success rates might be influenced by the fact that some who flourish need only minimal aid. Overall, most of the Mercy Corps loans are to women and minorities.

Savings and lending programs also help those trying to rebuild their lives. Symon Lee, 40, owner of Furever Pets in Northeast Portland previously had a career as an industrial designer. In 2001, after family illnesses, Sept. 11 attacks and layoffs at his firm, he took a new path, opening a pet store in northeast Portland. He turned to Mercy Corps in 2003; it helped him write a business plan and consolidate debts. He has paid off his $17,000 loan, expanded and has one part-time and two full-time employees. "Ultimately, our goal is to produce our own products — this for me is a stepping stone," Lee says.

Jennifer Richardson was a sculptor in New York City who came down with a chronic illness after the attacks. In and out of hospitals and bankrupt, she made her way to Portland. With the help of a $7,000 Mercy Corps loan, she opened Jennie Greene Floral Designs. "I had an idea, but I wasn't eligible for a (bank) loan," says Richardson, who has met her loan payments.