

# Obtaining Finance in Latin America and the Caribbean<sup>1</sup>

## 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:

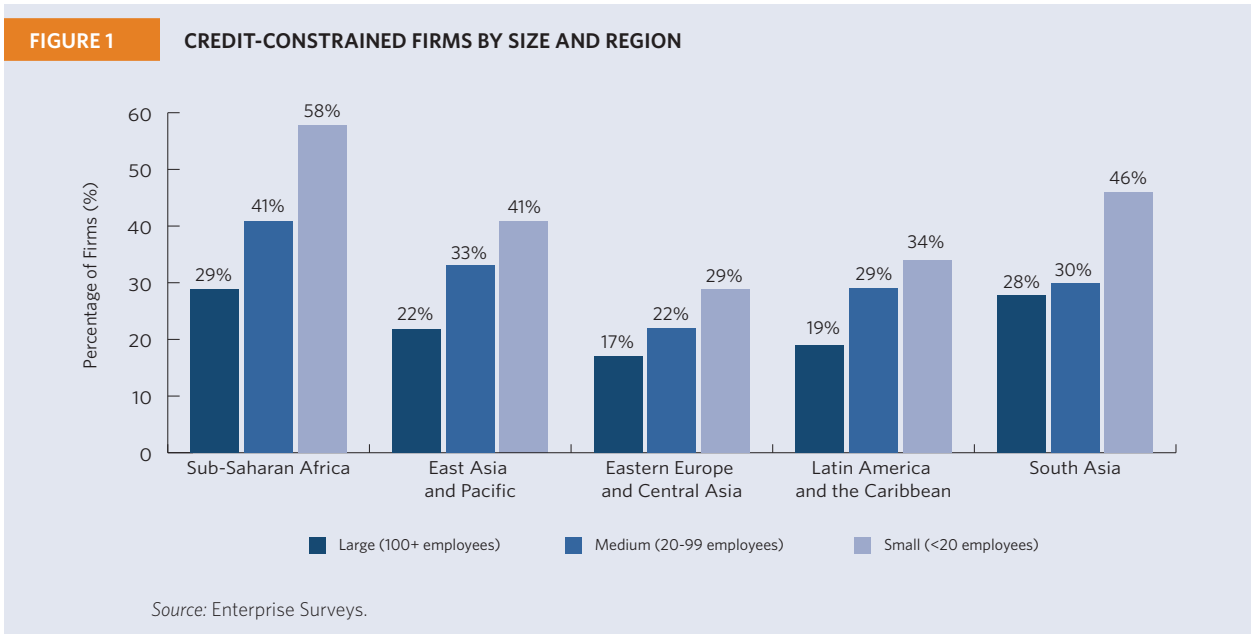
The information collected in the surveys refers to characteristics of the firm at the moment of the survey (2006, 2010 and 2009 for Brazil) or to the last completed fiscal year (2005, 2009, and 2007, respectively). In addition, sales, employment, and labor productivity annual growth rates are calculated 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.

## Enterprise Survey data provide detailed information on firms' applications for and use of credit, information that can be used to measure their credit constraint status

Firms use financial resources and services to make or receive payments and investments, or to manage cash flow. Firms often have insufficient funds to meet their needs and seek external financing from banks or other sources of credit. Good financial services are therefore crucial for firm growth. Enterprise Surveys measure the sources and uses of firm financing, including the sources of credit, the role of internal resources, and the utilization of financial services and instruments such as deposits, loans, and collateral.

Since the 1990s, the Latin America and the Caribbean region (LAC) has experienced accelerated growth in the banking sector, as well as in the bond and stock markets; financial market participation has also grown, as has financial inclusion. Enterprise Surveys make it possible to assess whether these developments have translated into greater firm access to financial markets and services, or if, as recent sources have speculated, the expansion has been biased in favor of consumption (de la Torre, Ize, and Schmukler 2012). Comparing survey responses in 2006 and 2010 can help determine whether private sector participation in financial markets increased between these years.

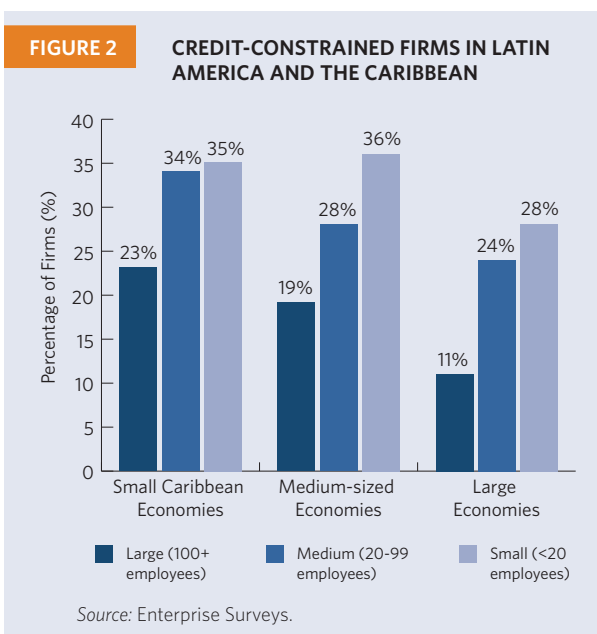
With respect to the credit side of financial services, the Enterprise Surveys collect rich information regarding firm-level financing decisions in the fiscal year prior to the surveys: the various sources of financing for working capital and investment on fixed assets; applications for loans or lines of credit from banking and credit-only institutions; the motivation for the applications as well as their approval or rejection. This information can be used to measure the extent to which firms were credit constrained.<sup>2</sup> All firms are divided into one of two categories: those that are non-credit constrained, and



those that are partially or fully credit constrained. Firms that are non-credit constrained are those that have received credit from financial institutions, or that are fully satisfied financing themselves with internal funds or using other external sources of finance.<sup>3</sup> Partially or fully constrained firms are those whose applications for loans or lines of credit were rejected by financial institutions, or those that did not apply for these types of financing

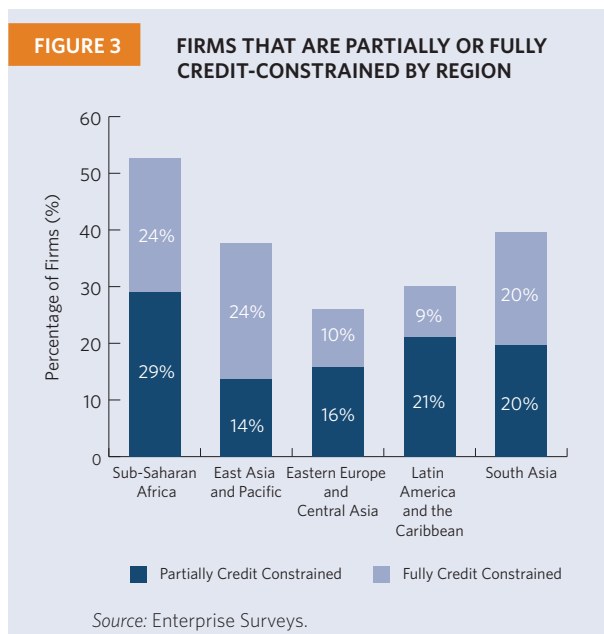
because of the prevailing market terms and conditions. Partially or fully constrained firms, consequently, had to resort to other sources of external finance or to their own internal funds.

### The Latin America and Caribbean region fares relatively well globally when it comes to the share of private sector firms that are credit constrained



Based on global surveys, nearly 38 percent of firms surveyed worldwide would classify as credit constrained. In the Latin America and the Caribbean region, the performance is better: less than 32 percent of firms fall into the credit constrained category. Indeed, LAC, along with Eastern Europe and Central Asia, are the two regions in which firms are least likely to be credit constrained. While small and medium-size enterprises are slightly more likely to be credit constrained in Latin America and the Caribbean than in Eastern Europe and Central Asia, they are considerably less likely to be constrained than similar firms in Sub-Saharan Africa, East Asia and the Pacific, and South Asia (Figure 1).

Within the LAC region, the small Caribbean countries have larger percentages of credit constrained firms than the medium-sized or large countries of the region (Figure 2). This result holds across all firm sizes: small, medium,



across countries. Some countries, such as Panama, Argentina, and Honduras, saw substantial increases in the share of credit constrained firms (increases of 17, 16, and 15 percentage points respectively). Meanwhile, in Bolivia, Paraguay, and Uruguay, the percentage of credit constrained firms fell by more than 10 percentage points over the same period.

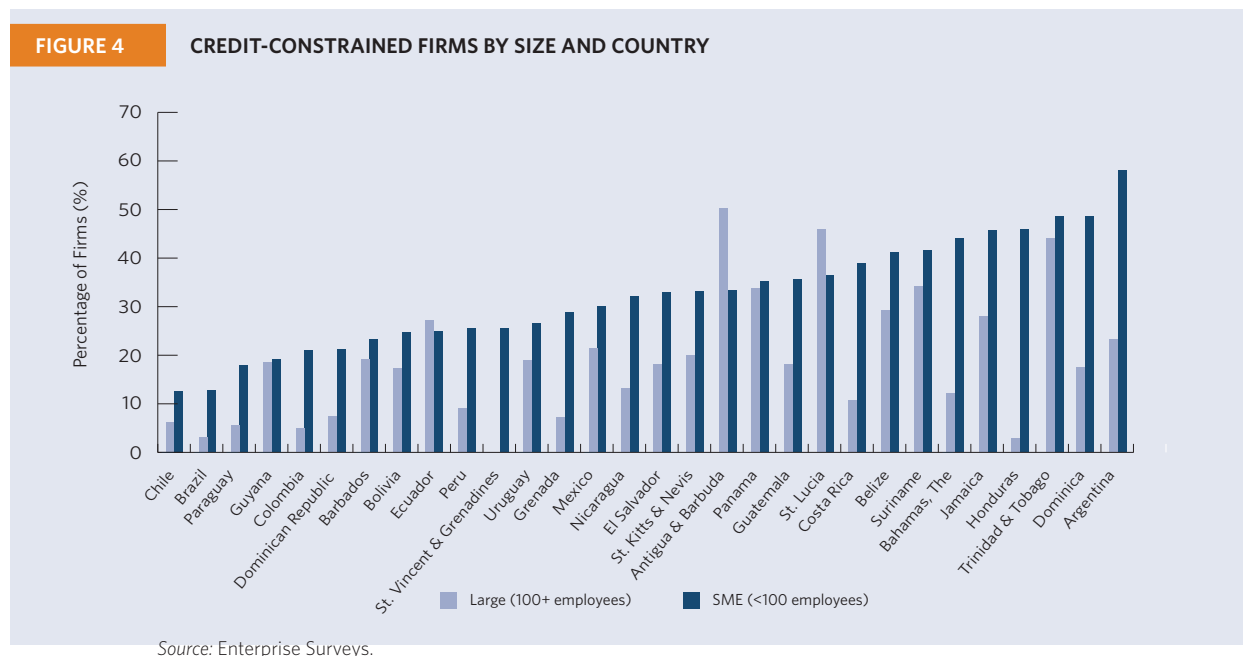
**Latin America and the Caribbean has the lowest share of fully credit constrained firms in the world but the second highest share of partially credit constrained firms**

Credit constrained firms are either fully or partially credit constrained. Both types were either explicitly rejected on their attempts to get credit from financial institutions or self-selected out of formal financial markets because of the prevailing market terms and conditions. Fully credit constrained firms, however, were also unable to raise any other form of external finance, whereas partially credit constrained firms were able to obtain some external finance from sources other than financial institutions, such as input suppliers, informal moneylenders or friends and relatives.

and large-sized firms. The large economies of the region exhibit, on average, the lowest share of credit constraint, across all firm sizes. Still, there is considerable variation even among large economies. In Chile, only 11 percent of firms are credit constrained, while in Argentina the figure is slightly greater than 54 percent.

Cross-sectional data from 14 countries surveyed in 2006 and again in 2010 show no major change in the share of credit constrained firms over this period, 27 percent and 28 percent, respectively. But there is large variation

The Latin America and Caribbean region, together with the Eastern Europe and Central Asia region, has the lowest share of fully credit constrained firms of all regions of the world for which Enterprise Survey data is available (Figure 3). The region’s share, 9 percent, is much lower than the global average of 17 percent. However, the LAC



region has a high share of partially credit constrained firms; the second highest share across all regions, behind only Sub-Saharan Africa. These results highlight the importance of alternative sources of external finance to the private sector in the LAC region.

Considered by firm size, there are large differences across countries in the percentage of firms that are credit constrained. Small and medium-size enterprises (SMEs) are more likely to be credit constrained throughout the region, except in three countries: Ecuador, Antigua and Barbuda, and Saint Lucia (Figure 4). On average, an SME is 1.7 times as likely to be credit constrained as a large firm: 32 percent for SMEs versus 19 percent for large firms. Considering only fully credit constrained firms, the four countries in the region with the largest proportion of fully credit constrained SMEs are in Central America: Panama, Honduras, Costa Rica, and Nicaragua. A fifth Central American country, Guatemala, is sixth on the list.

Comparing estimates from 2006 and 2010 for the 14 countries for which there is data for both years, it is possible to assess how the global financial crisis affected the financial condition of the formal private sector. The share of credit constrained firms increased only slightly, from 27 percent to 28 percent. Medium and large firms were more likely to experience an increase in credit constraint than small enterprises (Table 1).

**TABLE 1** CREDIT STATUS IN 14 LATIN AMERICAN AND CARIBBEAN COUNTRIES, 2006 AND 2010

Firm size	Year	Partially credit-constrained	+	Fully credit-constrained	=	Credit-constrained*
Small	2006	19%		14%		32%
	2010	17%		15%		32%
Medium	2006	14%		9%		23%
	2010	16%		11%		27%
Large	2006	7%		6%		13%
	2010	9%		7%		16%

\* Due to rounding error, percentages may not add correctly.  
Source: Enterprise Surveys.

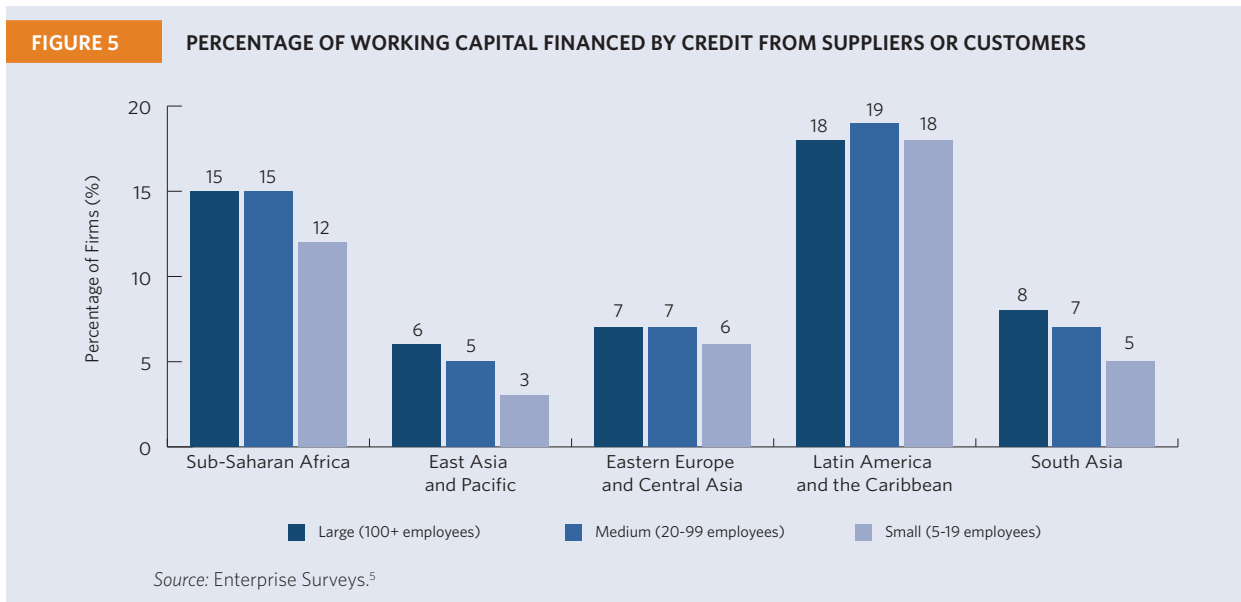
## Credit constrained firms in LAC are associated with lower productivity and low employment growth

Credit constrained firms in the region were significantly more likely to experience low labor productivity. Credit constrained firms are also associated with low employment growth. These results were found to be significant after accounting for other potential explanations, such as the age composition of the firms, their size, their type of ownership, and overall growth in each economy. These results, however, do not imply causality: productive firms might enjoy more access to credit because they are more productive, or firms might be more productive due to enhanced access to credit. Nonetheless, the association between performance and credit constraint seems to suggest that financial markets in the region are bringing capital to productive firms.

## Latin American firms rely more on external funds to finance their working capital than the average firm in the rest of the world

When it comes to financing for working capital, the results show that firms in Latin America and the Caribbean tend to rely more heavily on external sources than the average firm in other regions covered by the Enterprise Surveys. Thirty-eight percent of working capital in LAC is financed by external sources, while other regions of the world exhibit percentages below 30 percent. At the same time, there is great variation in the reliance on external sources of finance for working capital across countries, ranging from 8 percent in Panama to 60 percent in Colombia. Among the sources of external funds for working capital, firms in Latin America and the Caribbean rely more on credit from input suppliers and customers than any other region for all firm sizes (Figure 5). Bank financing is second in importance as a source of external finance for working capital overtaken only by credit from input suppliers and customers.

There is also variation in the reliance on external sources to finance working capital based on the size of the economy (Figure 6). Firms in the large economies of the region rely more on external sources to fund working capital than firms in medium-sized economies and in the small Caribbean countries. Also, firms in large economies utilize credit from input suppliers and customers more intensely than firms in medium-sized or small Caribbean economies.



### Investment in fixed assets in LAC are primarily financed with internal funds

The Enterprise Surveys also provide data on the sources of financing for investment in fixed assets. Internal funding constitutes the single largest source of investment finance in LAC, although it is considerably less important in large countries. In all 31 countries, investment is primarily financed through internal funds. In larger economies, credit from banking and non-banking financial institutions is relatively more important when it comes to financing investment than in medium-size economies and small Caribbean economies.

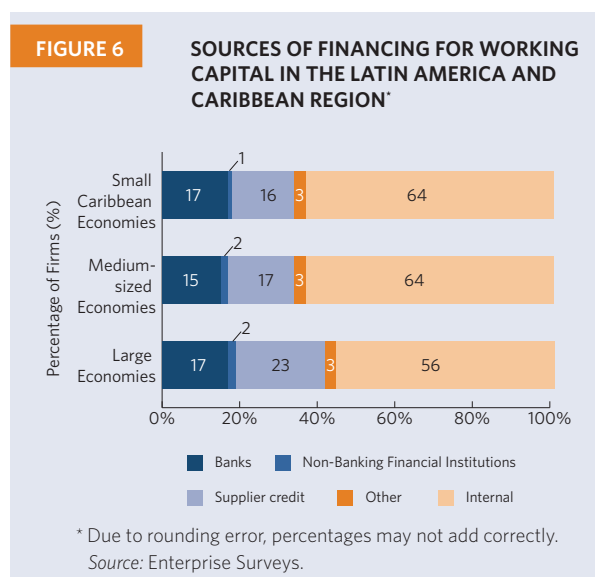
### The average firm in LAC is required to pledge collateral on bank loans at a lower rate than equivalent firms around the developing world

The LAC region exhibits the lowest share of firms required to pledge collateral when getting a loan or line of credit: 72 percent compared to a 78 percent global average. However, in almost all countries of the region collateral is required when getting a loan. In only four countries in the region—Brazil, Paraguay, Suriname and Peru—are fewer than half of the outstanding bank loans recorded as requiring collateral. Land or buildings are the

most common form of collateral. That said Brazil shows a surprisingly high use of accounts receivables as collateral.

### Private firms in LAC are well integrated with the deposit side of financial markets

The private sector in the LAC region is highly integrated with the deposit side of financial markets. At 93 percent, the average share of firms using deposit services in the LAC region is higher than in any other developing region of the world. The use of deposit services is high across



most countries in the region. In only four countries does the level of firms utilizing a checking or savings account fall below 80 percent: Nicaragua, Panama, Mexico, and Guatemala.

Overall, data from the Enterprise Surveys seem to indicate that in 2010 the private sector in the LAC region fared relatively well compared to other parts of the developing world when dealing with financial markets. The share of credit constrained firms is lower in LAC and so is the share of firms that are required to pledge collateral when getting loans. On the use of deposit services the region also fares relatively well compared to the rest of the world. These numbers seem to indicate that the region weathered the effects of the global financial crisis that started in 2008 relatively well compared to the rest of the developing world. However, there are a few signs of an increase in financial exclusion in selected countries: of the 14 countries with data available for 2006 and 2010, five of them show an increase in the share of firms fully credit constrained and in the share of firms not using deposit services.<sup>6</sup>

## Endnotes

- 1 Lead authors: Rita Ramalho, Jorge Rodríguez Meza and Judy Yang with the collaboration of the LAC report team.
- 2 For a more detailed discussion of the construction of the metric of credit constraints, see Kuntchev, Ramalho, Rodríguez, and Yang, 2012.
- 3 This group includes recipients of credit from financial institutions who may have been rationed in the size of the loan they received. They are part of the “Maybe Credit Constrained” category described in Kuntchev, Ramalho, Rodríguez, and Yang, 2012.
- 4 This is found to be significant after accounting for other potential explanations, such as firm size, age, foreign ownership and the overall growth in the economy. This was the case in 2006 for the 14 countries surveyed that year, and in 2010 for the whole region.
- 5 Data was not collected for most Eastern European and Central Asian countries.
- 6 Argentina, Honduras, Guatemala, Panama, and Peru.

## References

- Ayyagari, M., A. Demirgüç-Kunt and V. Maksimovic. 2006. “How Important Are Financing Constraints? The Role of Finance in the Business Environment.” World Bank Policy Research Working Paper 3820. World Bank, Washington, D.C.
- De la Torre, A., A. Ize, and S. Schmukler. 2012. “Financial Development in Latin America and the Caribbean, The Road Ahead.” World Bank, Washington D.C.
- Kumar, K., R. Rajan and L. Zingales. 1999. “What Determines Firm Size?” NBER Working Paper 7208. National Bureau of Economic Research, Cambridge, MA.
- Kuntchev, V., R. Ramalho, J. Rodríguez-Meza, and J. Yang. 2012. “What have we learned from the Enterprise Surveys regarding access to finance by SMEs?” Mimeo. World Bank, Washington D.C.

**Enterprise Surveys provide the world’s most comprehensive firm-level business environment data in developing economies.**

An Enterprise Survey is a firm-level survey of a representative sample of an economy’s private sector. The surveys cover a broad range of business environment topics including access to finance, competition, corruption, crime, gender, infrastructure, innovation, labor, performance measures, and trade. The World Bank has collected this data from face-to-face interviews with top managers and business owners in over 130,000 companies in more than 135 economies. Firm-level data and summary indicators are available on the website.