Community Credit

An essential tool in economic and social development

Réseau québécois
du crédit communautaire

November 2000

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- Community credit is an **innovative response** to the needs of the unemployed, social assistance recipients, low-income workers and people with no waged work. People who want to make a place for themselves in society but have many doors closed to them.

- There are major obstacles preventing many people from accessing the usual forms of credit: they may require only small loans that are of little interest to lending institutions, may lack the necessary guarantees, business experience and credit history, or have problematic credit ratings.

- Accompaniment, training and needs-based follow-up activities are combined with flexible financing to remove the obstacles that often isolate people and prevent them from fully participating in the economy.

- Community credit is part of a constellation of alternative financing in Quebec and an **indispensable complement** to institutional economic and social initiative mechanisms and structures.

- Community credit has a remarkable track record in Quebec. Since its inception, over $1.5 million dollars has been invested, 657 local jobs have been created and maintained and 237 previously marginalized citizens have carved out a place for themselves within the mainstream business economy.

- Despite their impressive track record, community credit organizations remain financially fragile and must count on the support of their socio-economic partners to continue their missions of development.

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Introduction

In recent years, community credit has become increasingly popular in Quebec and throughout North America. While community loan circles take a collective approach to credit, community loan funds provide financing on an individual and project-specific basis. Together, these two approaches for a major part of the bedrock in Quebec's anti-poverty economic and social initiatives.

In 1998 there were over 400 community loan funds in the United States and approximately 200 community organizations operated loan circles.[1] A recent study in Canada reveals that there are 34 not-for-profit community credit organizations,[2] but it is estimated that between 40 and 50 organizations are currently operating in this sector.

The evolution of community credit in Quebec has led to the creation of a remarkable number of organizations. In fact, Quebec accounts for about half of the total number of community credit organizations in Canada. **There are 22 organizations that operate loan circles and six community loan funds in Quebec.[3] These organizations operate in 10 administrative regions of the province and their diverse practices reflect the specific needs and available needs-based resources of each region.** The majority of loan circles make do with annual operating budgets of less than $100,000 and fewer than six employees. By contrast, community loan funds operate based on a total average annual budget of between $100,000 and $200,000 and fewer than six employees. All of these organizations operate under the aegis of the Réseau québécois du crédit communautaire (RQCC).

Quebec's expansive growth of community credit can be attributed to several interrelated factors. To begin with, globalization in financial markets has led conventional financial institutions to drastically rationalize their operations. Consequently, credit for "high-risk" clients has been severely cut back. Meanwhile, a major restructuring of the job market has brought about an impressive increase in the number of self-employed workers. From 1989 to 1998, their numbers rose by 5.5%.[4] We know that self-employed workers are often considered to be bad credit risks or unprofitable clients since their loans are often modest and they may not have a credit history. **It was the convergence of these two major forces — tighter restrictions on the credit offering to disadvantaged clients and the glut of demand from independent businesses — that led to a surge in need for financing and support for a clientele that was becoming progressively more marginalized. The need for micro-credit is still on the increase.**

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[1] Joël Lebossé, *Micro-finance et développement local* (1998): 49, 51.
[2] CALMEADOW, *The State of Microcredit in Canada* (1999): 28.
[3] Réseau québécois du credit communautaire, *Le micro-crédit par le modèle des Cercles d'emprunt et des Fonds communautaires d'emprunt* (1999): 6.
[4] Statistics Canada, *Labour Force Survey* (1998).

Quebec community credit in perspective

Community credit is not just filling in where conventional financial institutions have pulled out. It is providing a personal and community development tool that allows disadvantaged people to claim a place for themselves in society. Indeed, community credit is part of a socio-economic movement in Quebec that was recognized by the *Chantier sur l'économie sociale* in 1996. Social economics are part of a new social and democratic order in which community groups and government bodies work together for local development. Community credit is an expression of the deep commitment of the community-based sector of society to the economic and social development of communities in Quebec.

The brief history of micro-credit in Quebec dates back to 1990. However, the real growth in this sector has taken place over the past five years in response to the ever-growing needs of the self-employed workers and marginalized people in our society. From the start, community credit was involved on several fronts at the same time, tackling ambitious objectives in its double role as a social and economic movement.

The objectives of community credit:

$ To create durable, quality employment while responding to the social, economic and cultural needs of a community.

$ To allow people who are unemployed and living in economically precarious situations to access financing for a business or self-employment project.

$ To reactivate people who are excluded from economic, social, cultural and political life in their community.

$ To combat poverty by contributing to the revitalization of disadvantaged neighbourhoods.

Community credit offers an innovative response to the need for non-conventional financing and development.

What distinguishes made-in-Quebec community credit other micro-credit? — **Its comprehensive approach geared towards fulfilling people's economic and social needs.** Loan circles and loan funds contribute to fulfilling these needs through their complementary activities.

A collective approach to community credit:

LOAN CIRCLES

Loan circles are designed for people who wish to be self-employed or to start up a microbusiness. People who want to make a place for themselves in society and in the economy. Members enjoy the many advantages of a collective approach in which peer support plays a key role. **Community loan circles take an approach that includes several steps:**

- ***Accompanying the borrower and the business***
  Personalized follow-up activities provide support for informed decision-making on best practices and business strategies.

  Training programs in management and business start-up are adapted to the steps involved in the evolution of a business (including pre-start-up, start-up, consolidation and expansion). Workshops develop independence and self-esteem among entrepreneurs.

- ***Providing access to credit by taking responsibility as a group***
  Support for self-employment or microbusinesses is provided through follow-up activities and access to credit, group assessments of loan applications, financing, peer endorsement, and the monitoring of entrepreneurial and personal development.

- ***Raising capital and mobilizing savings***
  Capital is built up by calling upon partners within the community.

Training and professional development activities from the pre-start-up phase to development and expansion, and peer support are the strategic elements that guarantee that loan circles will succeed where other financing and social reinsertion approaches have been less effective.

An individual approach to community credit:

LOAN FUNDS

Loan funds provide a flexible tool in the start-up and maintenance of microbusinesses, small businesses and businesses operating within the parameters of social economics that cannot access financing through conventional sources. Loan funds complement loan circles since their clients respond better to an individual approach to accompaniment and follow-up activities than to a collective approach and their financial needs may also be greater. **Community loan funds work in four distinct phases:**

- ***Raising capital and mobilizing savings***
  This mobilization allows borrowers to consolidate and build up their development capital by calling upon partners within the community.

- ***Project financing***
  Loans and guarantees are provided at competitive rates. Projects must be financially, economically and socially responsible.

- ***Technical support and accompaniment***
  This is a key element in the approach taken by community loan funds that aims to strengthen projects, develop the expertise of borrowers and protect the interests of both borrowers and the loan fund as such.

- ***Promotion of activities and concerted action***
  Community loan funds work to provide access to local networks, disseminate information, and raise community awareness. They also act to stimulate and increase support for projects through partnerships, pooling of local resources and concerted action.

Financial levers

Access to community credit allows borrowers to establish or re-establish their financial credibility by reimbursing loans under contract. In this way, community credit acts as a bridge between borrowers and other sources of financing and technical support — be they private, not-for-profit or public.

Above all, community loan funds allow people who have been excluded from economic and social networks to bring their projects to fruition and reintegrate into society while creating businesses.

A place in the sun

Community credit targets people who live on the sidelines of society, who are unemployed or who are in precarious socio-economic situations. These people want to improve their situations and to become more independent so that they can fully participate in the social and economic life of their community. They find it difficult or impossible to access credit from conventional sources. A study of the three biggest micro-credit organizations operating in Canada[5] provides the following borrower profile:

- One-third of borrowers are in the 41–50 age category and over 17% are over 50 years of age.
- Over one third have only a high school education (no further education).
- 55% of the borrowers are women.
- 68% could not count on any other source of credit for their project.
- 13% of the borrowers are involved in their first business or self-employment project.
- 71% work at home.[6]

The profile for borrowers in Quebec might be slightly different, consisting mainly of clients: **with no access to conventional credit networks because of the many economic and social obstacles they face; the majority of whom are women; who want to create their own jobs, often for the first time; and who have a relatively modest but vital need for financing.**

[5] These organizations operate in Toronto, Vancouver and Nova Scotia (in urban and rural areas).
[6] CALMEADOW, *The State of Microcredit in Canada* (1999): 21–22.

A model based on local partnerships and concerted action

Community credit may be defined as a made-to-measure instrument for the development of communities. Concerted action, partnership and access to community resource networks are the touchstones of its continued existence. But its diverse sources of capital and volunteer force show just how closely linked this source of financing can be to a community.

A made-to-measure tool for development

Sources of capital

Data gathered from four of the six community loan funds in Quebec has shown that:

- The capitalization of these funds was up to $1.3 million in 1999, including a reserve that varied between 20% and 40% of the sums invested.
- The main sources of capital came from community sources: individuals, private businesses, foundations, unions and financial institutions.

Deep roots in the community

Several loan circles have their own capital, but their reserves are considerably more modest than those available through loan funds. Diversity in sources of financing is a predominant characteristics of community credit in Quebec, North America and Europe, according to a recent study on the subject.[7] This diversity illustrates how the deeply rooted impetus of community credit can mobilize local savings in the cause of economic and social development.

Pooling local savings

Volunteer labour: a force to be reckoned with

Community credit has rallied the dynamic forces in communities to give of their time as volunteers. Of course volunteers have always played a key role in community credit organizations. In fact, the major role played by volunteers has directly contributed to reducing operating costs in these organizations and increasing the range and quantity of services they offer. With this in mind, it should be noted that:

Six volunteers for every employee

$ In 1999, 242 volunteers were working for 11 loan circles and five community loan funds in Quebec — a ration of six volunteers for every employee.
$ Volunteers play a predominant role as members of the boards of directors, and of support and loan committees.

[7] Joel Lebossé, 46.

The remarkable role played by volunteers is a tremendous example of how development has been embraced members of the community and a testimony to the catalyzing force of these micro-credit organizations. It is thanks to their volunteers that these organizations can maintain their highly participative and democratic decision-making structures.

Community credit catalyzes
$Participation
$Democracy
$Concerted action
&
$Partnerships within the community.

Community credit has developed concerted action and partnership at other levels as well. All community credit organizations work closely with each other through the RQCC. Moreover, several community loan funds provide financial support to loan circles, recognizing the complementarity of their respective approaches. And in the same vein, hybrid loan-circle/loan-fund models have been developed by other organizations with backgrounds in both approaches.

Several community credit organizations have also affiliated themselves with *corporations de développement économique communautaire* (economic community development corporations), Caisse populaires (credit unions), unions and other resources in order to diversify their sources of financing, reach a larger pool of borrowers and reduce their operating costs. These various partnership initiatives show that community credit is front and centre in the social economy.

A tool in financing and development

Community credit is now being recognized as a major resource among today's financing and development structures. Indeed, as a tool for **financing**, community credit is rightly considered to be an innovative financial instrument that can fulfill the needs of self-employed workers and microbusinesses alike.[8] As an instrument for **development**, community credit directly contributes to the integration (or reintegration) of disenfranchised members of our society. It allows them to fully participate in the economic and social life of their communities.

An innovative financial instrument in the small-loans market

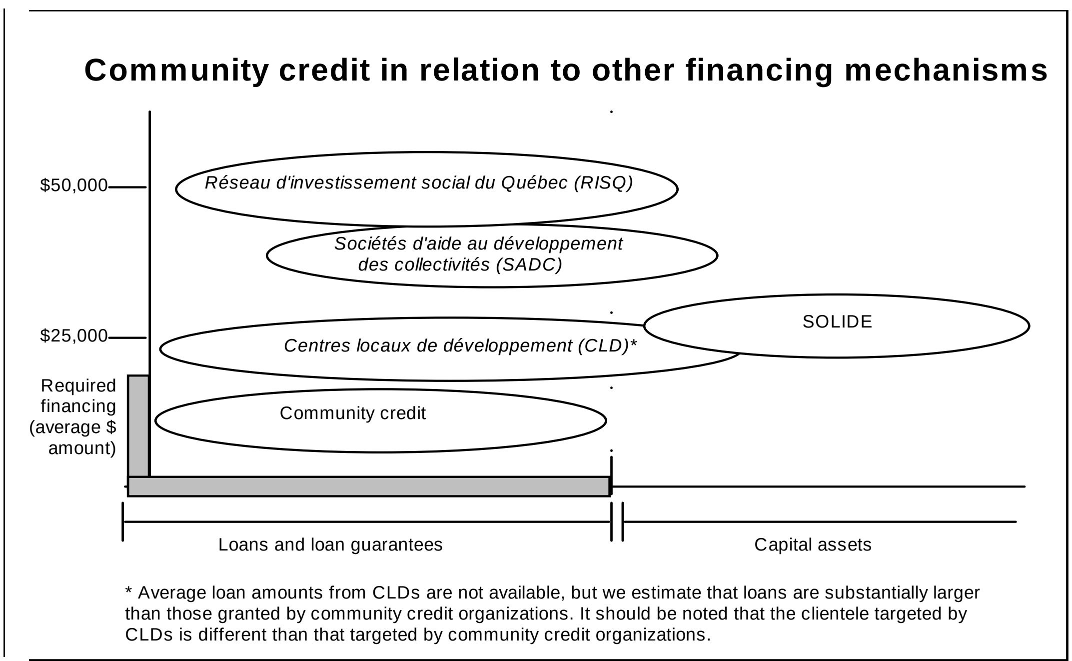
[8] Mendelle et al., *New Forms of Financing Social Economy Enterprises and Organizations in Quebec*. (2002): 6.

A unique market niche

Community credit has developed a range of products over the years. These products are geared towards **bridging the widening gap between conventional financial institutions on one hand and the need to finance self-employed workers, microbusinesses and social economy businesses on the other hand.** It is a recognized fact that conventional financial institutions do not adequately fulfill the needs of small businesses, much less the needs of marginal clientele.[9] By contrast, all of the credit organizations that operate in Quebec offer and guarantee loans. They specialize in the niche of very small-scale loans, normally up to $20,000. Sums are generally even lower in loan circles.

Even compared with other sources of financing (i.e., government funding programs such as the Sociétés d'aide au développment des collectivités [SADCs] and the Centres locaux de développement [CLDs]; SOLIDE and the Réseau d'investissement social du Québec [RISQ]) community credit is in a league of its own (see Diagram 1).

Diagram 1



[9] For example, see the Standing Committee on Industry, *Supporting Small Business Innovation — Report from the Standing Committee on Industry* (1994); and the Canadian Labour Market and Productivity Centre, *Capital, Community and Jobs* (1998): 16.

The diagram above, which positions financing mechanisms in relation to the nature of financing (loans and loan guarantees or share capital) and the average size of transactions, shows that community credit occupies only the market niche of very small loans. Of course other local financing mechanisms play an important role in the development of communities in Quebec. However, they do not directly target self-employed workers and microbusinesses requiring financing under $20,000. In this respect, community credit organizations distinguish themselves in their role as community developers.

Community developers

A needs-based community development tool

As mentioned earlier, community credit is more of a tool for development than it is a financing mechanism. Financing mechanisms that are specific to community credit "almost all come from communities of social intervention and were developed as accompaniment tools in the areas of social and professional reinsertion."[10]

More than just dollars and cents: a tool for development

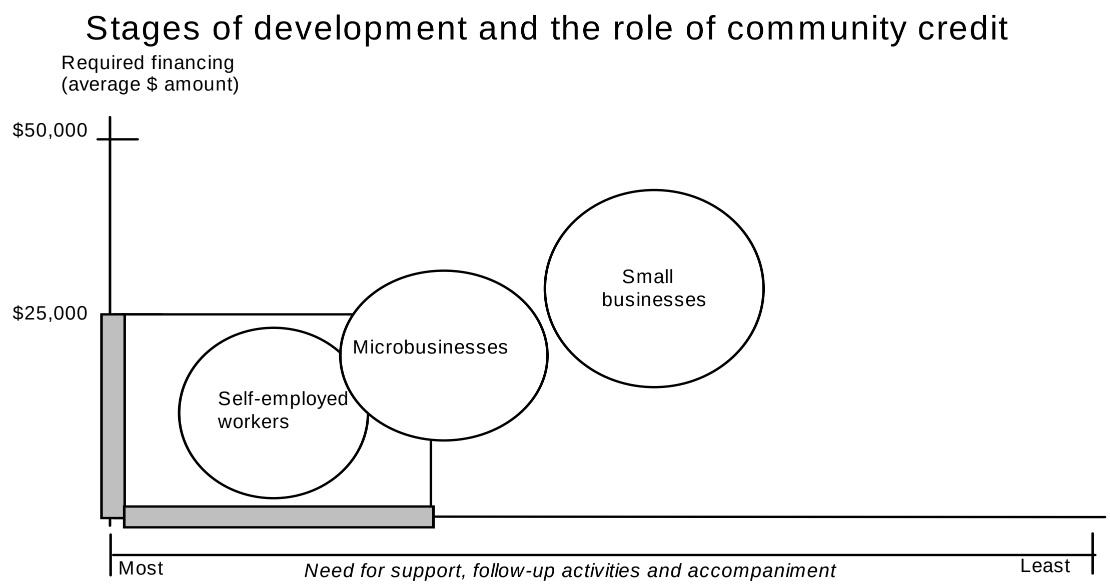
In Quebec, all community loan organizations work with the unemployed, social assistance recipients, low-income workers and the unwaged. Moreover, four of these organizations exclusively target a clientele of women, a category recognized as being among the most highly marginalized. Although the various community loan organizations share many commonalities, their structures, orientations and practices are integrally linked to the needs of their host communities. Thus, each organization develops community-specific **expertise in economic and social reinsertion, as well as in project financing**. The member organizations of the RQCQ offer professional expertise in project development, accompaniment, social reinsertion and financing of micro-projects that cannot be found elsewhere.

The success achieved by these organizations (see the next section) depends heavily on their accompaniment activities (from pre-start-up to development and expansion), the training and accompaniment they provide and the (individual or group) support they offer their clients. These activities are directly related to the needs of businesses and microbusinesses (see Diagram 2, below).

Community-specific professional expertise

[10] Our translation. Joël Lebossé, 45.

Diagram 2



* Adapted from CALMEADOW, 10.

Training received by clients ranges from drawing up business plans to managing a budget for a business and learning about household economics and strategies for access to conventional credit. Through these training programs, borrowers build self-esteem, prepare for the job market and enhance their chances of commercial or professional success.

Reclaiming their place as citizens

Follow-up activities, training and accompaniment also help clients maximize their chances of reappropriating their citizenship and contribute to the development of their community according to their skills and aspirations. Most clients choose one of the following paths:

- $ Job searches based on an entrepreneurial approach
- $ Going back to school
- $ Business development
- $ Personal development planning through community resources that lead to subsequent integration into the job market.

Community credit differs from other promotion measures for business development, employability and social economy in **that it takes a more comprehensive approach, focussed on the development of marginalized people and their integration into the social and economic life of their community** (through independent or microbusiness work projects).

A comprehensive and multi-dimensional approach

An outstanding track record

It is essential to recognize the many positive contributions that have been made by community credit, both as an instrument for financing and a tool for development. Indeed, it is universally acknowledged that the performance of community credit as a financial instrument for high-risk loan activities is enviable: **the average rate of reimbursement** on credit extended by community organizations is 95% in Canada. Community credit is outperforming conventional financial institutions. In point of fact, this excellent financial performance can be explained by the fact that its borrowers — especially those who belong to loan circles — are held accountable for their actions, and provided with individualized follow-up and support.

A 95% rate of reimbursement & personalized accompaniment

Across Canada, **operating costs per completed loan transaction are higher for governmental micro-credit programs than for community credit organizations**.[11] Volunteers and community credit partnerships contribute significantly to this outstanding performance.

Community credit activities also generate direct socio-economic spinoffs that go far beyond financial considerations. In 1999, data gathered from 17 of the 20 loan circles operating in Quebec revealed that:

- 1,345 people had participated in training activities
- 406 businesses had been started up and 344 additional businesses were in the offing
- 161 people had found jobs, 76 had gone back to school and 358 had been referred to other local resources.

[11] CALMEADOW, 39.

Local data gathered from four of the six community loan funds active in Quebec in 1999 showed the following results:

- $ 133 loans were extended to small businesses for a total of $1.2 million
- $ 135 jobs were created and 116 additional jobs were maintained.

Direct socio-economic spinoffs

These results are remarkable, when we consider the fact that the annual comprehensive budget envelope for operations in micro-credit organizations is barely more than one million dollars. These data do not include any of the tax payoffs for federal and provincial governments that would be generated by these activities.

- $ Additional revenue from the income tax paid by workers and newly created or maintained businesses.

- $ Additional revenue from the tax on the profits of newly created businesses.

- $ Additional revenue from the sales tax on goods and services purchased by workers and newly created or maintained businesses.

Payoffs in tax revenue

- $ Additional revenue from the indirect and ripple effects produced by creating new businesses (which generate increased economic activity among suppliers and more consumption among workers and employees)

- $ Reduction of expenses for employment insurance and social assistance from new jobs maintained or created by people who were formerly drawing social assistance or unemployed.

The qualitative benefits offered by community credit are many. Clients have a golden opportunity to reclaim their personal and financial independence. They receive their first loan and participate in training and follow-up activities so that they can enter the normal credit channels and carve out a niche within their communities. These services help borrowers to become full-fledged citizens who are making meaningful contributions to the economic and social development of their communities.

Moreover, when clients become employees in private businesses, we can also calculate that the training, accompaniment and support activities provided by community credit organizations likely reduce net costs for employers and make them more competitive.[12] In sum, the short history of community credit organizations has shown that their **direct and indirect positive effects largely outweigh the expenses incurred by their activities.**

Full-fledged citizens contributing to the development of their community

Issues in community credit

As discussed earlier, a significant portion of the population has been socially and economically excluded and marginalized in Quebec. Community credit provides people in this situation with a viable way to improve their lot in life. Among the province's collective efforts to promote community development, community credit organizations figure prominently in the financing of local initiatives and the organization of countless hours of volunteer work. But the challenges they face are considerable:

- $ Small loans and small loan portfolios directly contribute to increasing the average cost per transaction.[13]
- $ Support, accompaniment and follow-up activities require major investments of time and human resources in every project.
- $ The few salaried employees working for community credit organizations are confronted with a diverse variety of tasks to accomplish. The considerable breadth of this kind of multitasking is peculiar to community credit.

With these facts in mind, it is easy to see that the profit from community loan activities could not realistically cover all of the expenses incurred to meet the socio-economic and individual development objectives of community credit organizations.

Therefore, these organizations need stable partners to continue their missions and build up their assets. Their comprehensive, multidimensional approach and response to needs that can only be fulfilled through their offer of alternative financing. **The responsibility for ensuring satisfactory services to people who have lost their jobs and have been cut off from other sources of credit is shouldered by all of those who work for economic and social development.**

[12] Joël Lebossée, 17.
[13] CALMEADOW, 39.

Increasing the size and stability of their capital is another major challenge faced by community credit organizations. As we have seen, the capitalization of community credit depends on a variety of partners, lenders and donators whose future contributions are unpredictable. So although diversity in sources of financing is a sign that community credit has grown deep roots within a community, it also means that these organizations must spend a great deal of effort in searching for new capital and must work hard to maintain existing sources.

A strategy for consolidating community credit in Quebec

Stable partners needed

Quebec is the standard bearer of innovative practices in social economics, in the partnerships that it has forged in addressing community development issues, and in its original approaches to financing and developing self-employment and small business initiatives. With its extraordinary track record and its unique role, community credit is deserving of our continued support.

The Government of Quebec and its socio-economic partners share the responsibility of providing all citizens with an equal chance to improve themselves and actively participate in the economic and social life of their community. Therefore, we can hope that they will see the relevance of becoming involved as active partners in community credit organizations.

The financial vulnerability of these organizations would be greatly alleviated and the scope of their activities significantly increased if they could count on more stable sources of funding for their operations — estimated to cost approximately $1.2 million per year. To this end, several possible courses of action might be taken:

- Fiscal incentives could be provided to encourage individual, corporate and institutional investors to invest in the loan funds and circles.
- Contributions used to cover part of operating costs and interest-free loans could be allocated in order to increase capitalization.
- Partnerships could be established with the objective of co-financing projects.

Community credit organizations are always actively assessing their practices. But they must also ensure their visibility among potential clients and partners. On one hand, considerable latent demand for community credit has yet to be met.[14] On the other hand, micro-credit organizations could establish a referral system with financial institutions and governmental organizations that would provide a link to clients who have fallen through the cracks.

Supporting the development of community credit

In the final analysis, we have a responsibility to address the needs of the disenfranchised people in our society. **Community credit organizations have a privileged relationship with the people our society has left out in the cold — people who, more than anything, want to contribute to the development of their communities.** Recent history has shown that institutional answers are not enough. The obstacles facing marginal people and groups are far too great for them to confront alone. Community credit is a unique and viable way to achieve comprehensive and equitable development through concerted and complementary action with other stakeholders in social and economic communities. Therefore, our ongoing support for community credit organizations and their partnerships is indispensable to the continued success of their missions.

[14] CALMEADOW, 8–12.

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Our thanks to

Reseau d'investissement social du Québec (RISQ)
and
FondAction (CSN)
