APRIL 2023

EVIDENCE SNAPSHOT

# What does Research say on how to improve Access to Debt Financing for Women-owned or Led Small and Medium Enterprises?

WOMEN ENTREPRENEURS FINANCE INITIATIVE

## WHAT IS THE WE-FI EVIDENCE PAPER?

The We-Fi Evidence Paper reviews existing evidence on what works and what does not work in supporting Women-owned or Led SMEs (WSMEs) in developing countries and maps this evidence along the impact pathways of the four focus areas in We-Fi's Theory of Change: Access to finance, access to skills, access to markets, and an enabling environment. The evidence maps show where evidence is limited, emerging or strong and highlight several knowledge gaps where more evidence is needed.

For access to the ***full evidence paper,*** click here.

For access to the ***searchable database*** of publications used in the evidence paper and this snapshot, click here.

Women's entrepreneurship is a key driver of a country's prosperity. Women entrepreneurs are developing innovative solutions to help solve problems in their communities, create jobs, boost economic growth, and drive social change. Yet women entrepreneurs face policies, institutional biases, and social norms that disempower them. To make a difficult situation worse, the pandemic has disproportionally impacted women-led businesses. The Women Entrepreneurs Finance Initiative (We-Fi) aims to break down these barriers and help Women-owned or Led Small and Medium Enterprises (WSMEs) in developing countries grow.

*This snapshot, focused on debt financing, is part of a series which highlights select research findings and evidence gaps from the We-Fi evidence paper. Snapshots are released for the four We-Fi focus areas (access to finance, access to skills, access to markets, and an enabling environment) and other topics.*

## WHAT ARE THE CHALLENGES FACED BY WSMES?

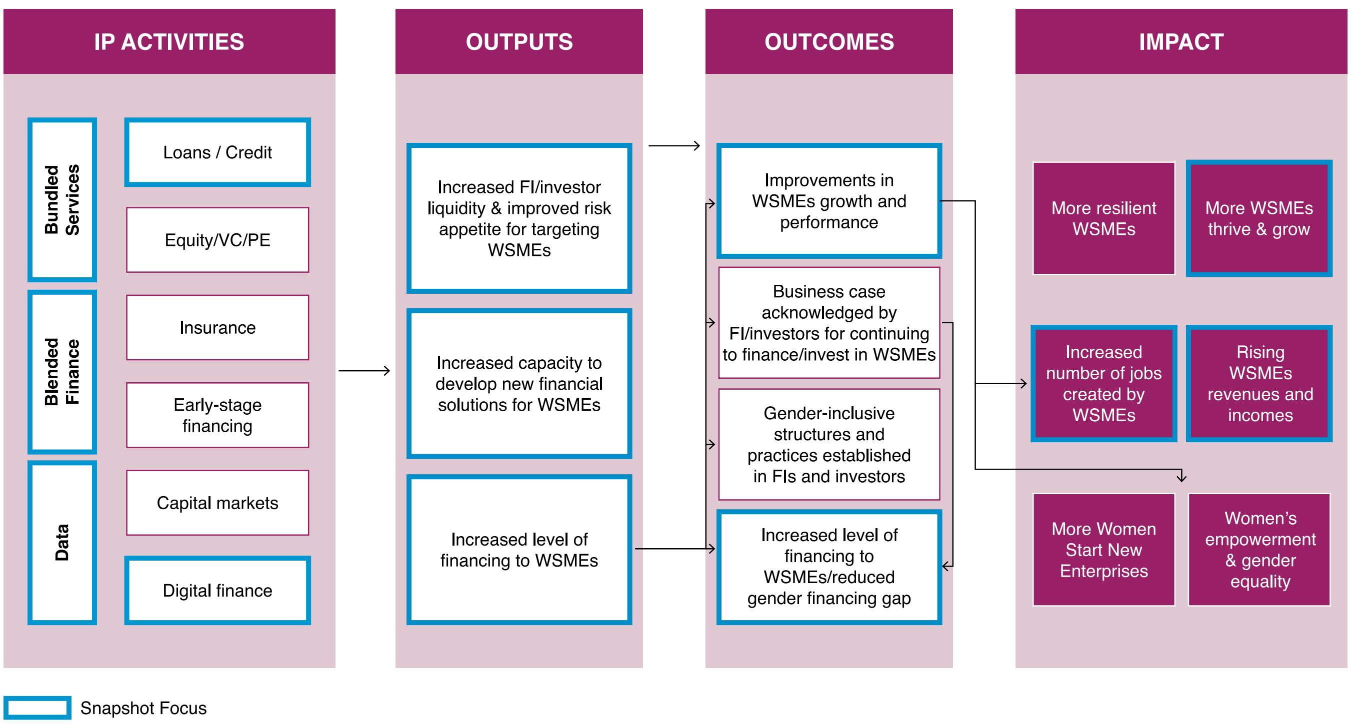
Women continue to be less likely than men to have access to finance. Accessing finance is particularly difficult for women entrepreneurs in the "missing middle". Women's ability to access loans is often hindered by collateral requirements or unfavorable banking practices, such as higher interest rates or shorter repayment periods. In addition, many women entrepreneurs do not even apply for loans because of low financial literacy, risk aversion, or fear of failure.

- $1.7 trillion gender financing gap[1]
- Loans for women are on average one third lower than for men[2]
- 70% of women in developing countries are without access to bank accounts[3]
- 11% of seed capital goes to women-owned startups[4]

## THEORY OF CHANGE

Addressing the complex challenges faced by WSMEs requires multi-dimensional approaches, innovative instruments, and a cross section of stakeholders. This snapshot focuses on the ‘Access to Finance’ component of We-Fi’s Theory of Change, and drills down into the area of debt financing. It lays out how different activities and approaches (e.g., loans, digital finance, blended finance) are intended to stimulate short-term outputs (e.g., better access to financing, new financial products and services for WSMEs), medium-term outcomes (e.g., survival of WSMEs, improved business growth) and long-term changes (e.g., higher productivity, and job growth).

### WE-FI’S ACCESS TO FINANCE THEORY OF CHANGE:

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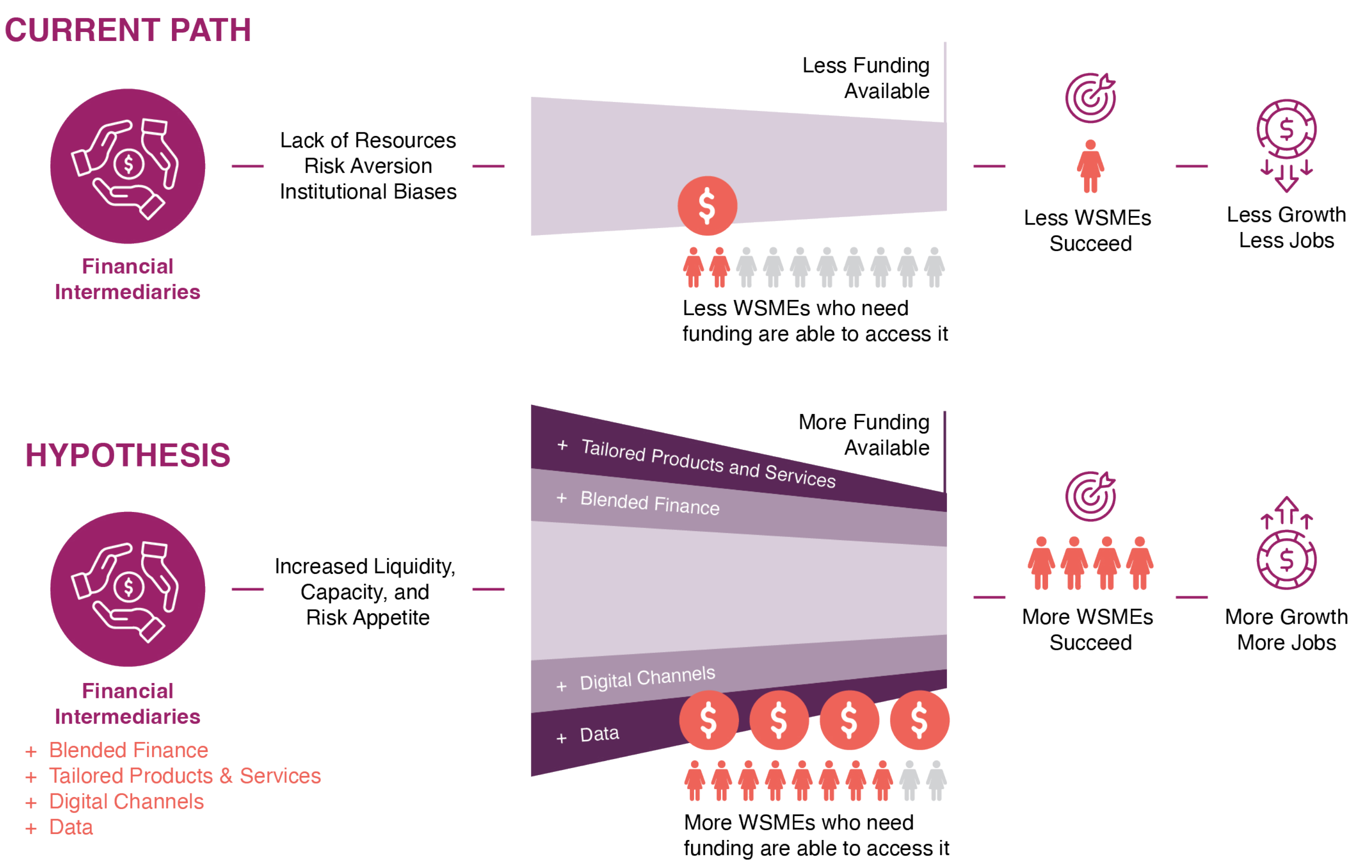
[1] IFC. 2017. “MSME Finance Gap: Assessment of the Shortfalls and Opportunities in Financing Micro, Small, and Medium Enterprises in Emerging Markets.” World Bank Group, Washington, DC. https://openknowledge.worldbank.org/handle/10986/28881.
[2] Data from GBA’s Global Women’s Market Survey, Global Banking Alliance for Women. https://financialallianceforwomen.org/wp-content/uploads/2017/02/InBrief-BusinessCase_FINAL.pdf
[3] Data from the Word Bank Global Findex Database, World Bank Group, Washington, DC, https://globalfindex.worldbank.org/
[4] IFC, Oliver Wyman, and Rock Creek. 2019. “Moving Toward Gender Balance in Private Equity and Venture Capital.” World Bank Group, Washington, DC. https://www.ifc.org/wps/wcm/connect/79e641c9-824f-4bd8-9f1c- 00579862fed3/Moving+Toward+Gender+Balance+Final_3_22.pdf?MOD=AJPERES&CVID=mCBJFra.

Today, ***financial intermediaries*** like banks, funds, accelerators, and insurance companies play a central role when it comes to catalyzing more capital to women entrepreneurs. Currently, institutional biases, risk aversion, capacity and liquidity constraints, and the lack of tailored products and services hinder financial intermediaries' ability to effectively serve the WSME market.

Going forward, ***blended finance*** can offer new solutions to de-risk financing / investments and provide capacity-building support to financial intermediaries to better serve the WSME market and increase the pipeline of funding available to them. The availability of ***new financial products and services tailored to the needs of WSMEs*** can help improve access and utilization of financing which might otherwise be foregone. Offering these tailored financial products and services in combination with complementary, ***bundled services*** can improve their impact on WSMEs. ***Digital channels*** can play a crucial role in delivering available funding to women entrepreneurs, as gender constraints such as mobility barriers can be overcome. Finally, the collection and use of ***sex-disaggregated data*** is necessary to track and understand gender outcomes and demonstrate the business case to investing in WSMEs. This positive business case will incentivize financial intermediaries to further increase the level of financing going to WSMEs.

Ultimately, the hypothesis is that these factors all have a role in creating ***better access to finance, enabling more WSMEs to grow and increase productivity and employment.***



## PRELIMINARY RESEARCH FINDINGS AND IDENTIFIED EVIDENCE GAPS

The following highlights preliminary research findings on access to debt financing and outlines persistent evidence gaps where more research is needed. While this is not a full overview of all findings and available studies mentioned in the evidence paper, it aims to provide a useful framing of insights.

### FINANCIAL PRODUCTS & SERVICES:

**How can innovative credit assessment methods be effective at easing WSMEs' access to credit (e.g., psychometric tests, cashflow-based lending etc.)?**

Collateral-free or reduced collateral loans underpinned by solid credit assessment mechanisms have shown some promising results as an alternative to traditional loan assessments. Financial institutions use alternative data from mobile phone usage patterns, purchase habits, or psychometric tests to determine credit worthiness. Evidence from Ethiopia focused on women-owned micro and small enterprises suggests that psychometric credit scoring significantly alleviates credit constraints for women entrepreneurs and can help them access higher value loans (growth-size loans). Similarly, non-gender specific results from a study in Peru show that psychometric tests increased loan use of SMEs by up to 59 percent points for applicants without a credit history, without leading to worse repayment behavior.

Evidence on access to debt financing is heavily focused on micro-credit (and micro-enterprises). There are very limited studies on SME financing. More studies exploring the effectiveness of different SME loans products are needed as well as studies on how financial loan products can be combined with training and other complementary services (bundled services) to achieve the best results for WSMEs.

#### EVIDENCE GAP #1: WSME LOAN PRODUCTS AND ALTERNATIVE LENDING MODELS

More studies are needed to explore how gender-specific SME loan products incl. innovative design features of loans and alternative lending models (e.g., asset-based lending, cashflow-based lending) can help WSMEs access financing, increase business growth and promote job growth and women's empowerment in the long-term. Also, more research is needed on other lending instruments like supply chain financing, trade credit, or credit lines.

#### EVIDENCE GAP #2: BUNDLING CREDIT WITH NON-FINANCIAL SERVICES

There are limited studies exploring how combining capital with other support interventions (e.g., credit + business training; credit + market access; credit + networking activities) can effectively increase WSME business growth and how such bundled services can be offered cost-effectively.

## DELIVERY CHANNELS:

**How can digital delivery channels more effectively deliver credit to women entrepreneurs and accelerate business investments and access to debt financing?**

Digital credit offered via mobile money can help women entrepreneurs access debt financing, for example by overcoming limitations in mobility (e.g., due to social norms). Numerous studies illustrate how mobile money increases women's access and use of a range of financial products and services from which they were previously excluded. For example, findings from Sub-Saharan Africa show that women-owned firms' use of mobile money increased their investment and spurred higher demand for more credit, which was not observed for men-owned firms. Other studies show how digital loan disbursement can add elements of privacy and control over how women invest their money, resulting in higher business investments and profits. Results from an experiment in Uganda, in which female bank clients were randomly assigned to receive micro-credit in a mobile account versus in cash showed that women who received the money in a mobile account had, on average, 15 percent higher profits and 11 percent more business capital.

### EVIDENCE GAP #3: EFFECTIVENESS OF DIGITAL FINANCE SOLUTIONS

More research is needed to better understand to what extent and/or how digital delivery channels can overcome gender constraints and improve the access and usage of WSME loan products for different sectors and contexts and how this translates into higher business investment, business growth, and demand for financing. This includes studies on how digital delivery channels can improve WSMEs access to trade finance and supplier and distributor credit. Lastly, more evidence is needed to explore potential risks and barriers that could hinder WSMEs to use digital finance and effective strategies to overcome them.

At the same time, gender gaps on connectivity and digital skills persist and could prevent WSMEs from benefiting from these opportunities or even put them at risk. For example, digital loans may come with issues of cybersecurity or risks of entering into debt spirals due to automated decision-making, low financial literacy and often opaque loan terms.

## LENDING / INVESTMENT PRACTICES:

**How does gender discrimination impact WSMEs' access to debt financing and how can gender biases in financial intermediaries be mitigated to ensure sustainable capital flows going to WSMEs?**

A study looking at gender discrimination among loan officers in Turkey found that male and female officers both held implicit discriminatory views and that discriminatory tendencies declined with experience. These findings imply that banks should ensure that lending decisions are made by sufficiently trained and experienced loan officers. In the venture capital space, Village Capital built and implemented a peer-selected investment methodology, which gives groups of early-stage entrepreneurs the power to make a collective decision on who should receive investment. Results show that investments are significantly more diverse (46 percent women-led companies) than the traditional VC portfolio (15 percent women-led companies).

Additional research is needed on effective ways and models to tackle gender biases in lending and investment decisions. This includes studies on blended finance, as there seems to be a broad consensus that blended finance plays a crucial role when it comes to risk-sharing mechanisms and strengthening the capacity of financial intermediaries to develop processes, structures, products, and services to better serve WSMEs.

### EVIDENCE GAP #4: EFFECTIVENESS OF BLENDED FINANCE

There is a lack of studies on blended finance mechanisms such as performance-based incentives or risk sharing mechanisms. More studies are needed to understand how blended finance can most effectively incentivize and enable financial intermediaries to deliver more and higher loans to WSMEs and what factors determine whether blended finance mechanisms can have a sustainable effect on financial institutions in the long-term. In addition, it's critical to understand how WSMEs' performance is affected when receiving financing from financial institutions who apply blended finance instruments.

## CONTEXTUAL CONSTRAINTS:

**How does the effectiveness of access to debt financing on WSMEs business performance depend on underlying contextual constraints?**

Generally, evidence on the effectiveness of access to loans on increased business performance of women entrepreneurs is mixed[5]. Various studies suggest that heterogeneity really matters in access to credit and impacts of lending may vary depending on the type of female borrower and underlying contextual constraints. For example, the findings from a meta-analysis estimating the heterogeneity in effects across seven randomized controlled trials from seven countries found that micro-credit typically did not impact business profits if the entrepreneur did not have any previous business experience. Another study using data from experiments in India, Sri Lanka, and Ghana compared the impacts of credit between women borrowers from single-enterprise households and multiple-enterprise households. The absence of a profit response for women-led micro enterprises in multiple-enterprise households reflected the fact that women's capital was usually invested into their husband's enterprise.

This shows that women-led SMEs should not be viewed as a homogeneous group. There are only very few studies that sex-disaggregate data and explore business outcomes for different segments of women entrepreneurs. Generally, more sex-disaggregated studies on women's entrepreneurship are needed but also more segment-specific research.

### EVIDENCE GAP #5: SEX-DISAGGREGATED DATA

The lack of sex-disaggregated data is a considerable barrier to better understanding what works for whom and why. To date, there is still a low uptake of financial institutions, governments, and corporates in collecting and using sex-disaggregated data. More evidence is needed to understand what it takes to collect better data and how data improves women's access to finance. More and better data will also help create more detailed segmentation frameworks for targeted research to explore the effects of different types of financing for different segments of WSMEs.

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[5] Although most literature focuses on micro-credit and micro-entrepreneurship.