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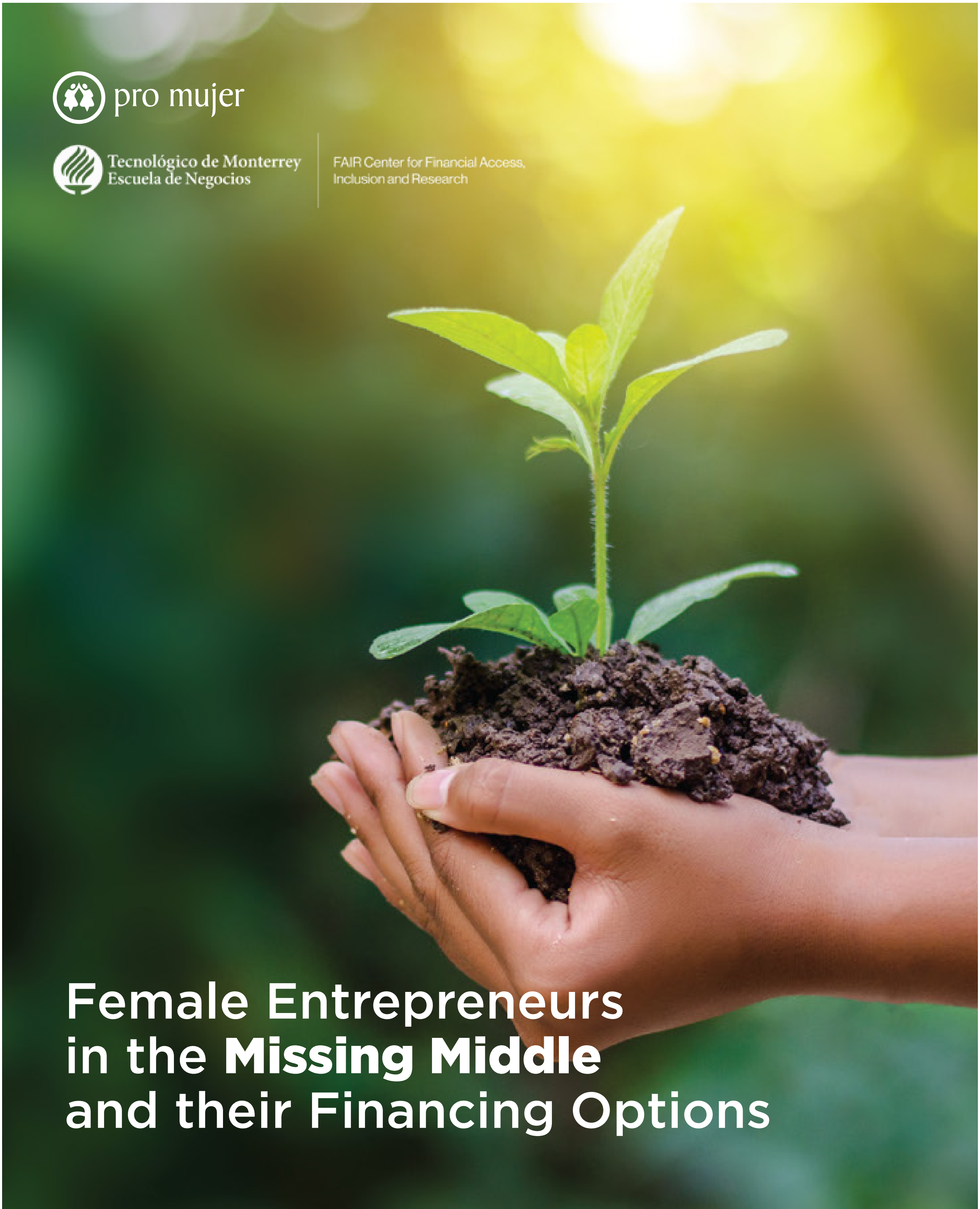

Female Entrepreneurs in the **Missing Middle** and their Financing Options

WOMEN FORWARD INTERNATIONAL

ZONA SHERO

Center for Inclusive Growth

Female Entrepreneurs in the **Missing Middle** and their Financing Options

Authors:

- Eileen Galvan Carvajal, Tecnologico de Monterrey
- Alexa Fernanda Villarreal Hernández, Tecnologico de Monterrey
- Dra. Luz Maria Velazquez, Líder de Zona Shero, Tecnologico de Monterrey
- Eva Maria Guerra, Tecnologico de Monterrey
- Luz del Carmen Diaz, Tecnologico de Monterrey
- Natalia Wills, Global Representative and Gender, Pro Mujer
- Monica Ducoing, Country Representative Mexico, Pro Mujer
- Fernanda Garza, Project Manager, Pro Mujer
- Felipe Perez, Director Fair Center for Financial Access, Inclusion and Research
- Marie Kate Palau, Project Manager Fair Center for Financial Access, Inclusion and Research
- Monica Arreola, Tecnologico de Monterrey

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Introduction:

Latin America has the highest number of female entrepreneurs in the world *(Global Entrepreneurship Monitor, 2020)***.** Despite the high percentage of entrepreneurship, there is a large financing gap, also known as: ***the Missing Middle.***

This gap has become a great challenge for female enterprises, since they are considered too large for microfinance loans but too small to obtain financing from commercial banks, risk capital or private equity. These venture capitals tend to focus on more established companies (World Economic Forum, 2021).

In Latin America, small and medium-sized companies play a fundamental role in the economy of their country, creating about 67% of job opportunities. However, their financial needs are often overlooked, since they receive only 12% of capital (World Economic Forum, 2021). Although the financing gap is a common theme in small and medium-sized companies, those which are led by women face greater barriers. The financing gap is estimated to be between US$10,000 and US$500,000 (World Economic Forum, 2021).

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There are various factors that limit the creation of an equitable financial and entrepreneurial ecosystem for women in Latin America, as well. Such as the lack of capital for women-led projects, gender and race discrimination, socioeconomic level, as well as the lack of access to products and services with a gender perspective.

This research demonstrates a deep understanding about the needs and gaps of women entrepreneurs whose companies are within the missing middle of Latin America, throughout the analysis of existent financial products from a gender lens perspective. The need of financial products with a gender perspective is clear through the qualitative and quantitative analysis.

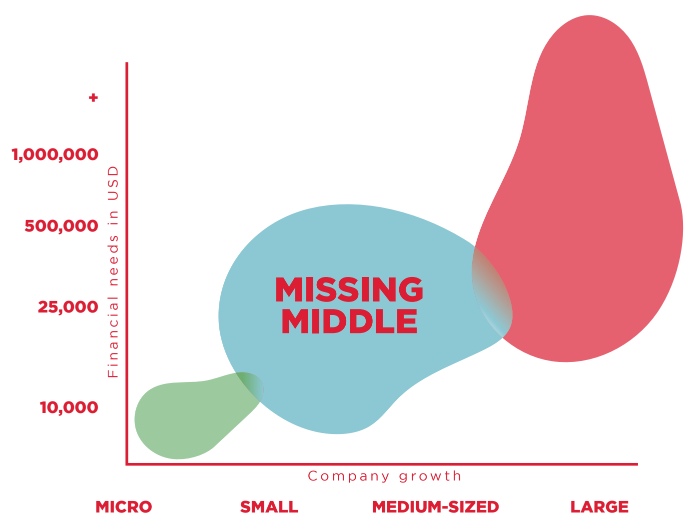
Micro and small companies predominate in Latin America, therefore, according to the Organization for Economic Cooperation and Development (OECD), they can be considered the basis of the economy of their countries. These micro and small businesses usually arise in family and local economies. The difference between a micro business and a small business lies in the number of employees they have, their annual earnings, and the contributed percentage to the country's Gross Domestic Product (GDP).

Micro companies are those that operate with less than 10 workers and generate profits of less than four million Mexican pesos per year. Although they make up 95% of companies in Mexico, they only impact 15% of the country's GDP. (Empresariales Magazine, 2021). Moreover, many of the micro-enterprises belong to the informal economy, employing 65% of the economically active population. The National Institute of Statistics and Geography (INEGI, acronym from the original name in Spanish) estimates that retail trade represents 25% of the activities belonging to this sector (2013).

On another front, small businesses employ between 11 and 30 workers and generate annual sales of more than four million and up to 100 million pesos. (Secretariat of Economy, 2021). Small businesses are usually independent entities that seek profit and develop their products or services within their community. They represent more than 3% of all companies and almost 15% of employment in the country; they also contribute more than 14% of the GDP (Secretariat of Economy, 2021).

Medium-sized companies are usually defined together with small companies, commonly called SMEs by their acronym. The definition of what type of companies are considered small and medium varies depending on each country. Medium-sized companies are those with more than 30 employees and produce more than 100 million Mexican pesos.

While micro-credits exist for micro-enterprises and investment funds exist for large companies, small and medium-sized companies suffer from a deficit in their financing offers. This gap is known as missing middle or missing middle segment. The term missing middle refers to the capital gap aimed to finance small and medium-sized companies (McKinsey Global Institute, 2019). This gap exists due to a lack of capital support for companies that are very small and therefore not considered sufficiently developed to attract the attention of private capital.



The capital needs of the missing middle estimates between US$10,000 and US$500,000. This financing gap is felt by 23% of formal micro, small and medium-sized enterprises in Latin America and the Caribbean (International Finance Corporation, 2017).

73% of small and medium-sized enterprises (SMEs) in Latin America that are led by women do not get sufficient economic resources to promote the growth of the company or are completely excluded from financial institutions. For micro-enterprises, the credit gap is US$5 billion while for small and medium-sized enterprises it is US$93 billion (International Finance Corporation, 2017).

The financing gap between large companies and SMEs was evidenced by a study reporting that in 2014 "*only 28% of banks worked with the sector because they considered it profitable or because they saw a business opportunity in it*" (Rojas, 2017). This perspective has been changing over the years, as in 2018 already, more than 75% of business investments in Latin America were for "*amounts less than $2 million dollars, with the majority ranging between $50,000 and $250,000 dollars*" (ANDE, 2020).

The same report indicated that the "availability of smaller investments does not necessarily mean that there is capital available for companies that are small and are in an initial stage" (ANDE, 2020). This causes a gap for SMEs, since most of the investments are directed towards large corporations or to micro-enterprises through micro-credits.

In 2014, OXFAM published a study about the difference in perception of Latin American men entrepreneurs compared to women entrepreneurs whose companies are in the missing middle. The most mentioned characteristic by investors and non-governmental organizations (NGOs) is that women entrepreneurs suffer from a lack of time compared to their male peers.

Those who belong to this gap or missing middle are usually Latin American companies founded by women, or with a shares ownership and participation of more than 51%, according to (2X Challenge, 2021).

The following graph shows fourteen characteristics according to impact investors and NGOs, distinguish Latin American women entrepreneurs from their male counterparts. Some of these characteristics can be considered as positive attributes, such as: greater tendency to collaborate, better ability to relate, and ease of teamwork. While others could be the cause of being in the missing middle, such as: less financial knowledge, less self-confidence, and risk aversion.

Characteristics of female entrepreneurs in comparison with male entrepreneurs: Themes emerged from interviews with Impact investors and NGO/Capacity developers

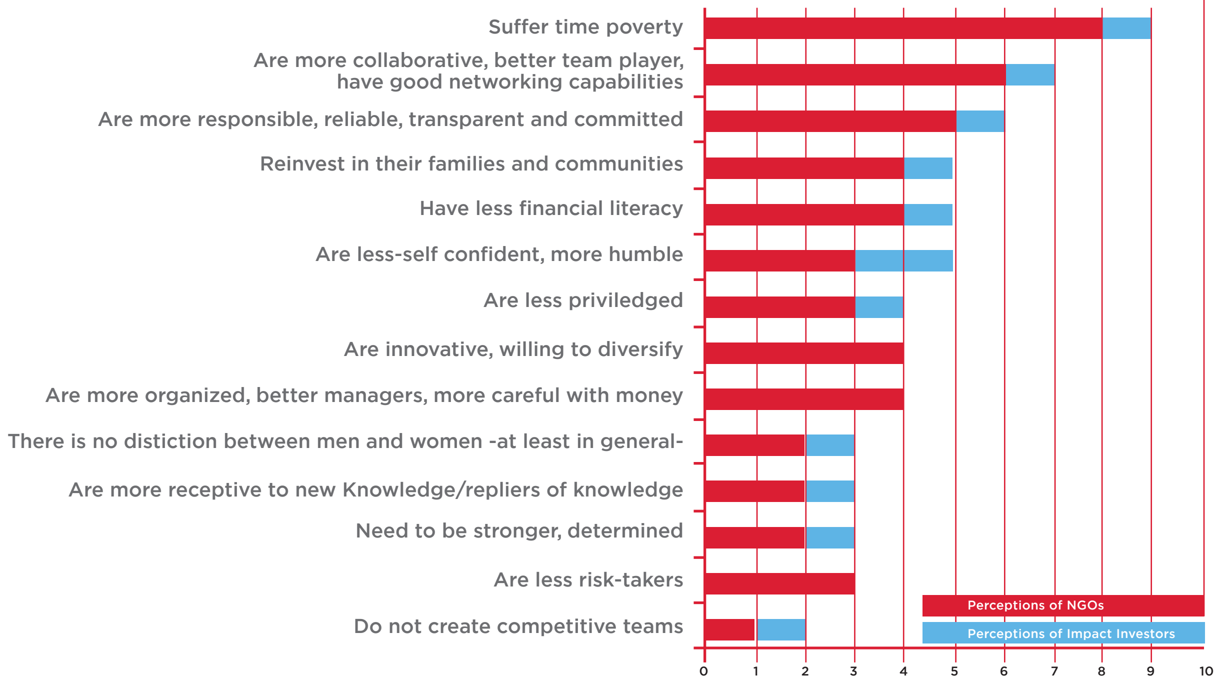


Figure 1. *OXFAM America, Value for Women, and Boston College. (2014). "The problem of underinvestment in Women Lead Small and growing business in Latin America and the Caribbean: The most Missing of the Missing Middle." Amazon:https://s3.amazonaws.-com/oxfam-us/www/static/media/files/The_Problem_of_Underinvestment_in_Women-Led_Businesses_in_LAC.pdf*

Many of these perceptions respond to traditional gender roles in Latin America, such as the relationship between the female gender and the lack of strength, security, and determination.

As well as the stereotype that a woman must first be a mother and wife and then an entrepreneur and businesswoman. Perceptions and gender stereotypes affect the participation of women in the business world. In Latin America, less than twenty percent of women venture into entrepreneurship. While men with an "entrepreneurial spirit" are between 25% and 30% according to 2019 data from the Global Entrepreneurship Monitor (GEM).

This same organization reported that business activity is linked to the education received. The Women's Entrepreneurship Report shows a disadvantage of more than 5% for women living in Latin America compared to men of the same age range (2019). This same trend is observed in the perception of opportunities to undertake. The conclusions of GEM is that women in developed countries are more likely to perceive entrepreneurship opportunities than those living in developing countries, such as the ones in Latin America.

The perspective of women entrepreneurs has led to hypotheses such as Lehman Sisters, explained in an article by the International Finance Corporation (2021). This hypothesis indicates that financial institutions are made up mostly of men, such as Lehman Brothers, who assume more risks and have accelerated financial crises. Instead, had it been made up of the Lehman Sisters and not the Lehman Brothers, economic crises might have not happened.

The concept that women evade risks is an unfounded stereotype that affects female entrepreneurs seeking access to investment mechanisms. Renee Adams, in her article for the International Finance Corporation, demystified the idea of risk aversion, since the data indicates that: women entrepreneurs or in managerial positions who have arrived on their own merits, act quite similarly to men when taking risks (2021).

While entrepreneurial women and men decide to take risks, they do so differently. Women entrepreneurs, unlike men, have fewer expectations when requesting financing for their companies (Adams, 2021). This could be a reason why in GEM studies they are considered "less self-confident" or derived from the fact that male entrepreneurs see themselves as equals to male investors, but this is not the case with female entrepreneurs before male investors.

A specific example of this is in Ecuador, where only 46% of women have access to and use financial products, while the percentage of men that do, exceeds 50% (UN Women, 2021). The same organization reveals that for every six Ecuadorian men who have a basic bank account, only four women of the same nationality own one.

In addition to having less access to financial products, there is the factor that women receive lower wages than men, so obtaining bank loans is more difficult to achieve. The amount of income that women can verify with their paid work becomes a barrier since they need to leave guarantees in case of accessing loans and these guarantees are usually owned by male relatives (ONU Women, 2021). The lower access to investments, or the *missing middle*, is notable in the study carried out by *Value for Women in Mexico* in 2019. A sample of 745 Mexican businesswomen was taken, highlighting that 42% have never applied for a loan. Whilst 70% of them seek financing for their businesses, more than half of them ask for amounts between US$6,250 and US$150,000.

The missing middle of financing suffered by Latin American entrepreneurs is solved with non-formal means, 55% of them through their personal credit cards (*Value for Women, 2019*). The respondents also reported that banks in Mexico give little follow-up to SMEs led by women. There is a lack of services designed with a gender perspective, and it is not easy to use methods such as *crowdfunding*.

Tec - Pro Mujer research

To lead to the development of new financial products for Latin American women entrepreneurs, we need to understand those who are in the missing middle to spotlight the financing gap.

With the support of the organization **Pro Mujer** and its representatives in Latin America, ten interviews were conducted with businesswomen who are in this missing middle in Mexico, Argentina, and Brazil. Bolivia, Peru, and Colombia.

At the same time, 280 online surveys were carried out on women entrepreneurs in the *missing middle* in Latin America to obtain first-level data that further details the shortcomings found by OXFAM and the United Nations. The sample had a confidence level of 95% and a statistical error of 5.85%.

This exercise was developed with the advice of professors from Tecnologico de Monterrey. The combination of qualitative methodology, with personal interviews and quantitative methodology with surveys, made a very complete study that affirms the conclusions found by international organizations. The first and most predominant result is that most women entrepreneurs in Latin America used self-financing as a financial instrument for the development of their business.

Secondarily, these entrepreneurs also receive loans from friends, donations, and financing from contests or calls. One of the ten businesswomen interviewed commented that "*I am paying everything with my personal credit cards and with what is generated we make a little fund, and we pay expenses. I have not taken a loan, nor have I applied for one -for entrepreneurship- because I have not thought it necessary*."

The sample had a trust evel of 95%
and a statistical error of 5.85%

The search for financial products outside the banks also responds to political instability, as mentioned by another entrepreneur who said, "*I am very afraid of tomorrow and of what may happen… not only in our country, but in the world, we are now living the consequences of our impediments as we experience shortages.*"

The ten entrepreneurs agree on two points in their search for financial capital and in what they want to invest it: advertising and marketing, as well as process automation.

The largest investment they need is on average US$200,000 for advertising, while for marketing it is US$20,000. The automation of processes estimates up to US$17,000.

More than 25% of those surveyed would use the capital to expand their business, followed by marketing and advertising.

Capital that Women Entrepreneurs Need to Develop their Business

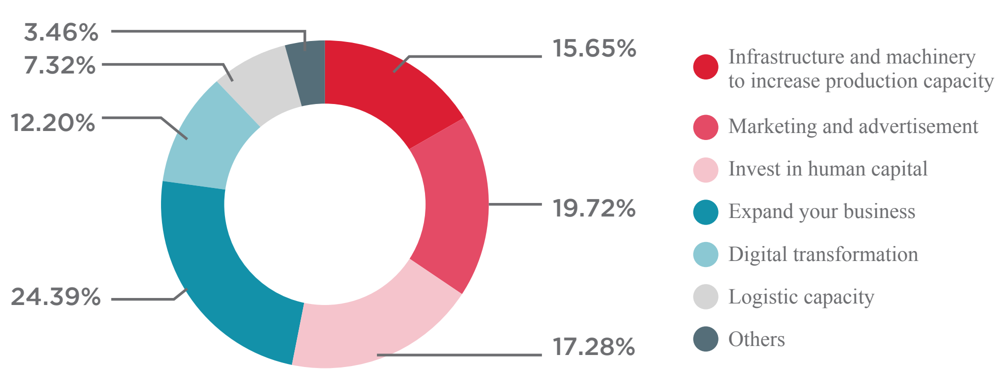


Figure 2. *Own elaboration. (2021). Capital that Women Entrepreneurs Need to Develop their Business.*

Eight of them have strong technological requirements, therefore they need to invest in electronic sales platforms, inventory control, warehouse management, and sales processes. For ecommerce they require US$63,000, while for inventories and sales processes they need to inject US$50,000.

Another convergence point was the merger between economic funds for entrepreneurship and personal funds, since 59% of the interviewed entrepreneurs manage the same bank account. Reason why, when applying for small bank loans, they do so personally and have paid them with an interest rate of 8% and 10%. In general, the women interviewed look for financial loans that are accessible regarding payment terms, between 36 and 60 months.

The following graph quantitatively corroborates what was mentioned in the interviews, that more than half of the entrepreneurs make use of their savings to start a business and to keep that business afloat.

Use of Financial Resources

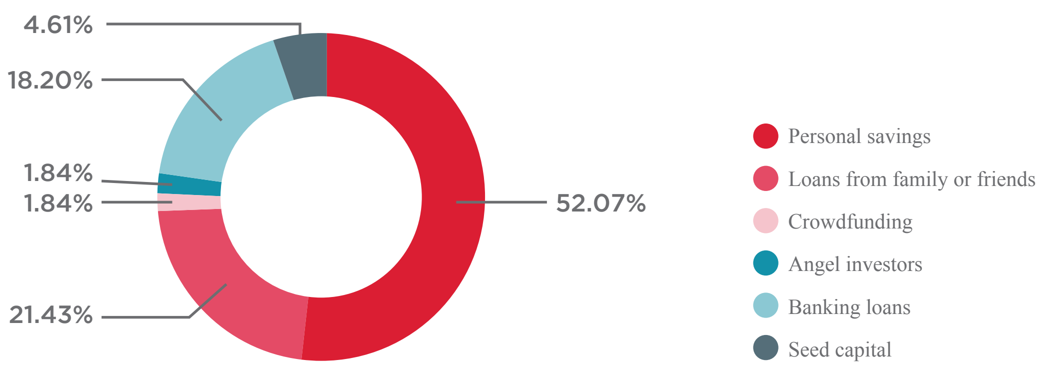


Figure 3. *Own elaboration. (2021). Use of Financial Resources.*

One concern with accessing larger loans is that they are in US dollars. A businesswoman commented "*if we take a loan in foreign currency, I have to be very careful because it is practically impossible in Argentina due to the exchange rate and the fluctuation that the peso is having with respect to the dollar*".

Therefore, the missing middle exists when searching for financial products in your domestic currency or, failing that, at a fixed interest rate.

The bureaucracy to access loans, investments and formalize a business in Latin America has the consequence that "it takes more than two years to market the product for sale and be able to have a physical store" (Female Entrepreneur interviewed, 2021). Another entrepreneur mentioned how they tend to see her company as a "project" because she is a woman and young.

Of the 280 women entrepreneurs surveyed online, only 13% dedicates full time to their business.

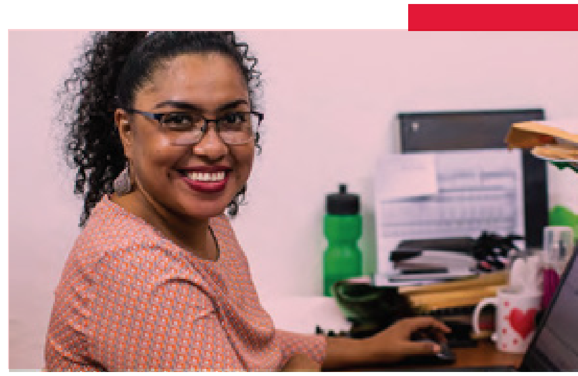
The rest combine other work or family activities, such as studying or having a formal job, beside their entrepreneurship.

The double or triple discrimination faced by female entrepreneurs in Latin America has prompted governments to offer incentives, as in Argentina where "*the Provincial Government offers a reduction in interest rates for meeting a certain percentage of women in managerial positions in a business*" (Female Entrepreneur interviewed, 2021).

"Discrimination is sad... you find a lot of difficulties for people, but in financial power it is greater. They do not pay attention to people with disabilities, transgender people, or women, all these types of people are victims of discrimination" explained a 52-year-old entrepreneur who has been running her company for 25 years.

Another spotted risk by the entrepreneurs is the social impact approach of their businesses.

Despite entrepreneurs having managed to initially obtain seed capital and donations, it is the financial opportunities that are missing, for this missing middle segment, so the SMEs can maintain themselves and grow. To close this financing gap, they look for investment rounds where they could raise capital and connect with strategic partners.



Predominant sectors within companies

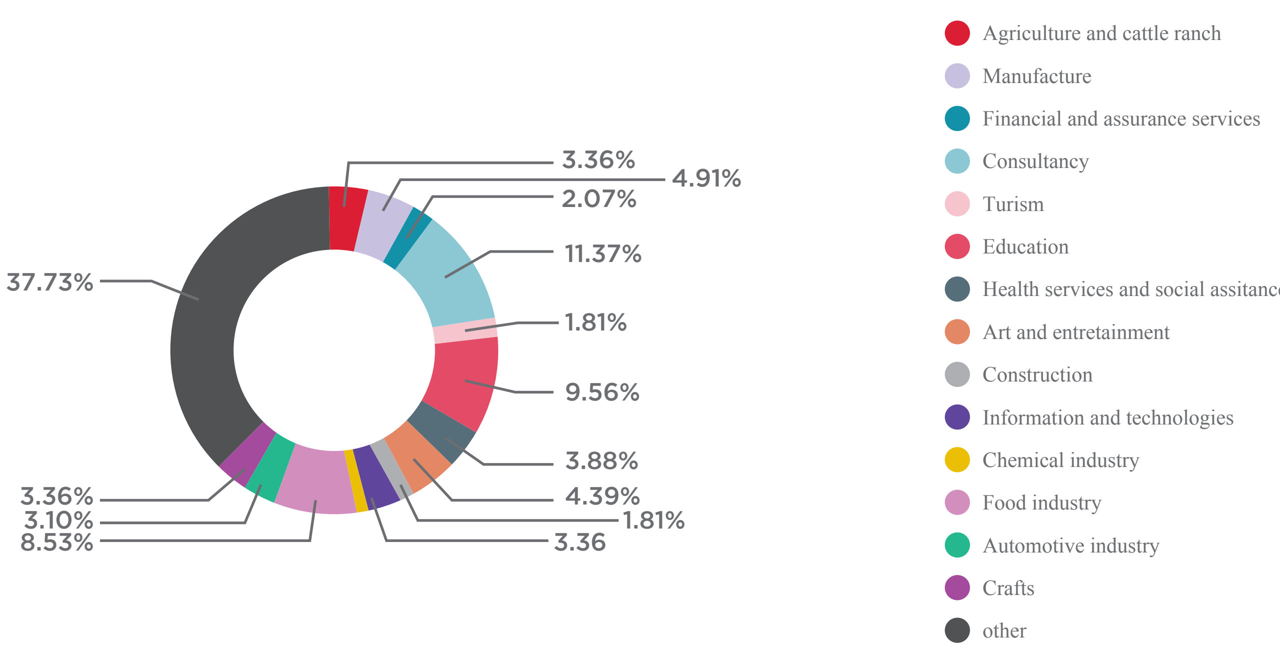


Figure 4. *Own elaboration. (2021). Predominant sectors within companies.*

The investment sought by the entrepreneurs does not always have to be capital. It can also be the acquisition of tools to structure and validate their business idea to take it to the next level.

The graph below shows the importance of non-financial support that entrepreneurs in the missing middle can receive. Almost 25% of the respondents have made use of educational content or courses or sought support networks.

"I think that the acceleration programs are good, because there is a bit of everything, there is also a lot of offer out there, but, but in my case the Star Path program helped me a lot. Because we were able to start giving the business a structure that we didn't have" commented one of the interviewed.

Use of Non-Financial Resources.

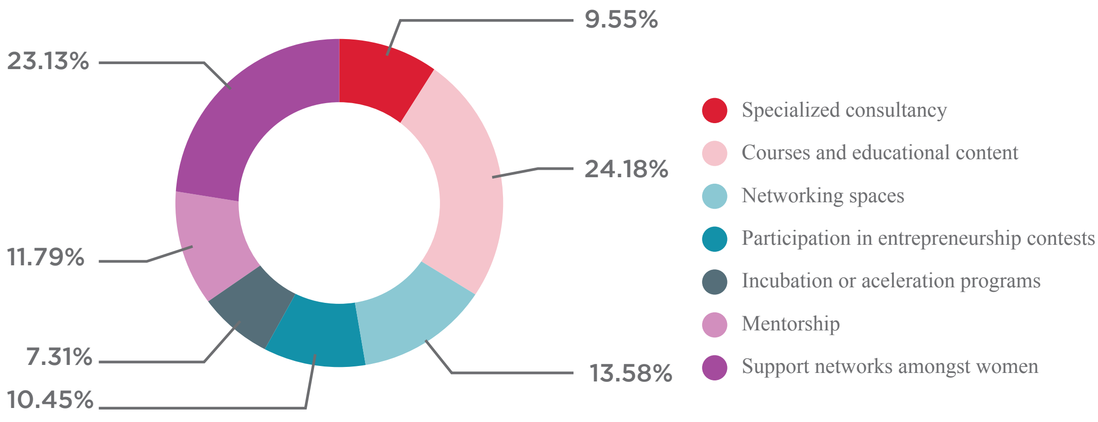


Figura 5. *Own elaboration. (2021). Use of Non-Financial Resources.*

After the analysis of primary and secondary sources such as reports, studies, interviews, and surveys, five key points were found to reduce the missing middle of Latin American women entrepreneurs through financial and non-financial investment.

The lack of inclusion of women within an entrepreneurial ecosystem in the region, neglects the growth and diversity of growing small companies. Some of the key findings are:

1. Women are less risk-averse than perceived. Nonetheless, the majority of the former are associated with sacrifices of space and relationships, dedicated time to the business, and the companies' social focus.

2. Women experience situations of inequality when accessing business loans. Some of the barriers which perpetuate this situation are the lack of financial education, high interest rates and the inflexibility they provide.

3. There still exists a strong need for entrepreneurial spaces and financial solutions with gender lens perspective to enable growth

4. Women entrepreneurs seek smart capital; not only flexible loans, but an experience of financial services where they feel valued and understood.

Key points to understand the Missing Middle segment:

1. The creation of spaces for women.

2. Specialized consultancy.

3. Financial education programs for the acquisition of credits.

4. Financial education programs to support networks for women to strengthen their projects, as well as the empowerment of themselves.

5. Development of flexible financial services, suitable to the capital needs of women.

Taking into account these points is pivotal to attend to the missing middle niche in Latin America, which needs average loans of $334 thousand US dollars. This amount is considered very small for capital investors and very large for small institutions. Therefore, it remains invisible.

More organizations must be encouraged to create support groups for women entrepreneurs, just as Pro Mujer does, where its members can receive training in various fields depending on the line of business, take tax workshops, mentoring, and consulting.

The missing middle gap may be smaller if the needs of Latin American women entrepreneurs are made visible.

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