Mapping Enterprises in Latin America and the Caribbean[1]

Basic Definitions

Countries surveyed in 2010 and how they are grouped for analysis:

In 2010, Enterprise Surveys (ES) interviewed 12,855 enterprises in 30 Latin American and Caribbean countries. In addition in 2009, 1,802 firms were interviewed in Brazil also following the standard ES global methodology.

For analytical purposes, the 31 countries are categorized into 3 groups:

Small Caribbean countries: Antigua and Barbuda, The Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Suriname, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines

Medium-size countries: Bolivia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Jamaica, Nicaragua, Panama, Paraguay, Uruguay, and Trinidad and Tobago

Large countries: Argentina, Brazil, Chile, Colombia, Mexico, Peru, and Republica Bolivariana de Venezuela.

Two waves of Enterprise Surveys, 2006 and 2010:

Fifteen countries were surveyed in 2006 using the ES global methodology: Argentina, Bolivia, Chile, Colombia, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay, and Republica Bolivariana de Venezuela. In total, 10,930 firms were interviewed in 2006, of which 3,535 were re-interviewed in 2010.

Reference periods of the survey data:

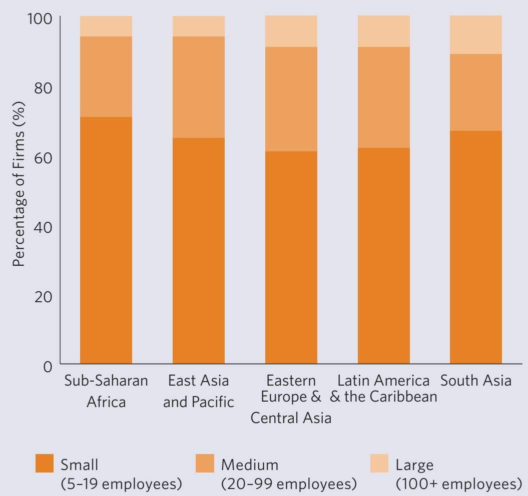
The information collected in the surveys refers to characteristics of the firm at the moment of the survey (2006, 2010 and 2009 for Brazil) or to the last completed fiscal year (2005, 2009, and 2007, respectively). In addition, sales, employment, and labor productivity annual growth rates are calculated comparing data from the last complete fiscal year of each survey and recall data. Consequently, growth rates refer to the period 2002-05 for the 2006 surveys, 2004-07 for the 2009 Brazil survey, and 2007-09 for the 2010 surveys.

The Enterprise Surveys (ES) provide information on the characteristics of firms across various dimensions, including size, legal status, ownership characteristics, trading status, and links to the informal or unregistered sectors.

As is the case elsewhere in the developing world, the overwhelming majority of firms in Latin American and the Caribbean (LAC) are small and medium enterprises (SMEs—fewer than 100 employees). Indeed, 91 percent of LAC firms fall into this category. The share of SMEs is higher in the small Caribbean countries, where 94 percent of enterprises are SMEs; elsewhere in the region, 90 percent of firms are SMEs (Figure 1).

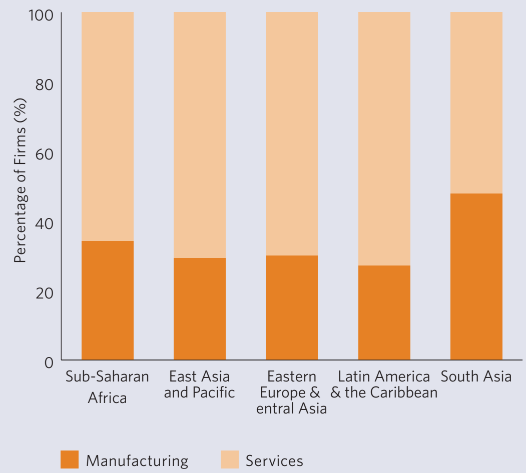
The average firm in LAC employs 42 full-time workers. Large firms, those with 100 or more employees, average over 273 full-time employees in LAC—21 percent higher than the 225 employees in large firms elsewhere in the developing world. Moreover, firms in LAC rely less on temporary employment than firms in other regions: on average, firms in LAC hire 5 temporary workers per year, approximately a third compared to those hired by firms in SAR (18 workers) and EAP (13 workers).

FIGURE 1 **DISTRIBUTION OF FIRM SIZE ACROSS REGIONS**



Source: Enterprise Surveys.

FIGURE 2 **FIRMS IN LAC ARE MORE LIKELY TO BE ENGAGED IN THE SERVICES SECTOR THAN IN MANUFACTURING**



Source: Enterprise Surveys.

As elsewhere in the developing world, firms in LAC are primarily found in service industries (Figure 2). Seven out of every ten firms in the region are in the services sector. The proportion is higher among the small Caribbean countries (80 percent) than in the rest of the region (69 percent). These averages are in line with global figures: 67 percent of firms elsewhere in the developing world are service firms.

The LAC region contains a larger share of older firms than any other developing region in the world. Only 26 percent of firms in LAC have been in operation for less than 10 years.[2] The share of young firms is thus far lower than in Sub-Saharan Africa (50 percent), East Asia and the Pacific (46 percent), Eastern Europe and Central Asia (36 percent), and South Asia (46 percent). The story is the same looking only at SMEs in LAC, where only 27 percent are young compared with over 45 percent in the rest of the developing world.

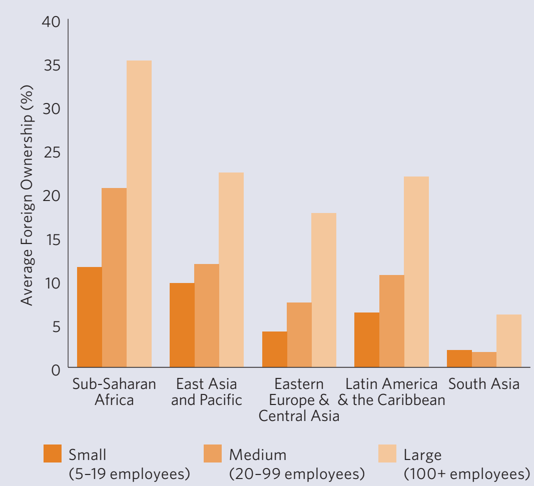
Compared with firms in the rest of the world (with the exception of ECA), firms in LAC are more likely to be closed shareholding limited liability companies.[3] Indeed, 46 percent of firms in LAC are closed shareholding companies, while fewer than 5 percent are publicly traded shareholding companies. Thirty-one percent of firms in LAC are sole proprietorships and almost all of these are SMEs, 98 percent.

International engagement in the private sector in LAC lags behind the rest of the world

Compared with other regions in the developing world, foreign ownership in LAC is at median levels: foreign owners have a 9 percent stake in LAC firms on average, lower than the 15 percent in Sub-Saharan Africa and 11 percent in East Asia, but above the 6 percent stake in Eastern Europe and Central Asia and the approximately 2 percent stake in South Asia. As in other regions, the share of a firm that is foreign-owned is higher among large firms than in small and medium firms (Figure 3). Despite regional efforts to attract foreign direct investment, the data show that 87 percent of all firms in the LAC region have no foreign ownership and only 6 percent are fully foreign-owned. The level of foreign ownership in small Caribbean countries is double that of the large countries of the region: firms in the small Caribbean countries have an average of 11.4 percent foreign ownership, compared to 5.2 percent in the large countries.

With respect to trade, eighteen percent of LAC firms are involved in exports, directly or indirectly, putting trade at average world levels: lower than in Eastern Europe and Central Asia (22 percent), but higher than in South Asia (11 percent) and Sub-Saharan Africa (10 percent). Firms in the small Caribbean countries are the most likely to export, directly or indirectly, and their exports as a proportion of firm sales are also higher than for firms in the rest of the

FIGURE 3 **PROPORTION OF FIRM OWNERSHIP THAT IS FOREIGN-OWNED**



Source: Enterprise Surveys.

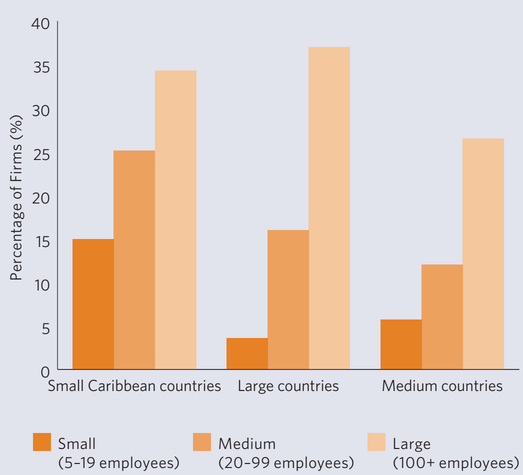
region. Nineteen percent of firms in the small Caribbean countries export directly, compared to 11 percent in large LAC countries and 10 percent in medium-size countries. Even among small firms, the small Caribbean countries are more linked to foreign markets than the rest of the region, with close to 15 percent of small firms being direct exporters, compared with only 6 percent for medium-size countries and about 4 percent for large countries (Figure 4).

As opposed to the trend observed in exports, firms in LAC are relatively more dependent on the rest of world when it comes to inputs. Seventy-one percent of manufacturing firms use imported inputs in LAC, higher than the average of 61 percent elsewhere in the world. Within LAC, the small Caribbean countries have a higher percentage of importing firms (74 percent in the small Caribbean countries versus 71 percent in the medium-size countries and 65 percent in large countries). In some countries of the region, this dependency on foreign markets for inputs is almost universal: over 90 percent of manufacturers in Grenada, Barbados, and St. Kitts and Nevis use foreign materials and supplies.

Competing with informality

The widely held view that informality is common throughout Latin America and the Caribbean is confirmed by the ES data. Across the region, 63 percent of registered

FIGURE 4 **PERCENT OF FIRMS EXPORTING DIRECTLY**



Source: Enterprise Surveys.

firms in the survey report competing with informal or unregistered firms. This is only slightly lower than in Sub-Saharan Africa (66 percent) and considerably higher than in East Asia and Pacific (EAP), Eastern Europe and Central Asia (ECA), and South Asia (SAR). Excluding LAC, the global average of firms that report competing with informal firms is 54 percent.

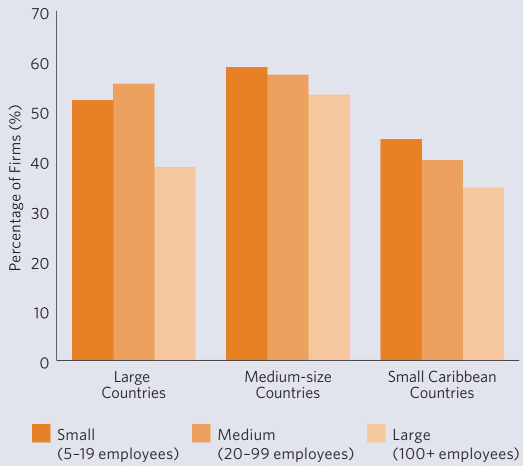
Within LAC, competition with informal firms is common across all firm sizes. Small firms are the most likely to face competition from informal firms, as is the case in every region of the world, except EAP. However, only in LAC and Sub-Saharan Africa do more than half of firms of all sizes experience competition from informal firms; in other regions of the world, at least among large firms, less than half experience this type of competition.

When it comes to registering a company, throughout the region, the vast majority of managers—75 percent on average—report that the main reason for registering their company was to comply with the law. Economic motivations for registration were reported at a distant second: 9 percent of managers gave better access to financing as their primary reason, while 8 percent cited access to customers and suppliers who deal only with registered firms.

Eighty-seven percent of firms in LAC were registered when they started operations, an average considerably higher than that of Sub-Saharan Africa (82 percent), and East Asia and Pacific (84 percent), but below the ECA region (96 percent).[4] The fact that almost 9 out of 10 firms in LAC start formal and remain formal, coupled with the lack of economic motivation for registration, provide some indication that there may be a dual composition to the private sector: formal firms start up as formal and informal firms start up as and remain informal.

Another dimension of informality is when formal firms engage in informal business practices, such as selling without receipts or hiring unreported workers. Based on the ES data, over half of firms report having dealings with formal firms engaged in one of these practices. When it comes to facing competition from firms that sell products without receipts, it is, again, the small enterprises that report facing the greatest competition, in both the small Caribbean countries and in the medium-size countries, while in the large countries, it is the medium-size enterprises that report the highest competition from this type of firm (Figure 5).[5] Competition with firms that fail

FIGURE 5 **PERCENT OF FIRMS THAT COMPETE WITH FIRMS SELLING PRODUCTS WITHOUT RECEIPTS**



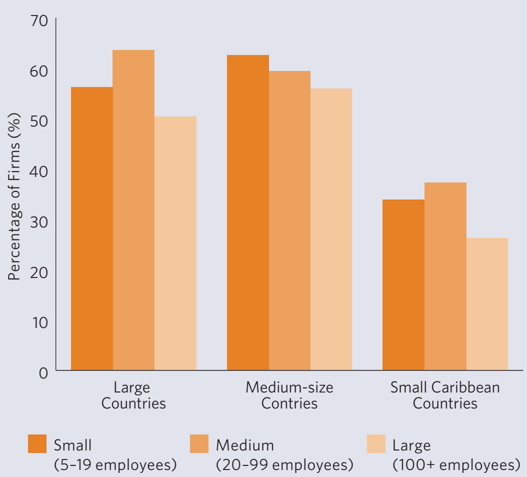
Source: Enterprise Surveys.

to report workers is consistently lower among large firms (Figure 6). The small Caribbean countries exhibit a lower incidence of both informality practices across all firm sizes.

Who are the entrepreneurs in LAC?

The ES data confirms that family networks are still very strong in the private sector in Latin America and the Caribbean. For example, in 43 percent of the firms interviewed, the founder of the firm was still its manager at the time of the interview (and as pointed out earlier, the average firm in LAC is relatively old, with a regional average of 20 years). Among those firms in which the founder is still the manager, more than one-third (38 percent) were created due to lack of better employment opportunities, which also suggests the social function the family firm may be playing in the LAC region.

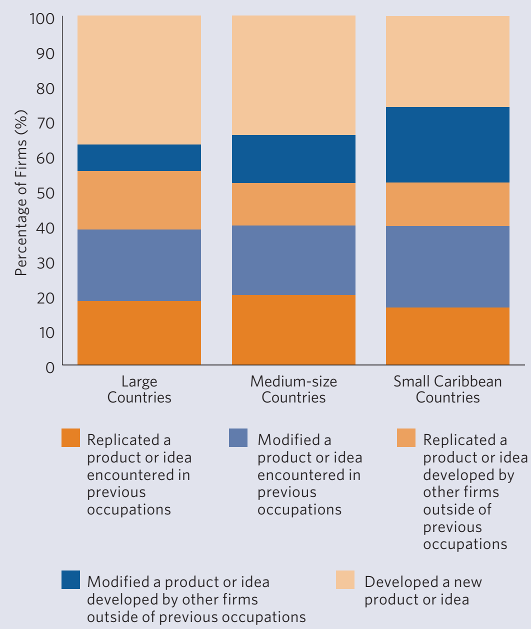
FIGURE 6 **PERCENT OF FIRMS THAT COMPETE WITH FIRMS USING UNREPORTED WORKERS**



Source: Enterprise Surveys.

Looking at firms that are managed by their founders, approximately two-thirds were formed by copying or modifying an idea from the founder's previous work experience (Figure 7). While entrepreneurial firms are often credited with being job and growth creators, firms that opened their doors to develop an original idea turn out not to be the best performers. In large countries—though not in medium-size or small Caribbean countries—firms that were founded to develop a new product or idea have significantly lower employment growth rates than those that were founded to replicate a product. Similarly, in these large countries, firms that began operations by modifying an existing product or idea performed less well than those that simply copied a business idea or product. These results hold after accounting for other potential explanations for the differences, such as sector of activity, firm age, exporting status, foreign ownership, and firm size.

FIGURE 7 **WHY DID YOU START YOUR BUSINESS?**



Source: Enterprise Surveys.

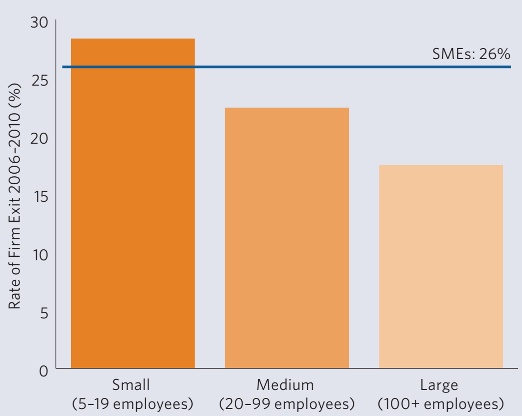
How do firms exit and enter the market in LAC?

The Enterprise Surveys also provide an interesting perspective on the evolution of the private sector over time. Given that the ES was implemented in 2006 in 15 LAC countries and that samples are representative of the formal private sector at the time of the survey, observing their evolution over time can develop a picture of the characteristics of firms that exit the market.[6] Between 2006 and 2010, one in four firms exited the market in LAC. Not surprisingly, SMEs exited the market at a higher rate than large firms: 26 percent of small and medium firms exited the market over this period, compared to 17 percent of the large firms (Figure 8).

The data show that firms with higher productivity in 2006, as measured by sales per worker, are more likely to remain in business in 2010 than less productive firms, after taking into account other potential explanations for their survival, such as firm size, sector of activity, etc.[7] This is an indication that despite the global economic crisis experienced during this period, the market economy of the region seems to have worked efficiently in driving the less productive firms out of the market.

The data also show that small and younger firms are significantly more likely to exit the market: an expected outcome, as older and larger firms have learned to deal with their business environment. Lack of access to credit also proved to be significantly associated with market exit, access to credit being a necessity for firm survival.

FIGURE 8 **SMEs ARE MORE LIKELY TO EXIT THE MARKET**



Source: Enterprise Surveys.

Endnotes

1. Lead authors: David C. Francis, Jorge Luis Rodriguez Meza, and Judy Yang, with the collaboration of the LAC report team.
2. This result is contingent on the “age” of the sampling frame used to draw the sample for each country, which varies across countries. Sample frames in the LAC region are not particularly older than those used in other regions of the world (typically 2 or 3 years old) and there is no reason why this should affect differentially the age distribution of LAC firms compared with the rest of the world.
3. Shareholding companies that do not trade their shares in the stock exchange.
4. For the Middle East and North Africa region and South Asia this information is available for very few, small countries in the region.
5. Brazil is not included in this analysis of informality or in the next section’s analysis of entrepreneurship, as the questions addressing these issues were not included in the questionnaire used in this country in 2009.
6. Not all firms from 2006 were selected for full ES interviews in 2010; in order to allow a representative sample of “fresh” firms (i.e., firms that were not previously interviewed), limits were placed on the number of panel firms interviewed in survey design. In order to gather data on whether firms exited the market, all firms previously interviewed were polled to determine if they were still in operation. However, due to response rates below 100 percent and issues emerging from the quality of contact information, certain assumptions were used to estimate exit rates. Here, in addition to all firms confirmed to be in operations, firms were assumed to be in operation if an answering machine or fax line was reached, the respondent directly refused the interview, or if the firm moved outside of the area covered by the survey design.
7. Age, exporting status, the annual growth in the manufacturing and services sectors, and senior management’s time spent on regulation.