National Policy Centre for Women's Enterprise Evidence Paper

Women's Enterprise and Access to Finance

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Abstract

This National Policy Centre for Women's Enterprise (NPCWE) evidence paper examines access to finance for women entrepreneurs in the UK. While the sources of business finance used by women and men are very similar, research has shown that women start with lower levels of overall capitalization, use lower ratios of debt finance, and are much less likely to use private equity or venture capital. Reasons for these differences are explored, and illustrative case studies are included. The paper speculates the likely impact on women entrepreneurs of the economic recession and crisis in the financial sector. Finally, recommendations are made to facilitate the start-up and growth of women-owned businesses.

Summary

This National Policy Centre for Women's Enterprise (NPCWE) evidence paper examines the issue of access to finance for women entrepreneurs. There are growing numbers of women entering self-employment and business ownership; however, women-owned businesses are typically smaller in terms of employment and turnover, and are more likely to be based in the service sectors.

Finance has long been regarded as the main obstacle preventing women from starting and growing a successful business. Although the sources of finance are common to women and men, women perceive higher access barriers. Women owned businesses start with lower levels of capitalization, use lower levels of debt finance, and are much less likely to use formal and informal venture capital. Importantly, initial under-capitalization has a long term negative effect on business survival and growth.

The main reasons for the difference in finance usage among women entrepreneurs are associated with industry sector, business age and business size. Structural factors do not explain all the differences, however. Detailed research that has systematically compared matched samples of women-owned and men-owned businesses operating in the same sectors, and of the same age and size, has found residual gender-based finance differences remain. These are often explained in terms of supply-side discrimination, for which the evidence is rather weak, or in terms of demand-side debt aversion, for which there is a stronger case. Certainly, many women entrepreneurs are reluctant to take on unnecessary bank debt.

Recommendations

- > Gender and ethnicity disaggregated data should be made publicly available across the business support sector under the Gender Equality Duty.
- > BERR should monitor and track finance elements of the 'Real Help for Businesses Now' programme and The Aspire Fund to measure take up by women of these products.
- > Banks to focus specific attention on the provision of funding for women entrepreneurs.
- > Small business support agencies to develop women's enterprise information and education programmes around the theme of starting capitalization.
- > Continuing policy efforts are required in order to create economic equality between men and women, to enable women to accumulate resources for business start-up.

Introduction

The importance of women as a largely untapped pool of entrepreneurial talent has been widely recognized at the national and the regional level. A number of initiatives have been designed to expand the numbers of women involved in entrepreneurship, and to increase the number of high-growth businesses owned by women.

Access to finance is a key issue for all entrepreneurs, and there has been longstanding concern that women entrepreneurs may find access to finance particularly difficult. The current economic conditions and, in particular, the crisis in the financial sector, makes this issue particularly topical.

This policy paper reviews the evidence regarding access to finance for women entrepreneurs, considers the effects of the current financial crisis on women in business, and presents a number of recommendations for policy, finance providers, and women entrepreneurs.

Women Entrepreneurs in the UK

Around 720,000 enterprises in the UK are majority-led by women, representing 16% of the 4.5 million UK enterprises. Of businesses with no employees, 17% are women-led; however, of medium-sized businesses (50-249 employees), only 7% are women-led. There are encouraging signs that many more of our new entrepreneurs are women: 34% of the newly self-employed are women compared to just 27% of those currently self-employed[1].Women owned businesses are more likely to operate in the service sectors, which account for 80% of women-owned businesses and 70% of all other businesses (male-owned or equally-owned)[2]. Women owned businesses also tend to be smaller than male-owned businesses, with fewer employees and lower sales turnover [2,3].

Patterns of self-employment and business ownership reflect trends in the wider labour market. Traditional occupational choices steer men into skilled trades, while women are over-represented in administrative and public service occupations where conversion into self-employment is less obvious. The bulk of male self-employment is within the skilled trades (39%), managers and senior officials (16%), associate professional and technical (14%) and professional occupations (13%). In contrast, most female self-employment falls within four occupational categories: managers and senior officials (22%), associate professional and technical (20%), personal services (18%) and professional occupations (12%)[1].

Despite many initiatives to increase the number of women in self-employment and business ownership, the gender gap remains stubbornly wide.[3] Men are still almost twice as likely to start businesses as women. If women started businesses at the same rate as men, there would be 150,000 extra start-ups each year in the UK.[3]

The US has long been regarded as a leader in the issue of women's enterprise. The remarkable increase in women's enterprise in the US contrasts with the relatively slow growth experienced in Western Europe. The reasons for the higher rates of women's enterprise in the US are complex, but at least partly attributable to proactive policies providing enhanced access to finance for women. Proactive policies to support women-owned businesses started in 1979, the same year that the Small Business Administration's Office of Women's Business Ownership was established. The Community Reinvestment Act (1977) similarly helped provide funding to groups, such as women, who had previously failed to access financial services. As of 2006, there were 7.5 million women-owned and women-led enterprises, one third of all US firms, accounting for 17% of private sector employment and 15% of firm revenues.[4] If the UK matched US levels of female entrepreneurship there would be an additional 700,000 businesses in the UK economy.

Women Entrepreneurs and Finance

Access to finance has long been seen as the major obstacle preventing women from starting and growing a successful enterprise.[5] Although access to finance appears to be gender neutral, women perceive higher financial barriers.[6] An analysis of GEM data demonstrated that 'being female increases the probability that an individual will perceive financial barriers to business start-up by around 7.5 percentage points. In turn, these perceptions reduce female start-up rates by between 1.7 - 3.8 percentage points.[6]

The sources of finance used by women and men are very similar; however, research provides unequivocal evidence that women-owned businesses:

- start with lower levels of overall capitalization
- use lower ratios of debt finance
- and are much less likely to use private equity or venture capital

There is also unequivocal evidence that initial under-capitalisation, which is more likely to be experienced by women-owned businesses, has a long term, negative effect on future business survival and growth.

Sources of Finance

Women and men tend to use the same sources of finance in starting and growing businesses. The most commonly used sources of finance in UK small businesses are: bank overdrafts, personal savings, retained profit, bank loans, personal and business credit cards.[7]

When male and female business owners are compared, some very minor differences emerge. For men, the three types of finance most commonly used, after current accounts, are bank overdrafts (43%), credit cards (43%), and deposit accounts (38%). For women, the three most commonly used types of finance, after current accounts, are deposit accounts (39%), credit cards (39%) and bank overdrafts (33%).[8]

Start-up Capitalization

Women typically start businesses with lower levels of overall capitalization. Several studies have found that average levels of capitalization for women-owned businesses are just one third the levels of capitalization used by male-owned businesses [5,9,10].

The findings of one recent study illustrate this. Comparing the starting capital of a sample of male and female business owners, matched by industry sector, business age and location, the mean total starting capital of male-owned firms was £18,683, nearly three times higher than the mean total starting capital, £6,433, of female-owned firms[10].

CASE STUDY

The Dunsmore Consultancy

Anne set up her business in 1994, starting with a contract for £5,000 per month retainer fee over 18 months. The client was a successful blue chip construction company. The business needed minimal funding – office space was free, a couple of computers were already available, so start up capital was not required.

When Anne attempted to set up a bank account, it was with a cheque for work carried out and her only requirement was a business account. She first attempted to open a business bank account with RBS. It couldn't be done immediately and an appointment was made for three days hence. Anne was interviewed by a customer relationship manager in an open area. At an adjacent desk a family of four were having a noisy and emotional discussion with another manager about the repossession of their home. Anne produced her cheque and some identification. The manager told her that she needed to produce six months of bank statements and a further six months of bank statements from her husband before they would consider the request. The bank manager gave her a substantial form to fill in and told her to complete the form and return with the documentation. On the way back to her office, she went into another bank on spec and met the business banking manager, a very helpful woman, who completed the application for her on a computer, had no requirement for statements and who banked the cheque there and then.

Anne has changed banks since then, but has always run the business on a cash basis so has never needed a loan. Her requirements are easy access to her money and minimal charges. She feels that she flies under the radar of the bank because she doesn't require any loans. She has found it difficult to find a bank that offers a decent deposit facility as her most pressing financial concern is saving up for her annual tax bill and she would prefer a decent return on her savings.

Debt Finance

Women also typically use lower ratios of debt finance when starting and running their business. The same study of male and female matched businesses found the volume of bank debt finance borrowed by women-owned businesses was only 77% of that borrowed by male-owned businesses.[10] The 2007 UK Survey of SME Finances also found that women sought significantly lower amounts of finance.[8] Another survey of nearly 19,000 UK small firms found that women-owned firms were least likely to use bank overdrafts and most likely to use their own savings, personal credit cards, their family and other business / employment.[7]

The Cost of Borrowing

While the 2005 UK Survey of SME Finance found female business owners were charged more than male business owners on term loans (2.9% versus 1.9%),[11] no other study has found evidence to support this. Indeed, the follow-up 2007 UK Survey of SME Finance found no gender difference in median levels of bank charges, though male-led firms were charged a higher mean level, probably reflecting their larger size. In addition, the follow-up study found that female-led businesses, being smaller than male-led businesses, were more likely to benefit from free banking.[8]

On balance, there is little evidence that gender directly impacts on the cost of bank borrowing. The cost of bank borrowing is influenced by the size of business and the size of borrowing. Women-owned businesses tend to be smaller and therefore may benefit more from free banking. However, with regard to the cost of term loans, women tend to borrow smaller sums, and smaller loans may be subject to relatively higher administrative charges.

Private Equity and Venture Capital

Private equity and venture capital is used by very few businesses. Indeed, some research has suggested that businesses are more likely to be funded by lottery wins than by venture capital.[12] But, within the small pool of businesses backed by venture capital, disproportionately few are owned by women. The 2007 UK Survey of SME Finance found that only 1% of male-led businesses and 0% of female-led businesses had used new equity finance in the past three years.[8]

Even in the US where the venture capital industry is more mature, very few firms gain formal or informal venture capital. Women-owned businesses in the US are believed to attract just 3% of total venture capital funds.

Explaining Gender Differences in Finance Usage

Differences in finance usage between women-owned and male-owned businesses are associated with three main factors:

- structural dissimilarities between male and female owned businesses
- supply-side discrimination
- demand-side debt aversion

1. Structural Dissimilarities

The major differences between women-owned and men-owned businesses lie in the industry sectors in which their businesses typically operate, which have different financial requirements. In addition, business age and size may also influence financial requirements. Women-owned businesses are more likely than men-owned businesses to operate in industry sectors that require less finance to start-up and grow. Women-owned businesses also tend to be younger and smaller than men-owned businesses and therefore have yet to require significant growth finance. These differences explain many of the obvious gender differences in funding profiles.[13]

However, studies that have carefully matched samples of women-owned and men-owned businesses by industry sector, age and size have found persistent gender differences. This suggests that structural factors do not account for all of the gender differences in finance usage. Instead, two other explanations have been proposed, focusing on supply-side and demand-side factors.

2. Supply-side Discrimination

Many studies have suggested that bank procedures may disadvantage women business owners. For example, one Canadian study argued that the 5Cs of bank lending (character, capacity, capital, collateral and conditions) may be subjectively applied to the detriment of female entrepreneurs[14]. Overall, the weight of research findings has found no evidence that banks discriminate against women entrepreneurs. Neither is it within the banks' interests to deliberately exclude this increasingly important female market.

Other studies report that women are often dissatisfied at their experience with banks.[15] This is not evidence of discrimination; it is evidence of poor customer service.

3. Demand-side Debt Aversion

Many women entrepreneurs may simply be more reluctant than men to take on the burden of business debt and disinclined to engage in fast-paced business growth.[16, 17]

Women's relatively lower earnings in employment, coupled with their relatively younger age at business start-up, suggests that women have less collateral against which to borrow and shorter personal credit histories, which may explain their reluctance to take on debt finance. Female business owners may be discouraged by existing bank products which may not meet their needs, and may also make a positive choice to start-up by bootstrapping resources rather than by extensive borrowing. While there is a popular view of women being 'risk averse', there is little evidence. Rather, the evidence suggests that women may be simply reluctant to take on unnecessary bank debt.

Women Entrepreneurs, the Recession and the Crisis in the Financial Sector

The effects of both the current recession and the crisis in the financial sector on women-owned businesses have yet to be fully realized. Both factors are likely to affect women-owned businesses in different ways.

The effects of the recession on women-owned businesses are probably more certain. Any downturn in consumer spending is likely to bite first at those elements of consumer spending that are most dispensable. Personal services sectors are likely to be among the first sectors affected. To the extent that women-owned businesses are more likely than other businesses to operate within personal services, women entrepreneurs will probably be among the first to feel the effects of the recession.

The extent to which women entrepreneurs will be affected by the crisis in the financial sector is less certain. On the one hand, women-owned businesses are less likely to be affected by bank lending constraints for the simple reason that they seek significantly lower amounts of bank finance. Women owned firms are also less vulnerable as they tend to carry lower levels of debt. On the other hand, as this policy report recommends, women-owned businesses need encouragement to capitalize their businesses appropriately in order to achieve growth. Constraints on bank lending will impair survival and growth prospects of women owned businesses.

Recommendations

Further research

Gender and ethnicity disaggregated data for business and enterprise should be made public under auspices of Gender Equality Duty as several banks are now part nationalised. Such data could identify where challenges lie for women entrepreneurs in terms of behaviours; characteristics, growth paths and performance patterns. It is crucial to have relevant data as it is a pre-requisite for the development of evidence-based policies.

Monitoring and tracking

'Solutions for Business': the range of products now available (such as Starting a Business, Intensive Start-Up Support, Small Loans for Businesses, Enterprise Coaching and Starting a High Growth Business) can be of real benefit to women entrepreneurs. However, what is crucial is that data is collected on the gender and ethnicity of business owners to measure whether they are being accessed by under-represented groups in particular. Business Links can then use such data to illustrate whether concrete results are being achieved with these business support products.

RDAs: The National Policy Centre for Women's Enterprise recommends a common information package be developed for The Aspire Fund to ensure that women-owned or majority-led businesses across England get an equal opportunity to access the high levels of finance available. In addition, the outcomes of The Aspire Fund will need to be examined and a next steps strategy developed.

CASE STUDY

First Impressions Last Longer

Yasmin started her first company in 1999 and created the main trading wing, First Impressions Last Longer, in 2004. The company is both an environmental consultancy and also provides office supplies within an environmental niche. Yasmin and her partner financed the start up with a combination of redundancy pay, personal savings and consultancy contracts, so did not need to seek external debt finance. The company's main customers are firms with a strong focus on environmental concerns. Over the past five years, the company has experienced strong growth, employing twenty people at the end of 2008, and the ambition is to grow the business still further.

In the past few months, a small number of their large customers have gone into liquidation, owing the company half a million pounds. Despite the loyalty of their remaining customers, most of which are steady and enduring organizations such as local councils and long established environmental charities, their bank rejected their application for loan finance to see them through this difficult period. Yasmin and her partner approached the other High Street banks, but their applications for loan finance have been rejected by all of them. Their next steps will be to appeal for help through their local Business Link. The company has laid off five of its employees in the past few months, in an effort to reduce costs. The firm is now being financed through the owners' personal savings and their small private property portfolio.

Bank Focus on Women Entrepreneurs

There is strong evidence that women are deterred from starting businesses by perceived difficulties in accessing finance. The current crisis in the financial sector and reduction in lending to small firms will have increased the perception of difficulties in accessing finance. In the current climate, banks may not see the need to prioritize women; however, economic recovery requires the increased participation of women in entrepreneurship. Banks need to focus specific attention on the provision of funding for women.

Financial Education for Women

Women entrepreneurs seek significantly lower amounts of finance, but under-capitalisation at start-up has a long-term and negative effect on business performance and growth. Small business support agencies need to focus specific attention on developing women's enterprise information and education programmes around the theme of starting capitalization.

Labour Market Equality to Increase Business Resources for Women

The continuing pay gap between male and female workers restricts the financial resources available for the creation and growth of women-owned business. Women working in a full-time capacity earn 17% less than men. Over a lifetime, men earn nearly £250,000 or 37% more than equivalently skilled women without children[18]. One consequence of earning less in employment is that women accumulate less financial capital with which to initiate business ownership. Continuing policy efforts are required in order to create economic equality between men and women.

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The National Policy Centre for Women's Enterprise (NPCWE) provides a central knowledge base for research and data related to women's enterprise. The NPCWE, funded by BERR works at national, international and regional levels, collaborating with strategic partners to facilitate best practice and knowledge-sharing to create a long term increase in the number of sustainable women-led businesses.

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