Small Business Promotion and Microlending:

A Comparative Assessment of Jamaican and Israeli NGOs

by Benson Honig

Abstract: Loan programs in two different countries, Israel and Jamaica, are compared and contrasted, in order to identify common elements of project design, selection, and institutional norms. Utilizing agency theory, this article examines what types of borrowers successfully navigate the credit market and to what extent the bureaucratic processes employed by institutions influence and bias outcomes in unpredicted ways in organizations.

Entrepreneurs are well recognized as coming from a wide range of backgrounds; indeed, it is the very heterogeneity of their origins that allows many to provide the newness of perspective so necessary for their activities. However, hidden or tacit institutional biases were found to work against this diversity, limiting severely the impact of efforts to sustain an entrepreneurial culture and to promote economic development.

The characteristics of the lowest level of organizational actor(s) were found to differentiate successful innovation from unsuccessful attempts. Selection of the appropriate staff was found not only to influence the qual-

ity and nature of the tasks assigned, but also the very direction and choice as to exactly what the organization would do.

Introduction

The role of small scale industries in providing employment has increasingly become of concern to policy makers, donors, and researchers. Millions of people in developing countries produce a wide variety of goods and services, often operating out of makeshift locations and under severe resource constraints. Financial services to support these micro and small businesses are becoming the preferred point of support throughout the developing and developed world. GEMINI (Growth and Equity through Microenterprise Investments and Institutions), ACCION, the Grameen Bank, and PRODEM, represent just a few of the better known NGOs (non-governmental organizations) engaged in such lending activities (Hossain, 1988; Lycette & White, 1989; Rhyne & Otero, 1994).

While lending activities have proliferated, research regarding both the outcomes and the processes has been quite limited. Evaluating the influence of credit on various businesses is extremely hard to assess—imputing how much of one firm's success can be attributed to financial resources, as opposed to entrepreneurial capabilities, market conditions, and other factors, is, at best, a dubious proposition. Most NGOs are obliged to report their comparative success in terms of default data; high repayment rates are considered a success, low rates a failure. While this information is useful to bilateral and multilateral donors, it fails to assess a number of more critical dimensions, particularly which firms are helped and how they are chosen. This is the research gap that this article will examine.

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Background and Theoretical Framework

Consultants, community development agents, and managers are frequently charged with the objective of implementing new programs across widely different cultural landscapes. In doing so, they face formidable obstacles in ascertaining programmatic quality and consistency throughout their organizations. Like the game "telephone line" many of us played as children, ideas that seem clear and succinct at the top of the organizational hierarchy become incomprehensible once they diffuse to the field. Multiple interpretations by employees of the goals emitted from the funding source or top of an organizational hierarchy undermine the potential for rational planned outcomes that reflect the unique environmental qualities of each particular situation. One further complication is that organizations use very different approaches to decision making. Managers at the top of the hierarchy who have a clear line of access to relevant field-level information maintain a distinct advantage over the competition—as do those with greater levels of trust in their subordinates.

While institutional theory suggests that much of what organizations do is shrouded in ceremony and myth (Meyer & Rowan, 1977), limited efforts are typically made regarding understanding the source or root of such institutional norms and values. Turning the organizational hierarchy upside down, I propose in this article that the employees of organizations determine goals that are subsequently legitimized or reconstructed by authority figures. In order to illustrate this assertion, let us turn to examples of organizations that work across wide cultural chasms.

The World Bank and many bilateral agencies, such as USAID, are leaders in promoting and diffusing a wide range of development programs focused on small enterprise promotion and support, primarily in less developed countries (LDCs). For many obvious and well-heralded reasons, bilateral and multilateral donors have a vested interest in ensuring that markets remain open, tariff and trade barriers reduced, and subsidies are eliminated. Supporting new and small businesses is often linked to these ubiquitous policies.

Historically, many developing countries have favored erecting protectionist market mechanisms, such as import substitution, in order to nurture specific industries, including many small businesses. As monetary and financial policies in LDCs increasingly move toward normative world practices promoting competitive conditions, many small businesses and subsectors have fallen victim to radical environmental changes over which they have little or no control. Not only do LDCs exhibit such swings, but so do small businesses in blighted urban areas of many developed country cities. “White flight” and the exodus of the middle class, industry, and accompanied service and retail facilities often render them susceptible to exogenous factors out of their control. To help ameliorate some of these conditions, considerable efforts continue to be made to assist small businesses in economically depressed environments. Well-known examples include the Grameen Bank’s work in Bangladesh, ACCION in Latin America, multiple efforts in Eastern Europe and Africa, as well as the Small Business Administration (SBA) and other regional organizations in urban areas of the United States.

One very popular method of mitigation is to provide targeted assistance toward employment generation and small business adaptation schemes. Indeed, the World Bank proudly proclaims that they have provided many millions of dollars to microbusinesses, and USAID, likewise (under specific direction from Congress) claims to have provided considerable sums to small businesses, while the SBA in the United States had US$15 billion outstanding in over 100,000 loans to small businesses in 1993.

Worldwide, the two most common forms of assistance include small business/entrepreneurial training programs and microlending, of which the latter is the most prevalent. Small loans are popular for three main reasons:

1. They are fairly easy to monitor, in terms of distribution and default rates.
2. They are thought to require limited overhead and staff support.
3. They fulfill a specific need often mentioned by small business persons; namely the limited availability of capital from the traditional banking institutions, who are otherwise inattentive to small and microbusinesses and their financial requirements.

In the 1990s, targeted assistance was rarely a strict bilateral arrangement. As with many private and government organizations that have delayered and now out-source much of their noncritical activities, the aid industry increasingly relies upon outside contractors to perform the "nuts and bolts" of day-to-day operation in the field.

The development industry itself relies upon armies of consultants who are recruited on an ad hoc basis, sometimes taken from larger organizations that can no longer justify their overhead. Behind the rather large sums of money dedicated to small business development are consulting firms (sometimes referred to as "beltway bandits" in Washington, D.C.) located in capitol cities throughout the developing and developed world. Each agency caters toward a number of constituencies, each representing a requisite number of experts as well as policy makers with individual and collective agendas that may diverge from the economic criteria or from the donor at large (Hancock, 1989). Included are issues that may exist far afield of general business promotion, such as factors relating to gender, class, ethnicity, mobility, democracy, education, and free-market capitalism.

Once consultants have been identified through competitive bidding on the part of agencies, they are frequently sent to work with NGOs and with governments. These institutions exist with histories of their own—separate and unique from that of the donors and consulting agencies. Depending on their organizational cultures, they, too, focus on issues tangential to general business promotion, including factors relating to political partisanship, regional politics, gender, ethnicity, class, mobility, democracy, education, and free-market capitalism, to name but a few.

Finally, at the lowest level—at the point of contact between the aforementioned donors and agencies, and the actual client—exists the actor or development agent, whose role might be further defined as a trainer, educator, loan agent, representative, or program director. While the governance and bureaucratic nature of an organization may be determined by their historic development, or by governmental regulation, development agents are often in a pivotal position to affect outcomes due to individual bias and preferences. In many developing countries, actors may be governed by reciprocity, as characterized by personal market exchange, rather than by impersonal markets (Plattner, 1985). Relationships are long term, open-ended, and governed by noninstrumental components. Asymmetrical and imperfect information, as well as weak legal protection, contribute to this characteristic, as loan agents know little of the backgrounds of the people they assist, and they have limited enforcement mechanisms (Stiglitz & Weiss, 1981).

At the micro level, self-categorization theory provides a useful psychological framework for understanding relationships that evolve between the various actors. Individuals attempting to maintain high self-esteem are said to identify themselves into in categories such as age, race, status, and religion (Turner, 1987). For example, one study demonstrated that in-group members consider out-group members as less trustworthy and less honest (Brewer, 1979). From an individual standpoint, attributes of the organizational members at the "point of contact" will have a significant influence on the character of the clientele, regardless of the organizational structure or its governance. In situations where information is lacking and results are stringently adhered to, developing biases in favor of clients that resemble the development agent may be a useful survival strategy.

Theoretical Perspective: The Organization in Combat

Collective members of organizations typically set goals, make decisions, and implement strategies. The character, conditions, and methods of these processes continue to be hotly contested in the literature, which acknowledges the limited rationality of actors constrained by numerous variables forced to make decisions in a limited time frame (Simon, 1957; Steinbruner, 1974). In addition, international dimensions, resulting from the incorporation of actors representing various cultural and nationalistic perspectives, further compound organizational complexity (Hambrick, et al., 1998; Hofstede, 1980; Boyacigiller & Adler, 1991); however, space limitations prohibit an adequate discussion in this article.

To understand organizational decision-making from a more pragmatic perspective, let us move to a very constrained and structured organizational process: consider a military operation during the heat of battle. At the start of a war, commanding generals are typically in clear communication and control of their troops. They carefully lay down specific goals and objectives: "Take this territory," "Break through defenses here," "Proceed to this point," etc. As the war progresses, communication becomes disorganized, infrequent, and increasingly incomprehensible between the field and headquarters. Reporting becomes sporadic, the big picture appears quite fuzzy, and the original goals and objectives increasingly appear irrelevant, as the enemy reacts to the situation at hand and changes their position in real time.

In the field, meanwhile, small units, controlled by individual actors, are facing a barrage of stimuli possibly in direct contradiction to what was specified they would face in the original operational plan. These units have two alternatives: They can stick to orders, regardless of the irrelevancy of the original plan, or they can form new objectives based on the situation they now face. The first alternative, that of proceeding with the original plan, may entail considerable risks. For instance, the movie *A Bridge Too Far*, depicts British field officers during WWII refusing to deviate from their initial plan, resulting in the unnecessary mass slaughter of their own troops. In marked contrast, acutely aware of the organizational hazards inherent in failing to adapt and modify plans, the Israeli army learned to train and refine its troops to make battle-level operational decisions “on the fly.” Such decisions are conducted at the field level, sometimes conflicting with, other times directing, real time operational plans at headquarters. This form of limited direction and field-level innovation worked exceptionally well against the Egyptian front in 1967, where, as one analyst reports, “Of the four days that the campaign lasted, only the first was planned in any detail; the rest was pure improvisation” (Van Creveld, 1985).

During the 1973 Arab–Israeli War, contradictory organizational goals, combined with ineffective and inefficient decision making nearly resulted in Israeli military failure. As Van Creveld (1985) summarizes, “During the 1973 Arab–Israeli War, contradictory organizational goals, combined with ineffective and inefficient decision making nearly resulted in Israeli military failure.” He continues,

> Instead of certainty being created by means of supervision from the top downward, uncertainty spread from the bottom up . . . . Deficiencies . . . included . . . a faulty command organization; a lack of mutual trust among the senior commanders involved; incompre-

> hensible staff procedures; and the absence of a directed telescope to supplement the flow of information from below by an active quest for it from the top. Without exception, these deficiencies were organizational in nature. (p. 230)

As with the Israeli military, many NGOs maintain broad goals and objectives and loose flexible command structures. NGOs in the small business sector typically have formal mission statements that are quite broad and nonspecific. These can be more or less summarized as "providing assistance to all worthy entrepreneurs and small businesses that would otherwise have difficulty obtaining resources," or something to that effect.

Unlike military operations, where there is generally a winner, or private business, where there may be multiple winners (or losers), NGOs operate in an in-between dimension of political appeal, public policy, and core values.

If we analyze the role of "bosses" (principals) and "workers" (agents) we may conclude that nonprofit organizations will have greater employee-shirking activity than for-profit firms (Alchian & Demsetz, 1972). This occurs because nonprofits have a characteristic separation between management decision-making and control, in that managers initiate activities that are implemented and monitored by others who bear the risks. In addition, the consequences of improved management cannot be capitalized for the benefit of shareholders (Fama & Jensen, 1983a; Fama & Jensen, 1983b). Thus, the failure to institute appropriate monitoring procedures will be of even greater consequence with NGOs than for-profit-making organizations. From a military perspective, imagine generals forced to hire mercenaries whose pay and performance are determined by politicians, based on an array of potentially contradictory goals and outcomes.

The theoretical basis for the NGO comparison in this article utilizes agency theory (Jensen & Meckling, 1976). The director of an NGO is essentially the agent of the bilateral or multilateral funding agency, who serves as the principal, while, simultaneously, the director, acting as a principal within his or her own organization, employs agents to carry out the tasks of identifying, training, and approving clientele. Conflicts and discontinuities arise when the interests of principals and agents diverge. In this research, the organizations studied were primarily not-for-profit institutions, further distorting the relationship between the two levels of principals and agents—the donor community, and, within the organization, the internal management structure. As agency theory predicts that nonprofit organizations will have greater shirking activity than for-profit firms, the failure to institute appropriate monitoring procedures will be of even greater consequence (Zimmerman, 1979). How can this be overcome?

Comparative Framework: Israel and Jamaica

In this analysis, loan programs in both Jamaica and Israel are compared and contrasted. Minority microlending in both countries is quite limited, allowing for a fairly representative and comprehensive comparative analysis.

The Center for Jewish–Arab Economic Development has been operating a revolving loan fund for Israeli Arabs and Palestinian citizens of Israel since 1991. It is the only one of its kind in Israel and was started to provide opportunities for small business in the Arab sector, which commercial banks viewed as either too costly to evaluate or otherwise too high a risk. The organization has focused on loans to small, innovative Arab businesses that have little equipment or property to utilize as collateral. It has lent approximately US$650,000 to 26 businesses, with an average loan size of US$25,000. The organization provides extensive business and marketing training and maintains a very low default rate. For this study, more than one-half (14) of the 26 firms that received loans were interviewed at their locations in Israel. In addition, extensive interviews were conducted with each director and with individual loan agents, regarding the goals and process of their lending activities. In Israel, the owners of businesses in half of the loan portfolio were interviewed at their business location. An analysis was made of the portfolio as to the relative affluence, need, educational criteria, and gender of the clientele. Following the field study and analysis, a meeting was held with all the principal employees and managers of the NGO, and a survey instrument translated into Hebrew was distributed.

In Jamaica, the unavailability of credit to the informal sector is frequently cited as a major impediment to the operation and growth of small firms (Anderson, 1992; Dessing, 1990; Davies, Fisseha & Kirton, 1981; Lubell, 1991; Lycette & White, 1989; Statistical Institute of Jamaica, 1993). Although theoretically there are several potential sources of Jamaican credit, including banks, microenterprise lending agencies, family, and informal credit arrangements (partnerships based on cooperative lending pools), the limited scope and availability of such monies for Jamaican microentrepreneurs are widely acknowledged, and practical alternatives are few (Anderson, 1992; Statistical Institute of Jamaica, 1993; Honig, 1998). This dearth of institutional credit has been recognized by bilateral and multilateral institutions such as the International Labour Organization (ILO), USAID, and the World Bank. Beginning in the 1980s, they have undertaken to develop, promote, and support several credit institutions whose primary directive is to provide credit to Jamaican microenterprise.

A commercial credit union, as well as four different NGOs provides microloans in Jamaica, subsidized by USAID, the Dutch and Canadian governments, and other bilateral and multilateral agencies. As in the case of the Israeli NGO, each organization was evaluated and interviews were conducted with management, as well as the lending staff. Another 74 firms, randomly selected from the clientele fosters of all five microcredit agencies, were visited on site and interviewed. Loan portfolios of the different institutions ranged from US$100,000 to US$2,000,000, and average loan sizes ranged from US$600 to US$5,000. They had been in existence from between 2 to10 years, and four of the organizations provided business and marketing training, as well as credit facilities.

Findings

The examination of the clientele of a number of NGOs in the two different countries found individuals who did not match the broad organizational criteria of severely limited resource constraints. Many of their clientele were found to be either individuals with considerable access to alternative capital or those chosen by arbitrary criteria that failed to match the overall organizational goals of access and meritocracy. In Jamaica, for example, one firm was found to have borrowed a considerable sum (US$150,000), despite its not meeting any objective criteria as to size (this large factory had over 25 employees). Discussions with the loan agent indicated that the firm was chosen because of the reliability with which it could repay the loan, rather than on the criteria of need. The owner of the firm had extensive working relationships with banks and was utilizing the microloan program because his loan was subsidized at a below-market rate.

The Israeli NGO staff were found to be surprisingly ignorant of the character of their own loan portfolio. For example, six of eight reporting staff members (75%) thought that the average starting capital for the businesses they lent to was under US$15,000, while the mean for the sample was three times that figure (see Table 1). Four of seven reporting staff members (42%) thought they were helping more women than men, despite a loan portfolio of 93% male entrepreneurs. Most significant, seven of the eight staff members (87.5%) thought they were loaning to individuals who had no other credit alternatives, while 53% of the firm owners indicated that they had other credit alternatives but were using the loan fund because it provided credit at comparatively favorable rates.

The NGO

The NGOs in Jamaica exhibited similar dissonance between stated goals and empirical reality. A systematic comparison of the organizations' clientele showed that they tended to rely upon specific strategies or specializations, without being institutionally aware of their biases. Marital status, education, gender, and religiosity all appeared to be operating as credit rationing devices for the different NGOs, but the rates of usage varied considerably (Honig, 1998). For example, one agency was found to be lending substantial sums, well in excess of their official ceiling, to a large successful manufacturing firm. The owner of the firm, a millionaire, admitted that his attraction to the organization was only to obtain substantial credit at subsidized rates—he had many alternative sources, including major banks. To supplement their portfolio, this NGO lent a number of microloans to "model" firms, who were used as showcases during the appropriate international forums and inspections. This strategy allowed them to gain a reasonably high assurance of repayment, while also providing them with sufficient multilateral compliance, in the form of their model firms.

As with the initial plans before entering combat, the NGOs in Jamaica devised clear and explicit mission statements, charters, and business plans. Evaluating this formal documentation and analyzing the interviews conducted with the managing directors demonstrated how similar the formal stated organizational goals were between the different agencies. This was not too surprising, as there was considerable scope for interaction during joint inter-agency training programs conducted for loan officers, as well as career movement by management between the various organizations. For example, consider the following statements from the managing directors of the agencies, when asked specifically about their goals and objectives:

"The primary purpose is to provide . . . working capital and fixed assets as well as any type of temporary assistance they would require in order to start or upgrade [their microenterprise]."

"To equip people in the small and micro sector to come in 'mainstream' by offering financial and technical assistance."

"To provide credit and to provide technical assistance . . . to the smaller microentrepreneurial sector."

"We are a credit agency . . . We see ourselves more as a [community] developer."

Thus, while the organizational literature provided by each of the five agencies was remarkably similar, their practices were found to differ widely. In most cases, relevant literature, policy statements, and even applications could be freely exchanged between organizations with little or no obvious impact or conflict. Despite their similarity, however, they deviated widely from each other, and from their own organizational goals. How did this come about?

Conclusion

Having carefully studied a number of microlending organizations in both Jamaica and Israel, it became increasingly apparent that organizational objectives operating at different levels prevented institutions from doing what they claim they had set out to do. Further, it became apparent that a "bottom-up" type of strategy was directing the activities of these organizations, largely unbeknownst to the directors and managers. This observation is likely to have parallels elsewhere, particularly in sit-

Table 1: Israeli NGO: Expectations Versus Reality

	Expected By agency personnel	Actual Reported by owners
Firm Owners who have NO credit alternatives:	87.5%	47%
Number of employees between 2–5	87.5%	61%
Anticipated the correct percentage of Firm Owners with a College Education (25% to 50%)	62%	29% had a college degree
We help women more than men	42%	93% male clientele
Estimated Average Starting Capital of US$15,000 or less	75%	59% had starting capital over US$15,000; mean of US$40,000

uations that result in multiple and conflicting goal designations. For example, transnational firms set goals at the macro organizational level. These goals may conflict with regional or local objectives and may also contradict individual managerial or employee incentives and wishes. This competition between mutually exclusive objectives invariably leaves the employee in the "driver's seat" regarding which way to navigate the resulting confusion. The outcome is not necessarily beneficial.

Studying the process by which these monies are distributed is critical to understanding how goals and objectives are redirected and it may prove illustrative to many other organizations. Examining decision-making processes in both Israel and Jamaica suggests that too little attention is placed on the character of the implementing actors—the employees themselves. An extensive body of literature exists studying the nature of leaders, leadership selection, organizational culture, methodologies, and processes. While leaders themselves tinker with new methods of communication, incentives, and organizational structures, this article argues that it is the character of the lowest level of organizational actor(s) that differentiates successful innovation from unsuccessful attempts. Selection of appropriate staff thus influences not only the quality and nature of the tasks assigned but also the very direction and choice as to what exactly will be done. This is particularly true when goals and objectives are either vague or in conflict with other incentives or individual predilections.

In contrast to what usually occurs, foreign donors often require their principals (managers, representatives, consultants, etc.) to avoid selection criteria on the basis of financial or embedded relations. Such requirements are in place in an attempt to maximize the potential for economic development and avoid accusations of partisanship or nepotism. The NGO managers are thus left in a quandary—how to maintain low default rates, which are carefully monitored, while lending to individuals for whom they have little information. This research suggests that the dilemma was solved as managers provided their loan agents significant leeway in the decision-making process. The loan agents, acting without extensive monitoring and control procedures, characteristically relied upon informal networks, signaling, and in-group characteristics in order to identify reliable clientele. As a result, the organizations tended to conform to a selection process focusing on specific indicators targeted by the loan agents, rather than by the principals and donors. In some cases education was found to be crucial; in others, religiosity was a more important selection mechanism, each presenting an organizationally viable, if somewhat subversive, element to the decision-making process. This suggests a relationship between the tacit, or undisclosed, criteria and the organizational goals and objectives, even when those goals and objectives are not explicitly defined or codified. In these cases, in-group affiliation may be the most salient governing process.

Such decision-making biases, if left unchecked, are certain to have significant long-range outcomes that may even undermine the very activity supported by these institutions. Entrepreneurs are well recognized as coming from a wide range of backgrounds—indeed, it is the very heterogeneity of their origins that allows many to provide the newness of perspective so necessary for their activities. Hidden or tacit institutional biases may work against this diversity, limiting severely the impact of efforts to sustain an entrepreneurial culture and to promote economic development.

Microenterprise credit agencies would be well advised to pay careful attention to the characteristics of their loan agents on a range of dimensions including gender, education, social capital, Socio-Economic Status, and religiosity. Devising monitoring and incentive systems that closely parallel the objectives of the organization are particularly important and appear to have been absent in the case of the many NGOs studied. Failure to introduce new systems may undermine the targeted goals of microlending, while attention to these details should result in greater overall efficiency and programmatic consistency.

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