

Experiences of Somali Entrepreneurs in the Twin Cities

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I. Introduction

There is a universal belief among Somali entrepreneurs in the Twin Cities that they can become rich very quickly; therefore, they need to hurry up and start their business so they can get to the Promised Land and strike a fortune in the process. This sometimes leads to jumping into business without thinking it through. There is no question that Somali entrepreneurs are ambitious and hardworking people. Some of them work more than sixteen hours a day in a full-time job and at the same time run their own business. What they have accomplished in less than ten years is quite remarkable. Somali entrepreneurs and other new immigrants, such as Latinos and Asians, are overwhelmingly responsible for revitalizing old and neglected commercial corridors in south Minneapolis, such as Nicollet Avenue and Lake Street, and University Avenue in Saint Paul.

In 1994 there were no significant Somali businesses to speak of in Minnesota. Today, we estimate that there are over 550 Somali-run and managed businesses in this state.¹ It is an amazing accomplishment for people who have been displaced by war and forced to leave their families, homes, and assets behind. The stories of Somali entrepreneurs in the Twin Cities are unparalleled and unique.

This brief essay highlights not only the visible business achievements of the Somali community in the Twin Cities, but also its shortcomings and what can be done about them. Throughout this essay, I focus on business cases. All of the people are real and these are the true

experiences of a number of Somali entrepreneurs in Minnesota. I will not mention specific names of the businesses involved in my examples or the names of the entrepreneurs who dared to start their enterprises in Minnesota. Otherwise, you will read the complete story. We have encountered these tales in our work with the African Development Center (ADC), which was founded just eighteen months ago.

The African Development Center is in the early stages of an experiment in helping African immigrants establish themselves economically in Minnesota. The ADC envisions an urban community in which African immigrants, African culture, Islamic law, American culture, and American finance can coexist in a mutually supportive and productive way.

Three questions are the focus of this discussion:

- A. What are the major challenges facing Somali entrepreneurs in the Twin Cities?
- B. What are the ways in which Somali entrepreneurs have dealt with—or not dealt with—these challenges?
- C. What are some recommendations for how government, economic development organizations, and financial institutions can assist Somali entrepreneurs in the Twin Cities?

II. What are the Major Challenges Facing Somali Entrepreneurs in the Twin Cities?

Five of the biggest difficulties that Somali entrepreneurs face in running their own businesses in the Twin Cities are:

- A. Lack of Forethought (Planning)
- B. Market Saturation and Isolation
- C. Wasted Wealth
- D. Financial Illiteracy/Lack of a Relationship with Financial Institutions
- E. Ignorance of Regulatory Requirements

The following examples of actual Somali business behavior will instantiate the difficulties and give them a human face. Each challenge will then be analyzed separately to aid in drawing conclusions.

Example One

This first case demonstrates how Somali entrepreneurs often raise equity, form partnerships, dive into untested waters, and avoid accounting practices. A restaurant in South Minneapolis that we worked with at ADC had three major partners. Each invested about \$35,000. Next the three approached family members as well as acquaintances and friends to invest in their new restaurant. The partners collected approximately \$300,000 from about twenty investors. None of the investors signed any document describing the nature of their investment or the expected return on the investment. The investors completely trusted the three partners and believed that they would get their money back with a decent return at some point in the future.

Actually, there was no written partnership agreement between the three main players in this deal either. No attorney was consulted on how to form a partnership agreement. Nothing was agreed upon on paper except to form a partnership and manage a restaurant.

None of the three main partners in this deal had any previous restaurant management skills in the United States or in Somalia. They just felt that the location of the restaurant was great and that customers would certainly come in and dine. However, some of the critical details they failed to consider were menu planning, market considerations, portion costs, pricing, layout, training outline, cash control, financial statements, job descriptions, job specifications, policy manual, equipment sanitation, and personal hygiene. Furthermore, the partners neglected to check with the Division of Environmental Health of the city of Minneapolis to find out if the restaurant they were purchasing was in good standing. The partners paid \$80,000 to the previous owner without any type of business valuation. They did not even ask for the financial statements of the business they bought. They felt that the business was worth \$80,000 and they paid with other people's money. Almost all of the investors in this restaurant lost their equity. The restaurant was sold to a new set of Somali entrepreneurs and the vicious cycle began all over again.

Example Two

This case highlights the lack of forethought in understanding the intended business or anticipating regulatory requirements. Across from one of the *Suuqs* in Minneapolis there is a Somali-owned store that sells

clothing and videos. Additional space became available in the building and the business owners decided to expand and add a coffee shop. They hired a contractor to do the remodeling. This contractor was not licensed with the city, nor did he give them a written bid outlining the costs. The business owners paid the contractor \$4,000 up front. Regrettably, the contractor did not obtain a permit from the city for construction and the project was forced to stop. The business owners were then paying rent without generating any income. They proceeded with the leasehold improvements using a different contractor but ran out of cash nine months after signing.

The entrepreneurs asked the building owner for a postponement of rent payment until they had a city permit to operate and were actually bringing in cash. Unsurprisingly, the owner refused. He reminded them of the lease agreement that they agreed to and signed.

The owners went to court. After many months of legal wrangling, the parties reached a negotiated settlement. The business owners paid \$18,000 of rent without opening the coffee shop. As of this writing, they are paying rent on the space and are still trying to open the coffee shop.

Example Three

The third case focuses on accounting issues. A very successful food distribution company operates in Minneapolis, supplying many of the *Halal* markets in the metro area as well as many restaurants. The company contacted ADC for assistance with a cash flow issue. The terms under which they pay their vendors average 15 to 30 days. The term they extend to their customers is 30 days. However, most of their customers in reality pay in 45 or even 60 days. This creates a cash flow problem and limits their ability to finance the inventory.

The company provides meat that is slaughtered according to Islamic guidelines. Consequently, it must follow special rules for financing as well. A form of Profit Based Islamic Financing would be ideal but this does not currently exist for working capital issues. In addition, the company's financial package was not properly set up and had to be changed. ADC is still working with this client to ensure that the owners are capable of reading their financial statements and making sound business decisions based on their accounting records.

Example Four

The fourth case is a classic one. Two Somali entrepreneurs from greater Minnesota decided to open a gas station/convenience store. The site that they chose had been a full service gas station with mechanics performing repairs on site. They negotiated and signed a lease with minimal legal representation (a staff attorney from a law center).

They had conversations with city officials about the use of the site but did not get detailed information about regulatory requirements. No business plan was prepared. In addition, there were no written bids to estimate the total cost of transforming a space that had been exposed to toxic chemicals into a food safe environment. After almost \$40,000 had been spent on sporadic remodeling, the entrepreneurs contacted ADC.

ADC quickly determined that the lease had major flaws. The start-up was undercapitalized, city regulatory requirements were ignored, and the business owners had no relationship with local financial institutions.

The lease term, three years with a one-year option, was too short to allow for standard five-year financing arrangements. Even worse, however, the lease made the business owners liable for site clean up of any hazardous contamination without evidence of the condition of the site at the time the lease was signed. It also did not address spillage problems that could occur from the underground storage tanks. Several months after the lease was signed, the business owners became aware of an investigation by the Minnesota Pollution Control Agency (MPCA) of a spill that occurred before the date of the lease.

After spending a large sum of money on remodeling, the business owners learned that the city would require them to have bathrooms. They had talked to city officials but had not come away with a clear picture of city requirements. Having started with too little cash and having to reconstruct and add to the scope of the remodeling, their ability to open the business became questionable.

In addition, the owners had raised capital entirely from family and friends and had no relationship with local financial institutions and no partnership agreement to help them move forward. ADC contacted the MPCA and helped the business owners renegotiate their lease to alleviate their liability for the previous environmental contamination as well as to reduce payments during remediation. Unfortunately, the remaining issues are as yet unresolved.

Example Five

This is the story of an ADC client who is a successful businessman. He currently owns two gas station/convenience stores and one *Halal* market. He recently purchased a building in which he plans to open a full service grocery store and office space for lease. This man understands the American financial system very well. He has obtained capital to finance his operations from a variety of sources: conventional lending, economic development funds, and private investors. Financial statements and tax returns are central to his planning. ADC has prepared business plans and financial projections as well as put together loan packages at the request of this businessman. The contractors he uses are licensed and at least two bids are always obtained before work is begun. He has a good relationship with city inspectors. The markets he targets are not just Somali but anyone who passes his doors, and he tries to appeal to people from many cultural and ethnic backgrounds.

Not only is he a good businessman but he also invests in his community. There are many examples of his hiring young people, training them to run the different aspects of businesses, investing in their businesses, and helping them become independent. He is truly an asset to the community. This entrepreneur seems to follow the established “best practices” of American business.

A. Lack of Forethought (Planning)

1. Naïve Misperception about Business Success

The lack of planning is one of the major reasons that most small businesses fail. According to the Small Business Association (SBA), over 60 percent of small businesses fail within the first three years.² This is largely due to inadequate planning and undercapitalization. No statistics are kept on the number of businesses started by immigrants nor on the number of failed businesses owned by immigrants. Arguably, though, the failure numbers are much higher for people whose first language is not English and who were not raised in the American business culture. Thus, planning and access to capital are critical to Somali and other immigrant businesses.

The nearly universal belief among Somali entrepreneurs that they will become rich very quickly if they can only open a business often leads them to jump into a business venture without thinking it through.

While this underscores great creative energy and a strong work ethic, it is also a source of overconfidence that overlooks the necessary preparation for a venture.

2. Source of Capital

Somali entrepreneurs tend to raise capital mainly from family, friends, and acquaintances, with no discussion about the rate of return or conditions of repayment. Investors, therefore, exercise no underwriting control over the project. The entrepreneur has no need to prove the validity of his or her intentions, and is not required to produce a business plan.

Somali entrepreneurs are relationship-driven people. They like to intimately know the person with whom they are dealing. For the most part, they are very warm, forthcoming, and welcoming. In addition, they like to avoid any type of contractual business agreement and paperwork if they can. One handshake is enough, as far as they are concerned. They prefer informality in their businesses dealings. In the business world of Somali entrepreneurs, it is not what you know, it is who you know and who you trust. Had the Somali entrepreneurs accessed capital in a conventional way, they would have had to produce, at the very least, financial statements, a business plan, and a valuation of the current business.

3. Expertise in the Business at Hand

Somali entrepreneurs are often willing to open a business without any knowledge of, or experience with, the product. For instance, restaurants, bakeries, and groceries have been started by many people without prior knowledge or experience in the food industry.

4. Lack of Financial Projections

The process of raising and spending money occurs without understanding the reality of the potential income from the business. Even when the business is up and running, accounting is limited to counting the money in the cash box. Cash flow, income, and balance sheet statements are rare.

B. Market Saturation and Isolation

1. *Too Many Goods Chasing Too Few People*

Somali entrepreneurs all tend to open the same types of businesses, such as grocery stores, restaurants, and clothing stores. They also tend to focus exclusively on their own ethnic group. For example, if a white woman walked into a Somali restaurant, she would be viewed as if she's from Mars: "What is she is doing here? Does she not know we only sell to Somalis? How do we serve her? What does she want? Who can help her? Who can accommodate her in her own language?" These thoughts would race through the mind of the owner(s) of the restaurant. There are, therefore, few Somali businesses that break into mainstream markets.

Numerous Somali retail businesses in different commercial corridors in the Twin Cities area sell the same products. Sometimes you will see three grocery stores on one corner, or more than a dozen Somali women's clothing shops in a small Somali mall.

2. *Suuqs*

Marketplaces are opened without adequate planning for what will be sold in each shop. Then additional *Suuqs* are opened with many of the same products. The proliferation of *Suuqs* is not, therefore, a sign of the expanding availability of products or of widening prosperity. The following are all Somali or African malls in the Twin Cities:

- Caramel Mall, Lake Street and Pillsbury: 55 businesses
- Lake Plaza Mall, Lake Street and 5th: 45 businesses
- The Village Market, 24th and Elliot: 65 businesses
- The African International Marketplace, Highway 280 and University: 48 businesses
- Somali Mall, Cedar and Riverside: 30 businesses³

The landlords of the Somali malls in the Twin Cities benefit tremendously from the hard work and sweat equity of the Somali entrepreneurs who do business in these malls.

C. Wasted Wealth/Personally Subsidized Businesses

The use of the personal savings of both the business owners and the informal investors who help finance them is a great resource for Somali entrepreneurs. However, if this investment is lost, as it often is, these personal savings are lost to both the individuals and to the community. Invested more wisely, these personal savings would build wealth and contribute to the long-term prosperity of the community.

In addition, business owners who recognize that they are losing money often get another job to subsidize the business or recruit family members to work free of charge in the business, rather than close down the operation. This commits even more earning power to questionable use, resulting in a net loss of wealth to the community, both in capital and productivity.

D. Avoiding Financial Institutions

Most Somali entrepreneurs in the Twin Cities area are Muslims. The Quran forbids usury so many Somali entrepreneurs avoid receiving or giving interest. Therefore, they don't deal with banks and financial institutions effectively. The ability to raise cash from family and friends means that entrepreneurs can get started without banks but their companies are usually undercapitalized. Somali entrepreneurs really struggle with working capital for their businesses. After the initial equity injection, they will need some form of permanent working capital investment because they cannot turn their receivables and inventory into cash quickly enough to cover their operating cycle gap. For the most part, their accounting system is nonexistent or weak. Consequently, they cannot approach banks to get permanent financing like a term loan.

Somali entrepreneurs not only avoid banks because of the interest charged but also because their business may lack an accounting system. This leads to a dependence on cash transactions. Combined with avoidance of accounting and ignorance of regulatory requirements, this leads to big trouble with the IRS and the State Revenue Department. A time bomb is ticking for many businesses, for example the clothing businesses in the Somali malls.

E. Ignorance of Regulatory Requirements

Most Somali entrepreneurs have a hard time believing that American regulatory systems work the way they do. Even when they have a vague idea of the requirements, they tend to expect more flexibility and idiosyncratic interactions from the system. They are usually shocked when they learn about what is required, often only after making a mistake. This holds for everything from building codes to IRS payroll reporting requirements. This ignorance adds to the problem of jumping too quickly into business and adds to the cost of starting a venture.

III. What are the Ways in which Somali Entrepreneurs Have or Have Not Dealt with the Challenges that they Face?

For the most part, Somali entrepreneurs have not recognized the source of their problems. Some individuals cope better than others, however, because they are more open to getting assistance and are prepared to change. But the community as a whole is not even aware of the wasted wealth problem or why it's happening. There are three characteristic responses that perpetuate the difficulties: isolation, the revolving door, and subsidizing failure.

A. Isolation/Mistrust

Although Somali entrepreneurs are warm and welcoming people, they do not trust each other very much and have a hard time organizing their own business associations. They do not have a meaningful dialogue with each other, even if they are all part of a single mall, such as Lake Plaza on Lake Street or the Village Market at 24th and Elliot. Landlords at the Somali malls tend to take advantage of this lack of communication and unwillingness to form united fronts.

More importantly, this mistrust means the community as whole does not benefit from the experiences of individuals. Mistakes are repeated, and unfamiliar circumstances, including interactions with government and financial institutions, are avoided or ignored altogether.

The suspicion of each other also extends to people outside their communities. It is part of the reason there is an inherent mistrust of the American banking system and of governmental agencies designed to assist small businesses. This mistrust translates into business practices

that are not healthy, for instance working on a cash-only basis and not keeping good records.

Some community development organizations have conducted workshops for Somalis interested in starting businesses. They have also provided technical assistance for new and established businesses. Somali entrepreneurs who have participated in formal business planning classes or workshops clearly benefit from these programs, but many show little or no sign of actually acting upon the information. Too many Somali entrepreneurs still do not think through their options before they start.

Mistrust of the American business system in general also contributes to failure. Somali entrepreneurs often try to open businesses without much knowledge of the product they offer or the market they are targeting. They often enter markets that are already saturated and may fail to realize the potential of moving to more mainstream markets. They may not know how to make the shift.

B. Revolving Door of Partners

The informal nature of most Somali business partnerships exacerbates the fluid addition and subtraction of partners and helps mask the overall drain of wealth that occurs within the community. When partners find themselves losing money, they are usually able to find someone to buy them out or at least to take over the business, even though they know it is unprofitable. The new partners then discover that they, too, are losing money and find new partners. Each time this happens, new partners must find capital, often through informal capital contributions from family and friends, and additional wealth is drained from the community.

Partnership agreements are almost nonexistent and those that do exist generally do not have proper documentation. Little or no analysis of current business operations occurs either from current owners or future investors. Good financial record keeping is rare, which hampers any kind of discovery by potential partners as to the true nature of the success of the business. The result is the perpetuation of failed experiences.

C. Subsidizing Failure/Good Money after Bad

As business owners become aware that they are losing money, they tend not to analyze the reasons for the loss. Instead, they often respond

by spending more time on the business, enlisting help from family members, or even getting a part- or full-time job to help subsidize the business. The result is not only chasing bad money with good, it also wastes the time and energy of the individual that could be better invested in a profitable business or other employment.

Some Somali entrepreneurs deal with challenges by denying that the problems exist. They may also avoid working with the different levels of government and financial institutions. However, some Somali entrepreneurs have dealt with the challenges they face in conducting business in America quite well. Although they are in the minority, some entrepreneurs write a business plan, consult with attorneys, obtain bookkeeping services, and manage their businesses efficiently. Although they are the exception, they demonstrate that it can be done and they may be able to point the way for others.

IV. Recommendations for How Government, Economic Development Organizations, and Financial Institutions can Assist Somali Entrepreneurs in the Twin Cities

A. Government Agencies

Somali entrepreneurs have the potential to generate wealth for their families by their creativity, enterprise, and risk-taking. Therefore, government should create an environment in which Somali businesses and Somali families can dream and flourish.

Local governments can help these entrepreneurs by making the city bureaucracy more accessible and understandable. The cities of Minneapolis⁴ and St. Paul should try harder to help Somalis learn how to get permits and licenses for any type of business venture. Demystifying regulations and practices—such as rules for the construction and rehabilitation of buildings, land use requirements, health codes, landscaping, parking, and other environmental standards—would aid not only Somalis but others as well. In addition, local governments must hire qualified Somali-speaking professionals who can work with the ever-growing number of Somali businesses. The culture of every community does matter, and cities must think about how Somali culture views business and builds and manages assets.

B. Non-Profit Community Development Organizations

As mentioned previously, undercapitalization is one significant reason businesses fail. Economic development organizations must educate Somali entrepreneurs about funding processes as well as facilitate their access to capital. The African Development Center was created to do just that. Other organizations should also tackle these issues.

Economic development organizations as well as financial institutions could be helpful in developing tools like Profit Based Islamic Financing, which could bridge the gap between the Somali entrepreneur's culture and the norms of American business.

In addition to capital access, community economic development organizations must increase the Somali entrepreneur's understanding of the financial, legal, and regulatory aspects of producing and selling goods and services to mainstream markets as well as to other Somali and African markets. The basis of success in business is comprehending these issues.

There is a huge cultural gap between how Somali entrepreneurs start and sustain businesses and how community economic development organizations deliver their services. The development organizations must understand the culture of the Somali business community if they want to service it effectively. What this entails is hiring qualified and knowledgeable Somali-speaking professionals. There are hundreds of recent graduates from a number of colleges and universities in Minnesota who speak both Somali and English fluently. The new graduates must be welcomed into the field of community economic development in our state. They are the future of this state and this community.

C. Financial Institutions

Somali entrepreneurs have a general mistrust of the American banking system. This stems primarily from a lack of understanding of how the system works and why it is beneficial to them. Financial institutions must find ways to build trust. Communicating the benefits of banking relationships and finding ways to make the banking environment less threatening will work toward establishing a better and more trusting relationship with Somali entrepreneurs.

Since trust is the key to establishing a relationship with Somali entrepreneurs, the ability to enter into meaningful community dialogue about business-based wealth development and its pitfalls will

not occur unless mutuality is established. This dialogue should lead to more strategic individual decisions and a more broadly shared understanding of best practices for the real world of the Minnesota business environment. The journey could then lead to additional help in training, education, advocacy, and greater sensitivity among institutions to the special needs of Somali entrepreneurs.

Various institutions can assist Somali entrepreneurs by building the capacity of those who have demonstrated a willingness to work with Somali businesses. However, Somali entrepreneurs must also help themselves and each other. There must be an open dialogue among the entrepreneurs and the Somali community about their economic future and well-being in this state. Initiatives that support the development of Somali community organizations must be undertaken by the different levels of government, economic development organizations, financial institutions, and foundations alike.

In summary, government and private institutions can assist by understanding the cultural challenges of the Somali community, by hiring Somali staff, and by supporting efforts within the Somali community to promote a dialogue about the challenges facing Somali businesses and how best to respond. Only the Somali community can answer the basic questions involved in this complex cultural adaptation process: How should we change to become more successful in competitive America? How should we remain true to ourselves? ●

Notes

1. Survey conducted by African Development Center in 2004.
2. According to the Small Business Administration, its research predominately focuses on mainstream business.
3. Survey conducted by African Development Center staff in 2004.
4. The City of Minneapolis is developing a one-stop development service that tries to ensure quality development of property within the city through customer-focused delivery of plan review, permitting, and inspection services.