Bridging the Gap with Social Loans

Based in San Francisco, Mission Asset Fund (MAF) is a nonprofit organization dedicated to helping low-income, financially excluded consumers enter the mainstream financial system. One of MAF’s most successful initiatives is their Lending Circles program.

Lending Circles is a social loan program modeled after the peer-to-peer lending practices often found in low-income and immigrant communities. Informally, a social loan involves a group of people who contribute money into one fund that is shared among each member. MAF’s innovation is to formalize the practice and convert that social loan into transactions recognizable by the credit bureaus. The program allows consumers with nonexistent or sub-prime credit scores to establish a credit history as well as improve their credit standing.

The social aspect of the program has been one of the keys to Lending Circles’ success.

“Our participants rely on one another,” said Tara Robinson, MAF’s communications and development director. “They get to know the people in their circle and create a sense of community.”

Some clients enter a circle already knowing their fellow borrowers, while others are matched by MAF. Clients who do not know each other at first often become acquainted at MAF’s offices, giving them direct contact with the people involved in their loan and increasing their sense of responsibility to adhere to the repayment schedule.

“Meeting face-to-face and a strong sense of community is what underscores the high-rate of repayment,” said Robinson. “Our repayment rate is 99%.”

The Program Structure

After forming a Lending Circle, each borrower signs an official Promissory Note and begins making online payments. If five borrowers, for example, contribute $100 per month, each borrower takes their turn receiving the total loan of $500. MAF reports payment transactions to the credit bureaus, allowing borrowers to increase their credit score. MAF does not charge interest or fees. If a borrower must drop out of the circle, MAF steps in to take their place, ensuring that all obligations are met. MAF complements the loans with mandatory financial education classes.
Does the model work? Starting in 2010, MAF conducted a two-year study of 347 consumers. The results are telling. While the 138 participants in the control group (who were not part of a lending circle) increased their score from 456 to 497, a 41-point increase, the group of 209 participants who engaged in lending circles increased their average credit score from 435 to 603, a 168-point increase. Similarly, the outstanding debt of the control group **increased** by $2,911 on average, while debt for the treatment group **decreased** by an average of $1,051. By the end of their lending circles, borrowers’ average credit score was 603 points.

The study revealed that for people with no credit history, Lending Circles allows them to establish credit and reduce their debt. For people with an already established record, the program helps them get a better handle on their financial situation while reducing their outstanding debt.

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**How does a Lending Circle work?**

1. Each month (→) members of the circle contribute a predetermined amount to the fund.
2. Each month 1 member of the circle receives the sum of the contributions.
3. Each month successful contributions are reported to 2 of the major credit bureaus.
The Impacts

The impacts of Lending Circles are direct and long-lasting. Many fledgling entrepreneurs have been able to start their own businesses for the first time after borrowing seed money and building credit. Borrowers with existing businesses have used their loans to buy new equipment, upgrade their infrastructure, and expand their capacity. Others have used their loans to pay down high-cost debts, establish savings accounts, and fund college educations.

The program’s popularity has led to more specialized offshoots. In 2012, MAF created Lending Circles for Dreamers in response to a Department of Homeland Security directive known as Deferred Action for Childhood Arrivals (DACA). DACA allows young immigrants to obtain work permits and protection from deportation. Lending Circles for Dreamers organizes qualifying young people to lend and save for the application fee necessary to file for DACA through the US Citizenship and Immigration Services. MAF provides a one-third charitable match incentive. To date, 183 Dreamers have formed 17 Lending Circles.

In addition, Lending Circles for Citizenship enables immigrants to form peer lending groups to save for citizenship application fees while accessing a 25% matching contribution. To date, sixty participants have formed a total of ten Lending Circles for Citizenship.
The Future

Lending Circles has achieved such success that the program is being replicated in other communities. With financial support from CFSI’s Financial Capability Innovation Fund, MAF has partnered with six community organizations in California to extend the reach of the program. These organizations represent a diverse array of underbanked consumers, including low-income Chinese immigrants, Asian/Pacific Islanders, women, and families. Since September 2011, these six partners have facilitated a total of 256 social loans in 49 Lending Circles with a total loan volume of $186,150.

MAF is also taking Lending Circles nationwide by partnering with over twenty nonprofit organizations to offer the program in six states. More specialized programs are also in the works, including loans designed specifically for youth who are transitioning out of foster care facilities.

“We are also looking for new ways to take Lending Circles online and to scale,” said Robinson. “The program has been very popular. We want to accommodate our growing number of clients and help drive them toward financial capability.”

For more information about, or to partner with MAF’s Lending Circles, visit www.missionassetfund.org or www.lendingcircles.org.

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