

# Understanding Structural Barriers & Hidden Bias in Access to Credit for Women-Led Businesses



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This report was written by Value for Women in February 2018, based on a full research study undertaken by Oxfam and led by Amanda Elam of Babson College in 2017.

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# Executive Summary

Women-led businesses are an important vehicle for enhancing women's economic opportunities and agency, and often lead to poverty reduction and economic growth. However, structural barriers prevent women from scaling their enterprises by limiting their access to the financial, physical, human, and social capital required to succeed. Approximately 70% of the world's women-led small and medium enterprises (SMEs) do not have access to finance or lack the amount of finance needed to grow. Gender gaps in access to formal credit is one of the principal barriers impeding women-led businesses from exploiting their full potential and economic opportunities. There are many structural barriers holding women back from accessing the resources needed to grow their businesses. However, one less explored (and more difficult to assess) challenge in emerging markets is that of hidden gender and ethnic biases in the financial system.

This report, designed for international development organizations, governments, and financial institutions, does the following: **1)** highlights the key barriers facing women-led small enterprises across the developing world; **2)** identifies how hidden gender and ethnic biases impact the growth of women-led businesses; **3)** presents the results of a pilot case study in Guatemala inspired by a novel methodology, first applied to mortgage lending in the United States, that seeks to test for bias in bank-lending decisions for small enterprises; and **4)** provides recommendations for policymakers and financial institutions on how this methodology can be applied in developing countries.

Oxfam commissioned Babson College in 2016 to conduct a pilot study in Guatemala about hidden gender and ethnic bias in access to bank credit. The study employed a "matched-control" mystery shopper research methodology to assess whether customer service and financial access were similar across demographic categories. To our knowledge, it is the first time this type of methodology has been implemented in a developing country. The goal of this pilot was to test this methodology for identifying hidden bias in financial institutions' lending practices in Guatemala and to make the tool and the lessons from this pilot available for policymakers and financial institutions in developing countries. The main lessons from the pilot study were twofold. First, perceptions of bias do not necessarily align with results on hidden bias on loan terms. While the study did not find any direct evidence of hidden bias in the loan application process, likely due to a number of key factors, it did, however, find that most bank loan customers perceive gender and ethnic bias, which suggests a problem specific to how banks communicate their willingness and interest to lend to women and indigenous groups. Further, hidden bias against women and indigenous people is likely to also operate through the structural barriers outlined above which were accounted for in the control variables. In other words, the study sample purposively selected men and women entrepreneurs who had already reached similar levels of growth in their businesses; for women and indigenous people in the sample in particular, this means that they likely had overcome some of the structural barriers that many of their counterparts still deal with on a daily basis. Second, methodological factors, such as controlling for all the different variables that may affect credit decisions by financial institutions, can affect the identification of direct gender and ethnic bias.

The report concludes by providing a set of recommendations for financial institutions and policymakers looking to employ a mystery shopper matched-control methodology, as well as for those interested in ensuring that financial services reflect the needs and preferences of women and women-led businesses.

# Gender Equality is a Moral & Economic Imperative

## **Recent gains on reducing gender inequality have been reversed.**

In 2017 the World Economic Forum's Global Gender Gap Index<sup>1</sup> increased to 32% on average, up from 31.7% in 2016. Although a minor increase, it's the first uptick since the Forum began tracking gender inequality in 2006, signaling that the public and private sectors need to reprioritize reaching gender parity.<sup>2</sup>

## **Gender equality is good for economic growth.**

Recent estimates suggest that if gender parity were achieved on a host of economic outcomes, additional global GDP would be USD \$28 trillion by 2025.<sup>3</sup> Even if countries only matched the gains towards gender parity of the best performing countries in their world region, additional global GDP would be USD \$12 trillion by 2025.<sup>4</sup>

Beyond GDP, **gains in women's labor force participation in emerging economies have led to poverty reduction.** Women's economic empowerment has important societal benefits as women tend to reinvest significantly more of their disposable income in their families' wellbeing than men. For example, from 2000 to 2010 increases in women's labor force participation in Latin America and the Caribbean (LAC) has contributed to decreasing extreme poverty by 30%.<sup>5</sup>

## **The importance of women's labor force participation for economic prosperity and women's economic independence necessitates a focus on entrepreneurship.**

In developing economies, women's labor force participation relies heavily on entrepreneurship, where self-employment and small businesses provide a majority of the jobs. <sup>6</sup> SMEs account for more than half of all jobs worldwide,<sup>7</sup> and their share of employment is comparable to that of large firms.<sup>8</sup> In developing countries, SMEs account for 66% of full-time employment.<sup>9</sup> Since women-led business owners also hire more women,<sup>10</sup> supporting women-run businesses has a multiplier effect that extends beyond the business into the wider community. While many women-led businesses are over-represented among informal microenterprises, the women leading small businesses with the potential to grow and provide more employment opportunities for men and women in developing countries are systematically overlooked or discounted. With approximately eight to 10 million formal women-owned SMEs in developing regions, women-owned SMEs represent a significant share of employment generation and economic growth potential. <sup>11</sup>

## **Growing economic inequality is bad for everyone.**

In 2017, the wealthiest 42 individuals in the world held the same wealth as 3.7 billion people. This figure is down from 388 of the wealthiest individuals in the world in 2010.<sup>12</sup> One of the key trends underlying this huge concentration of wealth is the increasing return to capital versus labor. In almost all rich countries and in most developing countries, the share of national income going to workers has fallen. Women make up the majority of the world's low-paid workers and are concentrated in the poorest paid and most precarious jobs.<sup>13</sup>

## **Finally, reducing gender inequalities is the right thing to do.**

Women's rights are human rights and women should be afforded the same economic opportunities as men. For Oxfam, gender justice is at the center of its vision to create a humane economy, one in which all people have an equal chance in life.

# Structural Barriers Prohibit the Growth of Women-Led Businesses

Major reasons why women lack access to income is that women-led small enterprises tend to be smaller, have fewer employees, and be in less economically productive industry sectors than businesses led by men.<sup>14</sup> Despite the clear benefits of gender equality identified above, not enough attention has been directed towards addressing the structural barriers stymieing women-led business growth.<sup>2</sup> **Figure 2** below outlines the challenges facing women-led businesses in developing regions, with a focus on the principal financial, human, and social capital constraints. Structural gender inequalities and biases (see Box 1 for definitions of these terms) restrict the growth of women-led businesses by hindering their access to key financial, physical, social, and human capital. We highlight two types of barriers: **1)** those that women face in growing their businesses and **2)** challenges in the supply of public and private sector services and programs for women entrepreneurs (see Figure 2).

## Box 1: Key definitions

**Structural inequality and barriers to gender equality:** Structural inequality concerns the distribution of individuals and groups across what sociologists call the “opportunity structure” in a society. Structural barriers to gender and ethnic equality include: **i)** horizontal segregation of women-led businesses in highly competitive, low-profit sectors that limit women’s access to high-value markets; **ii)** vertical segregation (representation in management and leadership positions); **iii)** horizontal and vertical and gender inequalities in educational attainment<sup>3</sup> for young women and girls; <sup>15</sup> **iv)** time and mobility constraints due to cultural norms and household and care responsibilities; **v)** high levels of physical and emotional violence against women in social and workplace settings; <sup>16</sup> **vi)** income and wealth stratification; **vii)** geographic segregation (e.g., food deserts and lack of access to transportation and communication services). <sup>17</sup>

**Hidden (unconscious) bias:** Hidden bias refers to the implicit and often unconscious associations made between a particular status, such as one’s gender or indigenous status, and a role or task (e.g., starting a business or caring for the sick) that results in cultural stereotypes, ideals, role expectations, and judgments of competence that affect our actions or decisions. In business start-ups, hidden bias perpetuates gender, ethnic, and racial inequalities that interfere with access to key resources, such as bank credit, for certain groups of people. These cultural biases result from, and systematically reproduce, the structural barriers to gender equality in a society.

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<sup>1</sup> The Global Gender Gap Index captures the magnitude of gender-based disparities and tracks their progress over time. It measures the progress of 144 countries towards gender parity on a scale from 0 (imparity) to 1 (parity) across four thematic dimensions—Economic Participation and Opportunity, Educational Attainment, Health and Survival, and Political Empowerment.

<sup>2</sup> This report focuses on women-led small enterprises. However, given the lack of sex-disaggregated data from global data sources, in some cases data points are only available for SMEs or micro-enterprises. Micro, Small, and Medium Enterprises (MSMEs) are defined by the standards established by World Bank: Micro (1-4 employees); Small (5-19); and Medium (20-99).

<sup>3</sup> While globally, primary, secondary, and tertiary enrollment for girls has increased substantially in the last two decades, girls continue to be underrepresented in high-growth tertiary education careers like those related to science, technology, engineering and math (STEM), which affects their ability to work and start businesses in these areas.

**Women-led micro, small, and medium businesses:** International organizations and governments have different definitions of what qualifies as a *woman-led or woman-owned business*. On the microenterprise end of the spectrum, where sole proprietorship and informality are the norm, it is easier to identify women-led firms based on the sex of the owner, but defining a women-led business becomes harder when dealing with small firms with multiple owners or decision makers. Generally speaking, women-owned is used in the literature and by international organizations to refer to firms with 50% or more ownership belonging to women, while women-led is for firms with women in key decision-making positions (e.g., CEO, president, general manager).<sup>18</sup> Most of the data in this report comes from the World Bank’s Enterprise Surveys that define a woman-owned firm as one that has at least one woman owner, or one with a female CEO or high-level manager.

**Figure 1: Selected Structural Barriers for Women-Led Business Growth<sup>4</sup>**

	<b>Challenges for Women Entrepreneurs and their Businesses</b>	<b>Challenges in the Supply of Services for Women Entrepreneurs and their Businesses</b>
<b>Financial Capital</b>	Lower levels of financial literacy and knowledge on financial products than men	Financial products, services, and delivery mechanisms are not tailored to women’s needs
	Female entrepreneurs like to have more information before making financial decisions and feel less equipped to maneuver complex procedures compared to their men counterparts	Explicit and hidden gender biases in the credit approval processes of financial institutions Financial infrastructure weaknesses, such as limited sex-disaggregated data related to women or high collateral requirements
<b>Physical and Technological Capital</b>	Less ownership of land and property, limiting collateral for credit and investment capital	Laws, regulations, and norms which are explicitly or implicitly biased against women’s ownership of property
	Women are less likely to own mobile phones than men	Lack of sex-disaggregated data on cellphone subscribers and unconscious biases within telecommunications organizations <sup>19</sup>
<b>Human and Social Capital</b>	Less business experience and skills	Business development services and delivery mechanisms not as accessible to women Lack of quality training and relevant courses
	Less access to appropriate local, national and international business networks	Gender norms and traditions in established informal and formal business networks
	Less access to appropriate formal and informal mentors	Insufficient formal mentoring programs or business development services with mentoring components
	Fewer women enrolling in tertiary-level education in high-productivity sectors like STEM	Lack of programs or scholarships to develop pipeline of women in STEM, and men-dominated work environments

<sup>4</sup> Developed by authors based on Inter-American Development Bank’s Gender and Diversity Sector Framework Document 2015 (IDB, 2015).

# Barriers to Bank Credit for Women-Led Small Enterprises

Women's inability to access finance prevents them from investing in their businesses and accessing new local and international markets. Lack of finance opportunities is especially harmful for businesses owned by ethnic minorities, who rely on finance for developing and growing new small businesses. For many female entrepreneurs, access to capital remains their biggest concern relative to other business problems.<sup>20</sup> For this study, financial services include not only credit but also services such as savings, insurance products, mobile payments, among others. Credit as a product is in no way monolithic. For microenterprises in particular, credit can be prohibitively expensive and hinder growth. However, for established small businesses credit provides a viable alternative for growth capital, albeit subject to the right conditions.

An estimated **70% of women-owned formal sector MSMEs in developing countries are unserved or underserved by financial institutions.**<sup>21</sup> The section below outlines the primary issues facing women and women-led businesses when accessing credit.

## **Collateral requirements limit women-led businesses' access to credit.**

Because women in developing regions often have less access to property titles, they are less likely to meet the collateral requirements needed to access bank credit (typically, about half of collateral required is in the form of land, real estate, or factories).<sup>22</sup> The gendered differences in asset ownership due to legal barriers (e.g., restrictions on owning and inheriting property), sector-specific factors (e.g., no or few physical assets in service-oriented businesses), or lack of savings are an additional barrier for women-led firms. Even when women hold property titles, bank collateral requirements are sometimes higher than the actual amount of the loan. In Paraguay and Costa Rica, for example, collateral requirements are 369% and 267% of the loan's value, respectively.<sup>23</sup>

## **High rejection rates for women creates a self-defeating cycle.**

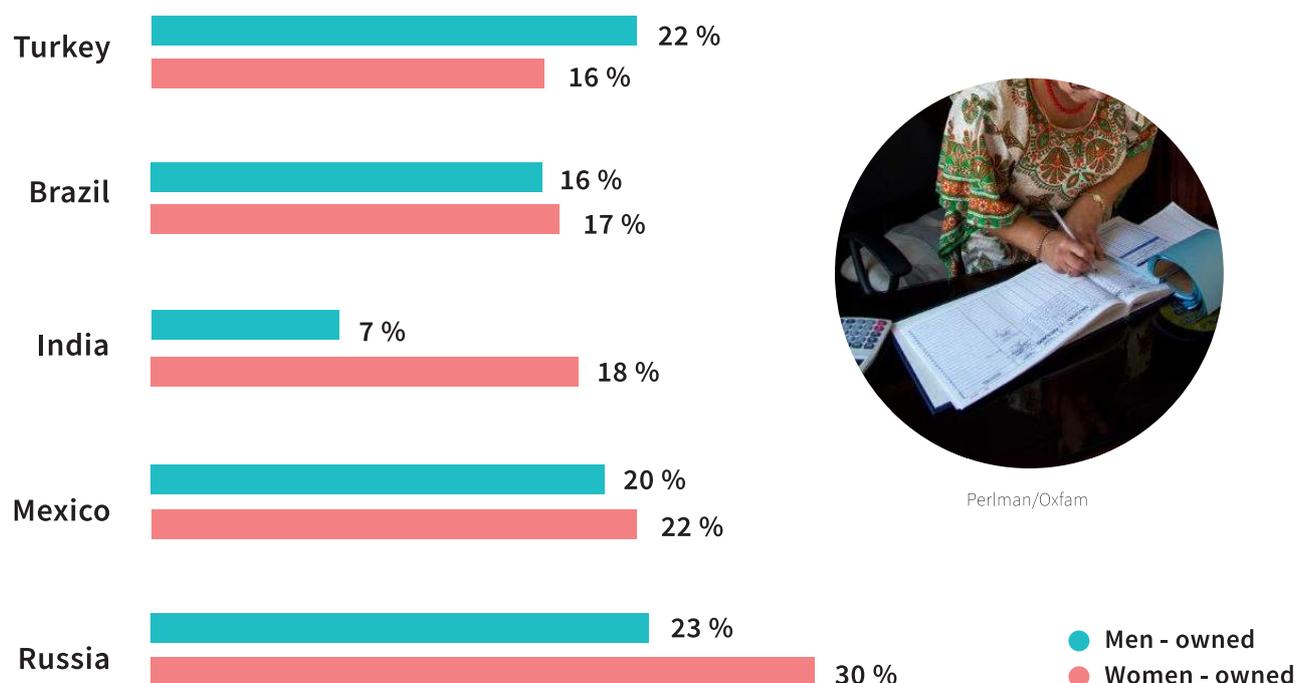
Evidence suggests that women are 5% to 15% more likely to have their loan applications rejected than men,<sup>24</sup> which helps explain why women business owners are often more reluctant to apply for business credit and avoid debt capital as a potential growth and/or development tool.<sup>25</sup> In fact, studies show that many women are less likely than men to seek capital from external financing because of low confidence and expectations of discrimination.<sup>26</sup>

## **Smaller business models designed to address a smaller, local market might also reduce the amount and odds of additional financing or capital resources.**

Banks are risk averse and their credit approval processes are designed for larger businesses and corporate clients rather than for small businesses. This preference for larger firms might inadvertently be a disproportionate disadvantage for women-owned firms as their businesses are, on average, smaller than men-owned firms. This overrepresentation of smaller businesses, in turn, impacts the likelihood of rejection, as well as interest rates and other loan terms. Importantly, women represent a majority of microenterprises in developing world regions and, as banks try to move to less saturated markets, they are viewing small businesses as a potential business opportunity. Larger banks are looking to "downscale" loan targets from large and medium businesses while microfinance institutions (MFIs) are looking to "upscale" to target SMEs. Unfortunately, although MFIs have a significant number of female clients in their portfolios, their upgrading and upscaling processes rarely consider the specific characteristics and needs of women, and thus lack a value proposition tailored to that growing client base.<sup>27</sup>

This is evidenced in female borrower drop-off rates as microfinance institutions commercialize and target larger enterprises. One study found that commercialization decreased the female portfolio of 25 MFIs from 88% to 65%.<sup>28</sup>

Figure 2: Loan Rejection Rates for Formal SMEs<sup>29</sup>



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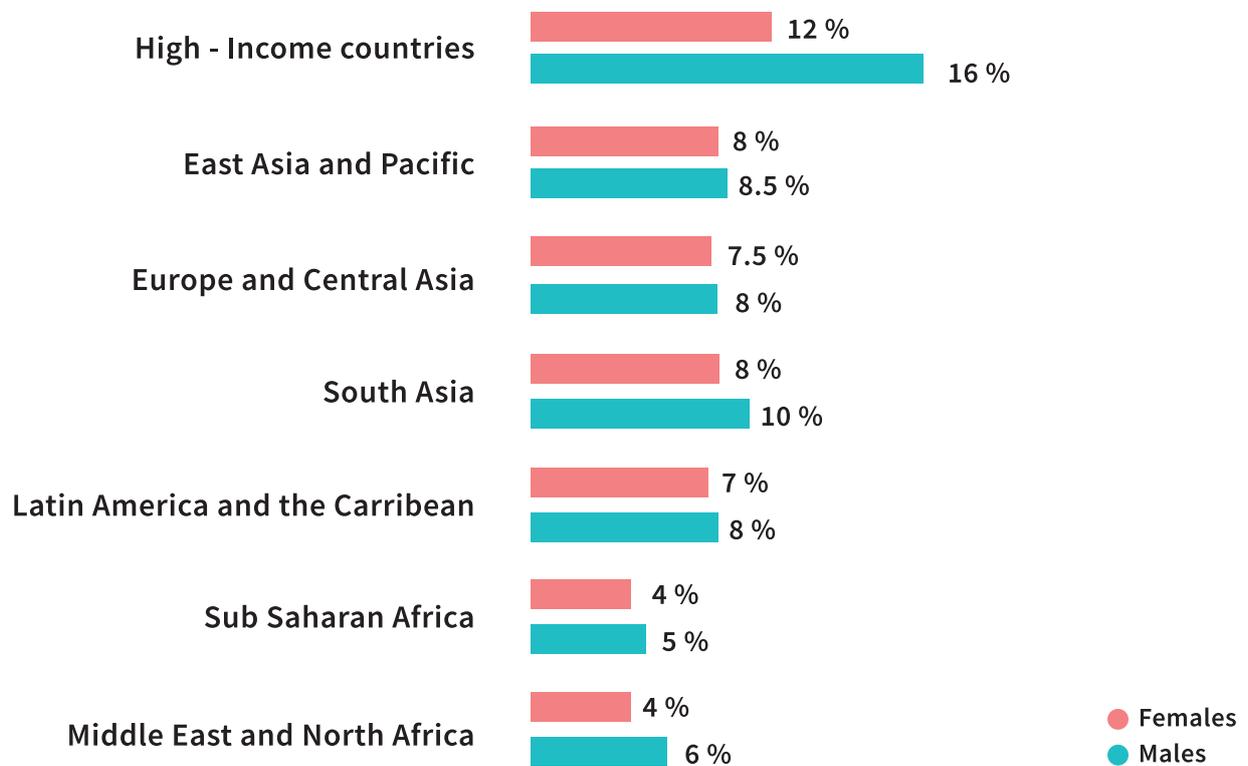
**High interest rates and credit costs are prohibitive for women-led small enterprises that can access credit.**

Women-led small enterprises with sufficient capital to access credit still often face high interest rates and credit costs. Such high risks cause some women to avoid taking loans. For example, women investors weigh risk attributes, such as the possibility of loss and ambiguity, more strongly than their men colleagues. In addition, women tend to emphasize risk reduction more than men in portfolio construction.<sup>30</sup> Women business owners may very rationally choose not to seek credit due to the high rates of rejection for women-led firms or exceedingly high costs of capital that pose a great risk to newer and small businesses.

**Due to structural inequalities, women-led businesses tend to be smaller and concentrated in lower productivity sectors. They also tend to have less credit history, fewer business assets, and less overall business experience.** Since significant financial education and business experience are often prerequisites in credit approval processes, women leading small enterprises are sometimes restricted from accessing credit from financial institutions. Women in developing countries are 20% less likely than men to have formal bank accounts, and 17% less likely to have borrowed money from a formal institution in the last year.<sup>31</sup>

Women business owners also tend to start out with less capital (debt and equity) and adopt more flexible and conservative start-up strategies than their male counterparts, which results in lower profits and long-term disadvantages in access to business financing.<sup>32</sup> In sum, much of the gender disadvantages in access to capital can be explained by structural inequalities, such as industry location, business age and size, and work experience.

Figure 3: Regional Breakdown of Gender Differences in Access to Business Credit for Starting or Expanding a Business or Farm <sup>33</sup>



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# Why Is Hidden Bias in Access to Finance Important?

**For the most part, the gender gaps in access to finance outlined above can be explained by structural variations in economies, businesses, and societies, as well as by business and personal characteristics;** however, even if all these factors are accounted for, gender gaps can still persist. In other words, when women and men entrepreneurs share the same characteristics (e.g., business, age, sector, size), gender gaps can persist in the form of a residual or unexplained effect at a given decision point which may be interpreted as evidence of discrimination or hidden bias.

## What Can't We See? Gender Stereotypes and Hidden Bias

**Gender stereotypes are one of the most common sources of hidden biases.**

Whereas women are often assumed to have more “communal qualities” like expressiveness, connectedness, kindness, and supportiveness, men are usually associated with more “agentic qualities” like independence, autonomy, and aggressiveness.<sup>34</sup> These gender beliefs often manifest into expectations of how men and women should perform and behave in the workplace. Because stereotypically manly characteristics align with stereotypical notions of leadership in most cultures around the world, women are often viewed as lacking leadership skills or, when asserting themselves, deemed as “bossy” or worse. Similarly, in many countries it is assumed that women entrepreneurs aspire only for smaller businesses or to supplement their family income, not to be the household’s main income earner.

**Many gender stereotypes are internalized and self-imposed.**

Research continues to find that women are less likely than men to see themselves in positions of power or capable of performing leadership roles.<sup>35</sup> Furthermore, often when women try to penetrate men-dominated industries, they are confronted with stereotypes that negatively impact their performance and leave them feeling emotionally down and inadequate.<sup>36</sup> These barriers are exacerbated by the lack of female role models in male-dominated industries. In Silicon Valley, one of the most privileged entrepreneurial ecosystems in the world, women remain underestimated, underfunded, and overtly harassed in their attempts to grow large, successful companies with venture capital funding.<sup>37</sup> Rarely are implicit and explicit bias formally regulated in venture capital contexts like Silicon Valley, where decision making remains highly discretionary.<sup>38</sup> On a positive note, when gender stereotypes are absent or mediated by mentors and advocates, women often become more motivated to pursue careers in traditionally male-dominated industries.<sup>39</sup>

**Gender interacts with other social status characteristics, such as race and ethnicity, in both developed and developing countries.**

This “intersectionality” refers to “the interaction between gender, race, and other categories of difference in individual lives, social practices, institutional arrangements, and cultural ideologies and the outcomes of these interactions in terms of power.”<sup>40</sup> In reality, one’s social status or legitimacy is rarely based on one characteristic such as gender, class, or indigenous status, but rather on how these characteristics overlap and intersect with one another.

**Research on status expectations further reveals that status discrimination is “task dependent” in that the positive and negative expectations associated with a given status characteristic are linked to a particular task** set and adjusted based on more specific information, like prior experience or perceptions of performance. For example, some people might expect that a man might be better than a woman at changing a tire, until they learn that a woman has previously worked as a mechanic or after witnessing her change a tire. Research has shown that in the case of male-linked task sets, women are held to a higher double standard than men and must perform twice as well to overcome preset expectations of competence.<sup>41</sup>

## Hidden Bias in Bank and Credit Approval Processes

**Hidden gender biases also help explain the gender pay gap.**

The often-reported USD \$0.82 on the dollar gender wage ratio or 18% gender wage gap in the United States is a raw figure<sup>42</sup> exacerbated by other social status characteristics like race, ethnicity, and indigenous status. In the US, Hispanic and African American women were paid only 54% and 64%, respectively, of what white men earned in 2013.<sup>43</sup> From a social reform perspective, these numbers can be misleading. They ignore, for example, factors such as industry, education, and experience. In fact, when key factors like occupation, industry, and work experience are controlled for, the US gender wage gap shrinks to 4%. In other words, most of the raw gap in pay can be explained by structural differences that have less to do with what happens in any given company than with social arrangements that influence how we organize ourselves in society through our private and public roles. **Part of this 4% comes from unexplained “hidden bias.”**

In LAC, for example, the unexplained gender pay gap still ranges between 9% and 27%.<sup>44</sup> A similar approach for determining the gender pay gap can be used for identifying hidden bias and the gender gap in access to finance. It involves identifying the residual gap that remains unexplained after controlling for key explanatory factors. Indeed, the pilot study, the results of which are highlighted in this report, was designed to do just that: **(1)** to calculate the gender gap in access to finance by isolating the residual differences and **(2)** to unpack the concept of hidden bias in the loan application experience of Guatemalan business owners.

**Financial institutions often defend lending decisions on the basis that the rules are standardized or differences are linked to structural inequalities.**

However, policies may not be applied equally at the individual level and systematic knowledge about these tendencies is scarce. The presence of bias in credit decision making is often visible on a system level or at the national level, not at the individual bank level, therefore not allowing investigators to analyze discriminatory practices in depth. As a result, the role of hidden bias in reproducing inequalities remains poorly understood and is not accepted nor monitored by most financial institutions in emerging markets.<sup>45</sup> This situation is due to a variety of factors, including the fact that financial institutions have to identify the problem and difficulty in reproducing studies that can identify bias by controlling for the structural inequalities and norms that lead to bias in credit approval processes.

**Although identifying hidden bias in credit approval processes is difficult, several studies have attempted to do so.**

One of the earliest studies from the 1980s in the US showed that lenders ascribed more favorable professional attributes to men borrowers than female borrowers.<sup>46</sup> Whereas men were evaluated more favorably than women on nine professional characteristics (persuasiveness, low need for support, low conformity, leadership, autonomy, propensity to take risks, readiness for change, endurance, and lack of emotionalism), women were evaluated more favorably on just two characteristics: low conformity and endurance. Other studies have found that although women were just as likely to receive funding, they still felt more discriminated against than their male counterparts; studies have also shown that women tend to feel less satisfied with their banking relationships, even if they receive similar treatment to their men colleagues.<sup>47</sup> These studies also demonstrate the difficulty in identifying hidden bias in loan application processes and the need to control for as many factors as possible when designing such studies.



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**Preconceived notions about gender can affect the decision making of bank staff.**

For instance, a recent study in Albania found that borrowers assigned to loan officers of the opposite sex pay higher interest rates and receive shorter maturities but not higher arrears.<sup>48</sup> In a second study examining 696 matched firm owner/manager–bank manager pairs, researchers found that male–male pairs of business owner/managers and bankers had the highest levels of trust, satisfaction with credit access, and bank knowledge, while female–female pairs had the lowest levels for each measure; with mixed pairs in the middle on all accounts.<sup>49</sup> These results suggest that gender status is an important factor in the loan application process.

**While women business owners are sometimes perceived as more risk averse and less likely to take chances in their small businesses, in fact women tend to approach business in much the same way as men.**

According to a recent study sponsored by the Bank of Montreal, business people, as well as academics, tend to view women entrepreneurs as less likely to engage in aggressive growth strategies or to take on risk that might ultimately enhance their business performance and/or operations. However, this study concluded that women entrepreneurs are equally as ambitious as their men counterparts and are committed to growing their business.<sup>50</sup> Oddly, there is a “catch 22” in that women are considered less credit worthy even if they are less likely to take high risks with credit.

***If financial institutions are not part of the solution,  
they may be part of the problem.***

## What Do Banks Have to Do with It?

**You Can't Solve a Problem You Don't Know You Have.**

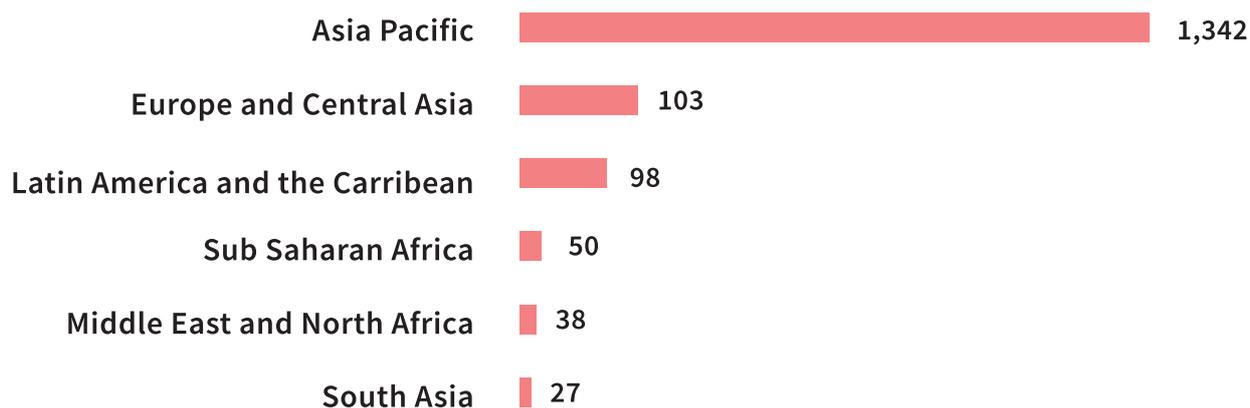
Even with all the data cited above, financial institutions in developing regions do not readily identify the differentiated needs of women-led businesses and the hidden biases that limit their access to credit. For example, a 2016 survey of 100 banks in LAC found that only 28% of banks thought that the women-led SME market was unserved. While this figure increased from 9% of surveyed banks in 2012, it still suggests a disconnect between banks and their female customers.<sup>51</sup> Tellingly, only 33% of the banks surveyed had the sex-disaggregated information necessary to identify women- and men-led SMEs. These trends are also reflected worldwide. A Global Alliance for Women (GBA) and McKinsey & Company study interviewed over 30 CEOs and other senior bankers from financial institutions and found that many banks continue to think that male and female clients are the same and that there is no “business case” for serving the female market. In many cases, financial institutions believe they are “gender neutral” and do not give preference to any particular sex.<sup>52</sup> In practice, of course, this implies a failure to recognize and understand the differentiated needs of women and men clients.

# Financial Institutions Are Letting Go of a Good Market Opportunity

Leaving out the impact women-led businesses have on creating inclusive economies and reducing gender inequalities, financial institutions are also overlooking a huge market opportunity—USD \$1.7 trillion USD to be precise. That’s the yearly demand of women-owned SMEs in emerging markets not met by financial institutions. In fact, by ignoring the growing demand and particular characteristics of women-owned SMEs, financial institutions may be missing some of their best potential customers.

***The gap between what women-owned SMEs demand per year in emerging markets and is not met by financial institutions is \$1.7 trillion.***

Figure 4: Credit Gap<sup>5</sup> for Women-Owned SMEs by Region (in USD \$ Billions) <sup>53</sup>



<sup>5</sup> The credit gap is the difference between what women-owned SMEs demand per year in emerging markets and the demand not met by financial institutions.



**Women-led SMEs tend to be better at repaying their loans.**

Global research has found that women are better at paying off their loans than men. One study of worldwide banks that are part of the GBA found that the nonperforming loan rate for women small-business customers is only 2.7%—33% lower than the rate for men. <sup>54</sup>

**Women tend to save more than men.**

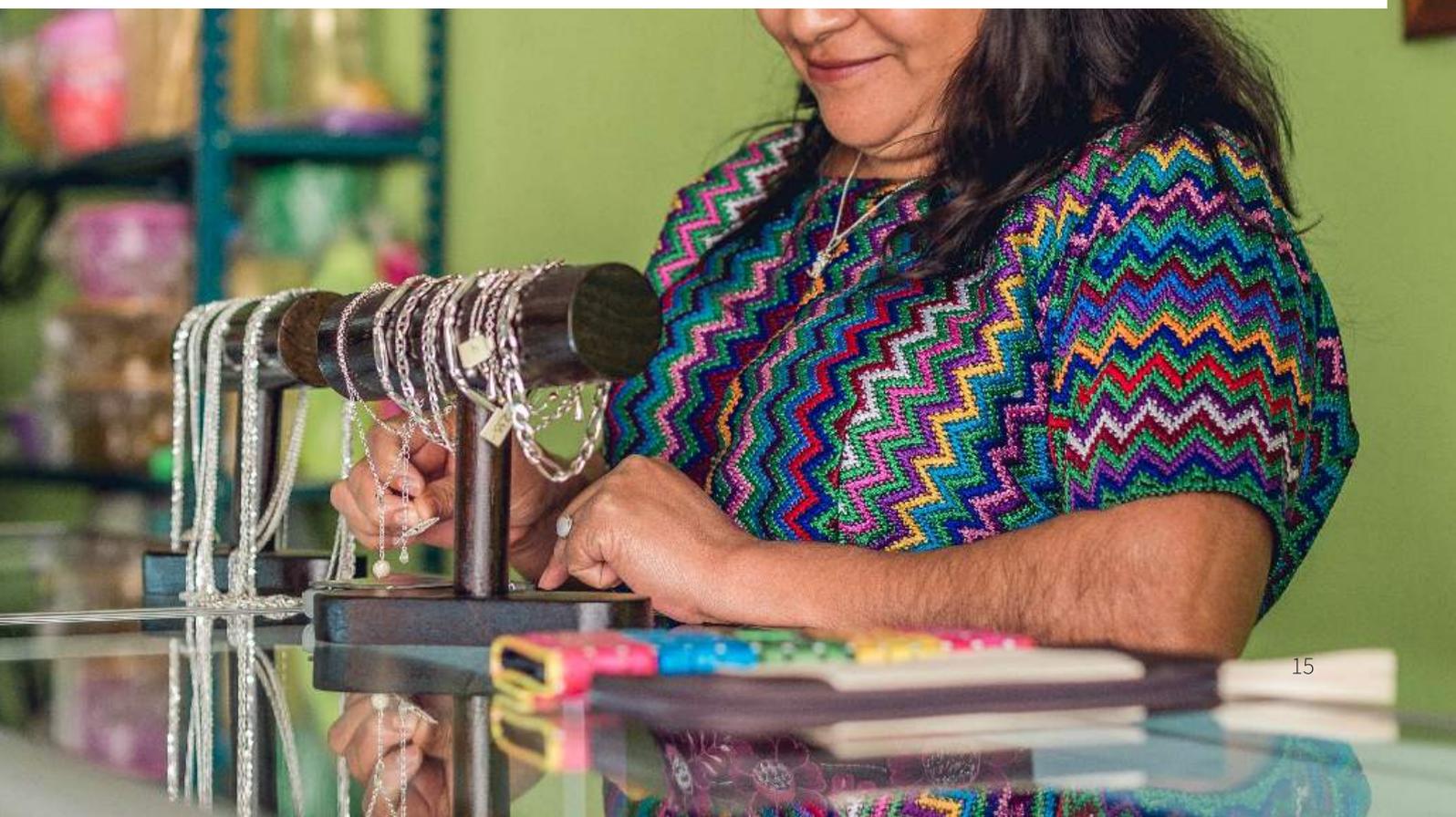
Although women are 20% less likely to have borrowed from a financial institution, they are only 14% less likely to have a savings account. <sup>55</sup>

**Banking on women is good for profits.**

The GBA database shows that 34% of bankers that have identified and targeted the women-led SME market report increased profits as a result of their efforts to empower women in emerging markets. <sup>56</sup> According to data published in case studies by the GBA, Banco BHD Leon in the Dominican Republic reported that its women's program had an internal rate of return (IRR) of 35% in its first year, while BLC Lebanon had an IRR of 33% in the first three years of its women's program. <sup>57</sup>

**Nevertheless, globally almost three quarters of women report being dissatisfied with their banking services.**

In a 2009 study of women in 21 countries, women were more dissatisfied with the financial services industry than any other service that affects their lives. <sup>58</sup>



# Case Study: Testing for Hidden Bias in Access to Credit by Gender and Indigenous Status in Guatemala





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# Guatemala Context and Women's Entrepreneurial Ecosystem

**Guatemala was chosen as a pilot case study given its high levels of inequality and poverty, as well as the presence of Oxfam projects looking to support the growth of women-led businesses through access to finance and business development services.** Wealth in Guatemala is unevenly distributed with well over half of the population subsisting below the national poverty line and nearly a quarter living in extreme poverty. The GINI coefficient in Guatemala is 48.7,<sup>6</sup> making it one of the most unequal countries in LAC. Indigenous people constitute 41% of the national population, yet represent almost 80% of the poor and most of the people living in extreme poverty.<sup>59</sup>

The women's entrepreneurship ecosystem in Guatemala is one of the least developed in the LAC region. In 2013, the Economist Intelligence Unit (EIU) and the Inter-American Development Bank (IDB) analyzed and ranked the entrepreneurial ecosystem for women in 20 LAC countries. The five categories were: **i) Entrepreneurial Business Environment; ii) Business Operating Risk; iii) Access to Finance; iv) Social Services; and v) Education and Skills.** The Women's Entrepreneurial Venture Scope (WEVentureScope) ranked Guatemala 16th out of 20 countries surveyed in terms of overall environment for female entrepreneurs, mainly due to low performance in the business environment and capacity and skills categories of the entrepreneurship ecosystem.<sup>60</sup> **Guatemala ranks 88th out of 190 countries in the World Bank's Doing Business** database, as it takes about twice as long and is twice as complicated to start a formal business in Guatemala compared to highly developed countries.<sup>61</sup>

**Additionally, Guatemala ranks in the bottom half of the 62 countries measured in the 2015 Global Entrepreneurship Monitor data** and ranked rock bottom in entrepreneurial finance and government policies supporting business start-up and growth. According to data from the Global Entrepreneurship Monitor (GEM), the female-to-male Total Entrepreneurship Activity (TEA) ratio in Guatemala is a dismal 0.7, compared to an 0.8 average across the countries in the LAC region.<sup>62</sup> Similarly, 45% of Guatemalan women respondents perceive opportunities for enterprises compared to 80% of Guatemalan men. In the public sector, the Ministry of Economy offers basic business development services to SMEs via 11 regional centers, albeit not targeted specifically towards women. Between 2008 and 2010, some 30,000 entrepreneurs took advantage of these services, 58% of whom were women, which suggests significant demand for business development services by Guatemalan women business owners.<sup>63</sup>

## **Regulatory barriers also restrict women-led business growth.**

For example, in Guatemala it is not illegal to discriminate based on gender or marital status when making credit decisions. Moreover, no laws exist that prohibit discrimination based on gender in hiring or mandate equal remuneration for work of equal value.<sup>64</sup>

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<sup>6</sup> The Gini Index measures the extent to which the distribution of income (or, in some cases, consumption expenditure) among individuals or households within an economy deviates from a perfectly equal distribution. A Gini Index of 0 represents perfect equality, while an index of 100 implies perfect inequality.



As of January 2016, Guatemala's National Statistics Institute reported 260,800 active companies in the MSME sector. **Women-led enterprises in Guatemala have fewer employees than their men-led counterparts, are concentrated in micro and small firms, and hire more women.** The World Bank 2010 Enterprise Survey found that while 22% of small firms had a female top manager, only 9% of medium firms and 3.5% of large firms had female leaders. Further, formal firms with female top managers have a higher percentage of full-time female workers (50%) than those without female participation (29%) in top management.

**Like in many other countries, in Guatemala access to finance is a major constraint for the growth of women-led businesses.**

The percent of GDP represented by domestic credit to the private sector (34.4%) is one of the lowest in LAC, which means that for both women- and men-led businesses access to credit is a major constraint to growth. Enterprise surveys in 2010 revealed that 45% of SMEs with a female top manager in Guatemala had a loan or line of credit from a financial institution compared to a total of 60% for all SMEs in the country and significantly lower than regional peers such as Chile (74%), Colombia (64%), and Costa Rica (51%).<sup>65</sup> Further, 50% of women-owned SMEs in Guatemala are underserved (i.e., have access to credit or overdraft but continue to note finance as a major constraint for growth) compared to 44% of SMEs led by men. In part, this is due to the fact that the value of collateral needed for a loan for women-led SMEs in Guatemala is 158%, almost double the required collateral assigned to their men-led counterparts.<sup>66</sup>

**In Guatemala, only 24% of working capital and 13% of capital investments for women-led SMEs are financed by banks and 0% by supplier credit.**<sup>67</sup>

The low percent of capital investments presents a particular challenge for growth where women want to transition from micro businesses to SMEs. It also constitutes an important opportunity for financial institutions.<sup>68</sup>

From 2011 to 2014, the World Bank Global Findex showed a **doubling in the percent of Guatemalan women holding bank accounts from 16% to 35%**, and an increase in account ownership for men from 30% to 48%, resulting in only a slight improvement in the gender gap in account ownership from 14% to 13%. Importantly, men's and women's account ownership is still well below the LAC average, and gender differences remain in relation to the use of financial products and services for personal and business use. The gender gap widens again when looking at formal financial savings, which are low overall with 13% of women having saved in 2014 compared to 17% of men. Among the 51% women who saved any money in the past year, only 14% were able to save to start, operate, or expand a business (or farm) compared to 22% of men.<sup>69</sup>

## Using a Mystery Shopper Tool to Test for Gender and Ethnic Bias

Because of the role bias can play in holding back qualified female loan applicants, it is important that testing for hidden bias become routine within emerging market banking systems. However, in our cross-country review of emerging market regulatory paradigms, we found no tools currently being used by banks to self-test for the existence of gender bias in credit decision making. In order to test a tool to identify hidden biases in credit approval processes for financial institutions and regulators, Oxfam and Babson College teamed up to conduct a pilot study in Guatemala. The **purpose of the pilot study was twofold:**

**i)** to investigate the direct influence of direct hidden bias against women business owners in financial lending processes, in particular indigenous women, and help expand the current knowledge base around the relationship between financial exclusion and economic inequality; and **ii)** to identify lessons learned in an initial test of a self-assessment methodology in a LAC setting.

## Figure 5: Background on US Self-Assessment Methodology

In 1994, the US Federal Deposit Insurance Corporation (FDIC) published guidelines for institutions to examine and compare their treatment of loan applicants. Using a self-assessment tool, the guide helps institutions assess cases of uneven, or potentially discriminatory, customer service in lending practices. The tools are designed to support financial institutions assess their treatment of different types of loan applicants, so that steps can be taken to correct system inequalities. Due to the methodological complexity involved in comparing loan terms and conditions, the technique is limited to comparing bank staff's differential treatment of loan customers. A self-assessment program should be employed to ensure equal access to loans and adequate programming to support the sourcing of good loan customers.

This study developed and tested a “mystery shopper”<sup>70</sup> research methodology designed to help banks quickly collect and analyze data about hidden bias, and the perception of bias, as it relates to gender discrimination in lending decisions. The mystery shopper methodology captured the perceptions and experiences of applicants—from the initial visit to the loan decision—as they went through the process of applying for loans. The study recruited 12 matched pairs of men and women business owners, half indigenous and half nonindigenous, from two different municipalities in Guatemala. Each participant was assigned five bank locations for in-person visits and loan application submissions. Controls were ensured through matching criteria, including business size, annual sales, industry, product/service category, age, and education, as well as through basic training on the loan application process. We compared access to credit for indigenous and nonindigenous men- and women-owned small businesses in Guatemala. Questions included a combination of closed and open-ended questions to measure perceptions and to capture first-person narratives. Video interviews provided both first-person narratives and an additional control for personal presentation factors.

To our knowledge, this is the first time a mystery shopping research methodology has been used to test not only perceptions of the loan application process, but also actual lending decision outcomes in an academic study. The field team hired to recruit and train participants and to collect the data worked through local municipalities to recruit men and women business owners. However, limited resources meant the pilot had a smaller sample size than initially intended, limiting the statistical power of the results (see Annex I for a section on Methodological Limitations and Challenges). The intended focus of the study was on microbusinesses—informal or formal microenterprises outside of a university incubator setting; however, the resulting sample ended up being all formal, registered businesses, almost all established, with only a few microenterprises included.



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# Key Findings & Conclusions

The use of mystery shopping method studies that test for bias has typically been limited to examining the experience of clients from different demographic groups by frontline bank staff. In this study, the mystery shopper approach was combined with a matched control design to investigate differential treatment and examined through two distinct ways: **i)** a comparison of self-reported loan terms and conditions offered by banks and **ii)** reflections from entrepreneurs about the differential treatment by bank staff. **While the study findings did not support the direct influence of hidden bias with the loan terms and conditions offered, participants nonetheless perceived gender and ethnic biases during the loan application process.**

This result is explained in part by the matched control design which isolated the direct influence of gender and indigenous status on the loan application experience and loan decision outcomes. The small sample size also resulted in lower statistical power, which means that many of the predicted differences, while observed, were not statistically significant. This result is likely due to the difficulty of identifying structural biases in such a small sample size, as well as to the lack of a more comprehensive list of control variables (e.g. profitability and credit history). Most applicants (men and women) reported that gender and indigenous status played a role in how well or poorly customers were attended to by bank staff. The findings indicate a strong awareness of the cultural biases pervasive in Guatemala and which banks could become acquainted with and seek to address if they want to be part of the solution. Only 30% of applicants received loan offers—this despite having received training and tips from research staff on the loan application process and what banks looked for in small business loan applicants. Still, these loans were offered at very high interest rates, on par with those of credit cards. While participants were more satisfied with some banks than others, on the whole applicants were disappointed with the process and outcomes. In sum, for this pilot study the mystery shopping tool proved useful in identifying perceptions of bias and documenting customer (dis)satisfaction with both the products and services provided.

## No Direct Hidden Bias - Hidden Bias Operates Through Many Factors

**The pilot study did not find significant differences in loan awards by gender alone.**

In fact, female applicants tended to receive larger loan amounts and longer terms than their male peers. Indigenous women business owners (IWBOs) reported the longest loan terms—27.3 months—compared to all other groups who averaged 16.2 months. These results are explained largely by the matched control design which isolated the direct influence of gender and indigenous status on the loan application experience and loan decision outcomes. In other words, loan decisions and terms were largely explained by the control variables, including industry, business size and age, loan amount requested, and the age and experience of the business owner. The small sample size also resulted in lower statistical power, which means that many of the predicted differences, while observed, were not statistically significant.

The differences observed by gender and indigenous status suggest that, **while hidden biases exist, they work in complicated ways to influence loan decisions and individual experiences during the loan application process. Hence, focusing on hidden bias is necessary but not sufficient.** This study was designed to support a residual analysis, a focused investigation on perceptions and evidence of discrimination among small business loan applicants in Guatemala. In this study, hidden biases work largely through mechanisms of structural inequality to influence bank-lending decisions. Moreover, these hidden biases vary significantly from person to person, resulting in different perceptions, understandings, and salience of gender and indigenous status in the loan application process. The pilot study sought to level the playing field by identifying women, men, and indigenous entrepreneurs who had already reached similar levels of growth in their businesses, thus helping to reduce the structural gender biases inherent in the wider economy.

**The study also did not find discrimination with respect to ethnic status.**

Surprisingly, indigenous business owners were almost twice as likely to receive loan awards compared to their nonindigenous peers (44% vs. 23%) and were significantly more likely, on average, to request higher loan amounts than nonindigenous applicants (approximately USD \$2,595 vs. \$1,508).<sup>7</sup> Contrary to our expectations, nonindigenous women business owners (NIWBOs) had the lowest loan award rate in the sample, at about half of that observed by indigenous business owners. This surprising finding is likely due to differences in business and personal characteristics between indigenous and nonindigenous business owners. The study's matching criteria controlled for gender, but not indigenous status. As a result, indigenous owners tended to be older with businesses that had been in operations for longer, while non-indigenous women tended to be younger and to run smaller, newer businesses than other business owners. Another possible explanation is that since the study was conducted in San Marcos and Quetzaltenango—regions of high indigenous concentration—the status factors that we might expect in other less homogenous regions were less evident.

**While the results did not show any evidence of direct effects of hidden bias, other international studies (summarized in previous sections of this report) about the factors impacting bank credit suggest that in our study of Guatemalan business owners, hidden bias against women and indigenous people likely operates through the structural barriers described above which were accounted for in the control variables.**

These findings are consistent with a gender system theory perspective on access to bank credit as well as prior international studies (summarized in previous sections of this report) on bank access to credit. In other words, the men and women picked for the study were carefully chosen, and women and indigenous entrepreneurs have overcome many of the structural gender barriers that many of their counterparts are dealing with on a daily basis. Compared to men business owners, women are overrepresented among the smaller, younger, and informal businesses in industries that are less attractive to banks. Structural gender biases and inequalities result in women being less likely than men to hold bank accounts, own property, and have established creditworthiness. Indigenous people are also more likely to run smaller, informal businesses and, compared to nonindigenous business owners, are less likely to hold bank accounts, own property, and have established creditworthiness and received financial education. These fundamental differences put indigenous people, indigenous women in particular, at a greater risk of being denied loans than indigenous men and nonindigenous men and women.

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<sup>7</sup> Amounts calculated using an average exchange rate of 7.45 Quetzals per United States Dollar.

# Perception Matters

Participants perceived gender and ethnic biases in the application process. The study uncovered multiple contradictions between the reality of loan offers and the perceptions of the individual borrowers.

## **Women reported discriminatory behavior from loan officers.**

Generally, women felt discriminated against and that they would have been treated better if they were men. Some men, however, felt they were discriminated against for being men. Women's and men's perception of discrimination may impact their behavior during loan application processes and influence the quality and satisfaction level of their experience. This highlights the need for financial institutions to better understand the needs and preferences of their male and female clients and change their procedures accordingly.

***Yes, I think it is easier for a man. I was asked if I was married in at least two institutions. In Enterprise Bank, I was told that it would be better if a man opens the account instead of me.***

*-Nonindigenous Woman Entrepreneur*

***Having analyzed the situation, I consider that women are less trusted. I noticed something because they asked for my civil status, if I was married or in a partnership. And if such, they would ask for my husband's identification.***

*-Nonindigenous Woman Entrepreneur*

***I think that in this environment men tend to be taken more seriously than women. I think that if a man would have been in my situation, he would have been given more consideration.***

*-Nonindigenous Woman Entrepreneur*

***Unfortunately, we still live in a world where machismo is present in daily situations. As such, I believe that I was treated better. At Large Bank there was a woman who was applying for a loan at the same time as me. She had to wait for a long time, not like me. The loan director served me immediately, which was preferential treatment.***

*-Nonindigenous man Entrepreneur*



While social statuses intersect to create individual standpoints and experiences, individuals may attribute differential treatment to one status over another. For example, one indigenous female loan applicant perceived her differential treatment as gender discrimination and not based on her indigenous status. This finding indicates a clear opportunity for banks to address discrimination head-on with better marketing and outreach.

**Indigenous entrepreneurs were more likely to report discrimination.**

Indigenous business owners were four times more likely to report differential treatment than nonindigenous business owners (80% vs. 20%). While 80% of indigenous participants commented that their ethnicity affected the way they were treated by bank personnel, only 50% of all participants reporting that gender resulted in differential treatment. Assuming such perceptions are widespread among Guatemala's indigenous people, this could certainly dissuade some potential indigenous borrowers from applying for loans.

***I think that there is some difference between being indigenous or not.  
I think that nonindigenous peoples are treated better.***  
–Indigenous Woman Entrepreneur

**Indigenous entrepreneurs were less likely to report courteous greetings.**

Almost 90% of nonindigenous business owners reported being received promptly and courteously at the bank, compared to less than three quarters of indigenous business owners. By gender, 97% of nonindigenous women business owners reported courteous greetings. Interestingly, nonindigenous women business owners reported waiting significantly longer than other groups before being greeted by bank staff. Indigenous women business owners actually reported the lowest wait times compared to all other groups (7.8 minutes vs. 11.61 minutes).

Sometimes the perceptions shared by the study participants were unexpected and touched on factors potentially related to ethnicity. While one male indigenous loan applicant stated that indigenous people actually have an advantage and that there may actually be a trend toward positive discrimination of indigenous people, a nonindigenous loan applicant noted “that loan officers are only interested in people’s incomes and lifestyles, not so much in their race.”

***But yes, now that we are talking about indigenous peoples’ rights, I’d say that they are generally better treated. I consider that institutions have now put in place positive discrimination.***  
–Indigenous Man Entrepreneur

Several male applicants expressed similar perceptions, with the exception of one participant who observed that women and indigenous seemed to be better treated than nonindigenous males.



***Back then it didn't occur to me. But you should have seen the way they were treating women. It's much different how they treat them. The treatment is better.***

*–Indigenous Man Entrepreneur*

***No, I don't. I spoke to some people about this and there doesn't seem to be any difference. I think that the main difference is between consumer credit and loans for SMEs.***

*–Nonindigenous Man Entrepreneur*

**Ethnic bias may be less salient in majority indigenous regions.**

One loan applicant suggested that the likelihood of discrimination varies by region and the type of population using bank services—e.g., the participant said status discrimination is less likely in regions and banks where indigenous applicants are more common. In these cases, socioeconomic status and class issues might be more important than ethnicity.

**Perception matters. An important takeaway for banks is that despite finding little evidence in our study of the direct influence of hidden gender or ethnic bias on credit access, there was a widespread expectation of gender and ethnic bias, which suggests that banks need to better communicate their willingness and interest to lend to specific populations.**

While the perceived importance of gender and indigenous status varied quite dramatically among loan applicants, so did the justifications and understandings about why this differential treatment occurs.

***Here in Quetzaltenango, the treatment is pretty much the same because the majority of the people are indigenous. But if we were in a different region, I think there would have been a difference, above all in regions such as Zacapa. I got to know many regions of the country and have witnessed discrimination.***

*–Nonindigenous Man Entrepreneur*

***I come from a community here in San Marcos that is located 15 minutes away...I did have to wait, however, even though I came with a baby. Also, when there was an older client, they served him first. I think that they care more about the amount of money you are applying for than your origin. I would suggest that the bank increase its staff so that they can provide adequate customer service for applicants seeking high- or low-value loans, or for indigenous and nonindigenous.***

*–Nonindigenous Woman Entrepreneur*

# Few Applicants Were Offered Loans and Fewer with Terms They Wanted

Generally speaking, none of the small enterprises taking part in this study benefit from current market conditions. Only about one third of the participants received loan offers, with a mean award of approximately Q \$12,000 (approximately USD \$1,611). Those receiving loans were still charged very high interest rates, averaging 34% for 18-month terms. As applicants tended to receive offers with high-interest revolving credit lines, most of the business owners from this study opted not to take loans at all. For them, the safer road is to reinvest retained earnings and to rely on personal savings and loans from family and friends for business needs.

*There are banks that say they support SMEs,  
but in reality their interest rates are extremely high.  
—Nonindigenous Woman Entrepreneur*

**Banks are not well placed to serve small businesses. While small business owners represent an important pipeline of future business, few banks surveyed have the systems in place to support new small businesses.** As previously mentioned, the unfavorable credit terms extended to participants in our study set up new businesses to fail. While several loan applicants described banks initially expressing interest in their SMEs, their interest faded when applicants requested large loan amounts and/or lacked certain credit eligibility factors, such as steady income and collateral. A few loan applicants also mentioned the burdensome paperwork and documentation required by the banks, which is often hard for small business owners to provide. One business owner described how banks—despite being ostensibly interested in serving small businesses—rarely ask to see applicants’ business plans, instead basing loan decisions almost exclusively on credit eligibility factors.

## Variation in Lending Practices between Banks

**Banks need to improve the customer service experience for small business owners and the mystery shopping tool can help in this regard. Certain banks had higher levels of satisfaction across the board.** The stark differences between banks indicate that some banks will have a greater advantage in expanding their small business portfolio than their competitors. Women value personal relationships and customer service very highly and are more loyal than men to individual service providers, such as their customer relations manager at a financial institution. For example, research from Westpac Australia finds that women who are satisfied with their banking experience tell nine other people about their bank. <sup>71</sup>

Participating banks are listed in Figure 6; all names are pseudonyms.

Figure 6: Descriptions of Banks Included in the Study

Bank Name	Summary Description
<b>Large Bank</b>	One of the three largest banks in the country; is developing an SME strategy.
<b>Large Bank 2</b>	One of the three largest banks in Guatemala.
<b>Enterprise Bank</b>	One of the three largest banks in the country; has been implementing an SME strategy for several years.
<b>MFI Foundation</b>	An MFI foundation that focuses on group microcredit and has developed an individual credit model to serve SMEs.
<b>NGO Finance</b>	An NGO with multiple entrepreneurial development, agricultural, social, and environmental programs, as well as select microcredit services available to individuals and SMEs.

The Mystery Shopping exercise revealed several findings related to customer satisfaction that could be of interest to banks:

Generally speaking, **men and women held similar perceptions of their experiences at specific banks. Large Bank stands out as having the best customer satisfaction**, with wait times for greetings almost three times faster than the worst performing bank. A third (33%) of the loans awarded were from Large Bank, which may help explain why 39% of men and women participants gave Large Bank a positive score. Almost four times as many participants recommended Large Bank loan officers as they did those of the worst performing banks (MFI Foundation and Enterprise Bank).

**Enterprise Bank received the worst customer satisfaction rating of the five banks.** Overall, Enterprise Bank received the most negative reviews (39% of men and women participants).

**In most banks, participants reported being greeted courteously.** Yet, the three best performing banks did three times better than the worst performers.

***I was treated well at Large Bank because I think that they want to promote SMEs. But when they saw my credit card, they backed out.***  
*–Indigenous Woman Entrepreneur*

***MFI Foundation and NGO Finance do not support SMEs either. They ask for a big mortgage and many certifications. They did not ask me for any business plan and were not willing to accommodate small entrepreneurs.***  
*–Indigenous Man Entrepreneur*

# Financial Education Has the Potential to Level the Playing Field

**The study highlighted need for more financial education, including knowledge of credit approval processes.** Increasing financial education is an important and effective way of overcoming the structural barriers disproportionately impacting women and indigenous people. Several study participants reported learning how bank credit works for the first time. Many first-time loan applicants were surprised, not only by the terms of the loans offered, but also by the amount of documentation and collateral required to secure those loans. Many study participants also reported a preference for avoiding bank credit given the high interest rates (30% to 60%) and described the challenges of securing loans with business or personal equity and/or sellable assets.

*We do not have any financial education. I am telling you that it was very educational because we do not usually deal with credit systems, interest rates, fixed terms, and all of that. I learned.*

*–Indigenous Woman Entrepreneur*

*It was a good experience. It was my first time asking for a loan. I found out that I don't qualify for one because I do not have a sufficient credit history and cash flow. I also realized that banks do not support you as a small entrepreneur. They are not interested in my project. No bank made me an offer, and if I want to request a loan again in the future, I will have to increase my transaction flow.*

*–Nonindigenous Woman Entrepreneur*



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# Recommendations

## What Can Financial Institutions Do?

**1. Rule out hidden bias: Financial institutions do not necessarily have the power to change structural barriers for women-led businesses, but they can use self-testing in order to assess potential bias and to better understand male and female satisfaction levels for both women and men.** These studies can range

from simple exercises at the branch level to national-level exercises. They could also include matched female and male peers (as well as different ethnicities where relevant) to determine biases and differences in perceptions between men and women. The study in Guatemala identified Large Bank as a leader in customer service for women- and men-led SMEs. This likely gives Large Bank an advantage over other banks in serving the women's market since research shows that women are four times more likely than men to tell others about negative service experiences.<sup>72</sup> Rooting out hidden bias is complicated. While structural barriers are often quite obvious and easily defined (e.g., women are represented among newer and smaller businesses, and thus have less access to credit than those led by men), hidden bias is harder to detect; to identify hidden bias, we recommend using the matched control design on a larger sample of 20 to 30 matched pairs. For this study, matched pairs were based on gender and monitored, but did not control for indigenous status, which may explain some of the notable findings about indigenous status differences. In addition to increasing the sample size, future studies should consider applying matching criteria to groups of four by gender and indigenous status. Additionally, an important lesson learned is that before conducting matched-control mystery shopping studies in developing countries, baseline trainings should be offered to ensure that participants have similar knowledge of bank-lending practices and processes, and to control for factors such as the number of times that participants have applied for credit.

**2. Use self-tests and mystery shopping exercises to identify sex-disaggregated customer satisfaction levels.** In particular, the bank-self assessment tool can help financial institutions develop differentiated strategies for women-led small enterprises and women's markets. If there is the perception of bias, as was the case here, banks have an opportunity to improve their processes with respect to marketing and customer service to ensure that clients of all demographic profiles feel welcome and attended to.

**3. Reduce hidden bias risk.** Financial institutions should invest in reducing the risk of hidden bias in bank operations and credit approval processes. Steps to do so can range from providing unconscious bias trainings for loan officers and client-facing staff to developing alternative credit risk assessment tools (e.g., psychometric credit approval process) that provide a more specific view of the client's ability to pay back loans. When combined with training for loan officers, alternative credit risk assessment tools can break down cultural and gender stereotypes within the institution about men's and women's ability to pay back loans or be successful entrepreneurs.

**4. Take steps to help women-led businesses overcome structural barriers to growth.** Financial institutions should invest in programs that help women overcome the structural barriers limiting their growth potential and ability to become better and bigger clients. Encouragingly, financial institutions around LAC and the world are increasingly developing "Gender Intelligence" trainings for their management and staff that explain the importance of marketing their financial services to women.

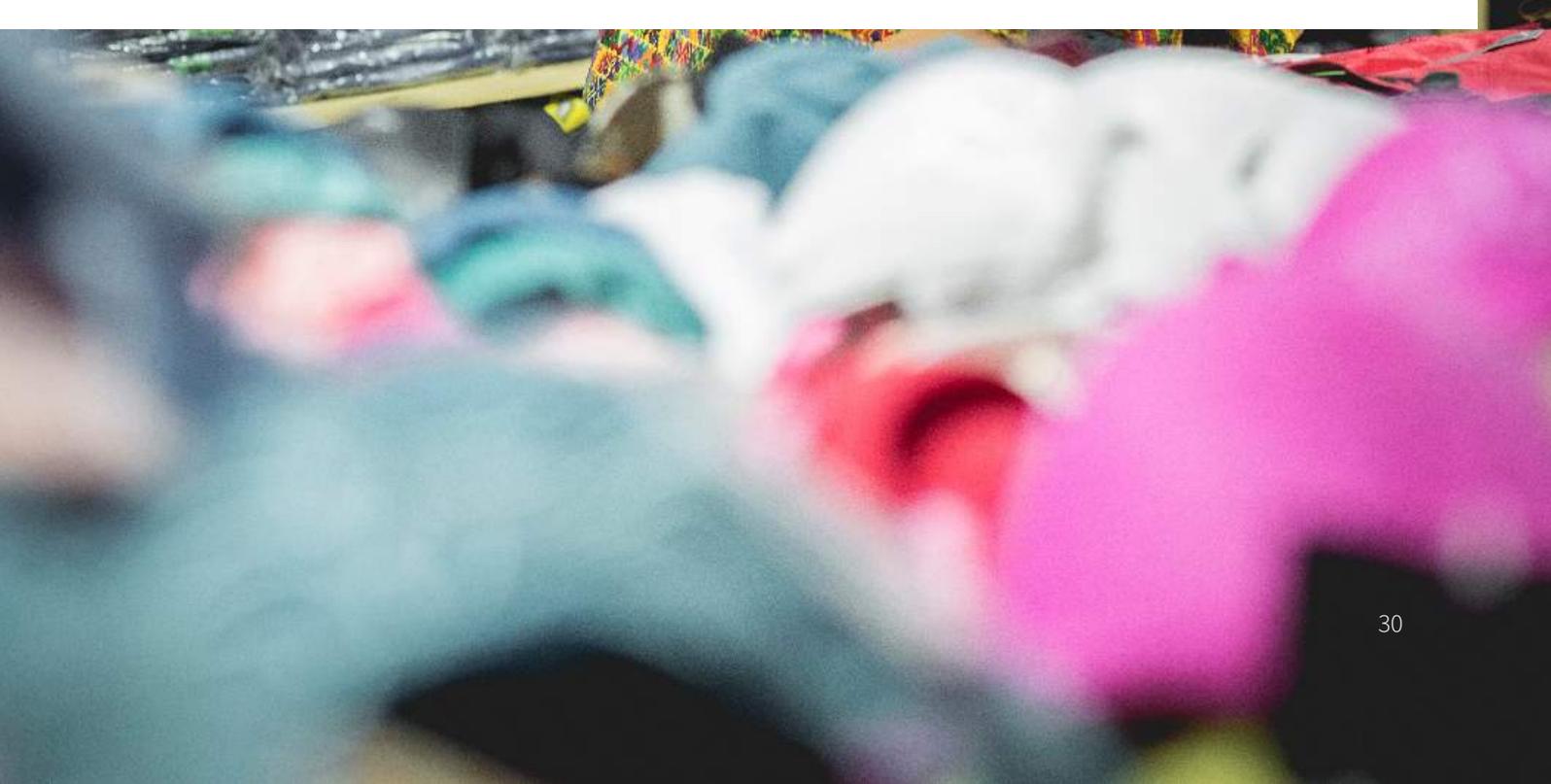


#### **5. What is not measured is not managed, so collect, analyze, and monitor sex-disaggregated data.**

Efforts to improve SME portfolio quality and growth can also benefit from gender data, which can be used as a management tool for identifying the differentiated needs of women and men clients. Sex-disaggregated management reports can also help pinpoint biases within the institution, as many banks linked to the GBA have seen. GBA data of over 22,000 clients in 23 countries has shown that servicing men-led small businesses is twice as expensive as servicing women-led small businesses.<sup>73</sup> This data has convinced bank managers in over 40 banks worldwide to develop women’s market and women-led SME programs.

## What Can Policymakers Do?

**Policymakers should encourage self-assessments and mystery shopper methodologies to evaluate and root out bias in financial institutions.** In more than a fourth of countries around the world (27%) it is illegal to discriminate in credit decisions on the basis of gender;<sup>74</sup> however, no methods are currently employed to ensure that banks are in compliance with this requirement in emerging economies. To begin with, the US FDIC’s guide offering suggestions for how institutions can compare their treatment of loan applicants through self-assessment is an excellent resource. The mystery shopper matched-control design is an important and novel framework for banks and other financial institutions to examine their own funding applicant data for evidence of hidden bias and possible structural factors that lead to different outcomes in access to business credit. This methodology has the potential to ensure that banks address the institutional processes leading to conscious and unconscious bias. National-level initiatives that develop larger samples will also yield more specific findings related to bias in the bank-lending system.



# Annex I: Guidance for Implementing Bias Self-Assessments



This annex includes a description of the mystery shopper matched-control study design used for the Guatemala pilot study. This novel methodology can be used by financial institutions for self-assessment and by policy-makers for cross-institutional studies of differential access to business credit. The annex provides guidance on two fronts: **1)** it outlines in detail the research methodology used for the Guatemala pilot study; **2)** it provides suggestions for improvements in future use of this methodology as well as a summary of the FDIC’s “Side by Side: A Guide to Fair Lending,”<sup>75</sup> which offers guidance on institutional self-assessments consistent with the Oxfam methodology. The self-assessment exercises provide a model for the type of self-assessment that organizations can use to identify hidden bias in lending processes.



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# Guatemala Pilot Methodology

The Guatemala pilot study developed a novel “mystery shopper” matched-control methodology in order to capture the perceptions and experiences of loan applicants as they apply for micro and small enterprise (MSE) loans, from their initial visit through the loan decision. The study recruited 12 matched pairs of male and female business owners, half indigenous and half nonindigenous, from two different municipalities in Guatemala. Matching criteria for each male-female pair included business size, annual sales, number of employees, industry, product and service categories, participant age, and basic training on the loan application process. Each participant was assigned five bank locations for in-person visits and loan application submissions. Participants were paid a small stipend to cover time and travel related to the study. Each participant completed a screening questionnaire, a questionnaire to assess each bank visit, and submitted a final loan decision report and video interview at the end of the study. Questions included a combination of closed and open-ended questions to measure perceptions and to capture first-person narratives. Video interviews provided both first-person narratives and an additional control for personal presentation factors.

Data analysis included descriptive statistics, independent two-sided means testing, and cross tabulations with Pearson Chi-square Independence Tests for the determination of individual differences (n=22) and differences across loan applications (n=132). Group analyses compared women against men, indigenous against nonindigenous, and four-group comparison of the intersection of gender and indigenous status. Additional data was coded from open-ended questions and video narratives to better understand loan requirements, and the perceptions and salience of status factors observed or experienced through the loan application process, including any reports of discrimination, evidence of differences in application requirements, and requests for additional information.

Our final sample included 22 participants as one indigenous, male participant was unable to complete the assigned bank visits, resulting in the omission of one matched pair. As expected, the matched pair sample design resulted in very few significant differences in individual or business characteristics. Two exceptions included individual age and business age by indigenous status. Participants ranged in age from 23 to 53 years old (yo) with a mean age of 39.6 years. As designed, there were no significant differences in age between male and female participants; however, indigenous participants (41 yo) were slightly older on average than nonindigenous participants (38 yo). The small businesses in the sample ranged in age from 2 to 30 yo with an overall mean age of 9.4 years. Indigenous participants tended to have older businesses with a mean age of 11.6 years, compared to seven years for the businesses owned by nonindigenous participants. This difference is explained by the oldest business (30 yo) being owned by an indigenous participant. There were no significant differences in business size across groups, with a mean of four employees and about 75% of the businesses reporting annual sales of less than Q \$20,000 (USD \$2,684). More than half of the businesses were service firms, while about a quarter were manufacturing and utility companies.

# Methodological Limitations and Challenges

Initially, the study intended to focus on informal microbusinesses—informal, microenterprises outside of a university incubator type of setting. The field team hired to recruit and train participants and to collect the data at multiple time points worked through local municipalities to recruit male and female business owners; however, the resulting sample ended up being all formal, registered businesses, almost all established, with a few microenterprises included. This is not a completely unexpected finding, but a deviation from the original intent of the study. Most research on the “last mile” microenterprises is generally done through household surveys and ethnographic type field work for a reason. Also, these types of microenterprises are rarely eligible for bank credit as the business owners are too often unbanked and do not hold valuable assets suitable to serve as collateral for bank loans.

Locations from six different banks in Guatemala were included in the study. Given that the study only looked at one specific bank branch per bank, the study findings are not nationally representative by bank (that would require a far larger sample size).

The small sample size ( $n=22$ ) resulted in low statistical power for analysis of individual characteristics. A better design would involve a much larger sample of 20 to 30 matched male-female pairs. Matched pairs were based on gender, not indigenous status, which may explain some of the significant findings of indigenous status differences. Future studies may consider applying matching criteria to groups of four by gender and indigenous. Missing controls relevant to loan application outcomes included measures of education, work experience, business profitability, and personal credit history.

Qualitative tools, particularly video interviews, were a very effective way of eliciting rich narrative data and adding context to the quantitative findings. When replicating this methodology, it is suggested that qualitative tools be employed, particularly video interviews for capturing the mood and nuances of participant responses.



COOPSAMA/Oxfam

# Considerations for Future Use

Below are a series of recommendations for implementing the mystery shopping tools in future studies.

## **Sample size:**

Sample size should be increased to ensure adequate degrees of freedom and minimum cell numbers for adequately powered statistical analysis. A sample design of 20-30 matched pairs (total of 40-60 participants) is recommended for a study of gender and ethnic status. Consultation with a well-trained statistician is advised to ensure optimal sample design.

## **Video Interviews:**

Use video interviews after each visit to capture perceptions when they are fresh in the mind of participants; if recourses are constrained, then video interviews can also help capture participant perceptions about their visits to different banks.

**Matching criteria for the business** to be applied in the screening questionnaire:

- Age
- Size (both employees and annual sales)
- Profitability
- Industry and product or service category
- Credit history (including loan approvals and denials, amounts and terms awarded, and number of times)

**Marching criteria for entrepreneurs to be considered:**

- Age
- Sex
- Education
- Credit history
- Ethnicity (depending on context)

# Testing Tools

**Paired tests:** A paired or matched test consists of sending two individuals (or two couples) separately to an institution to collect detailed information about its lending practices. The testers pose as potential applicants for the same type of loan.

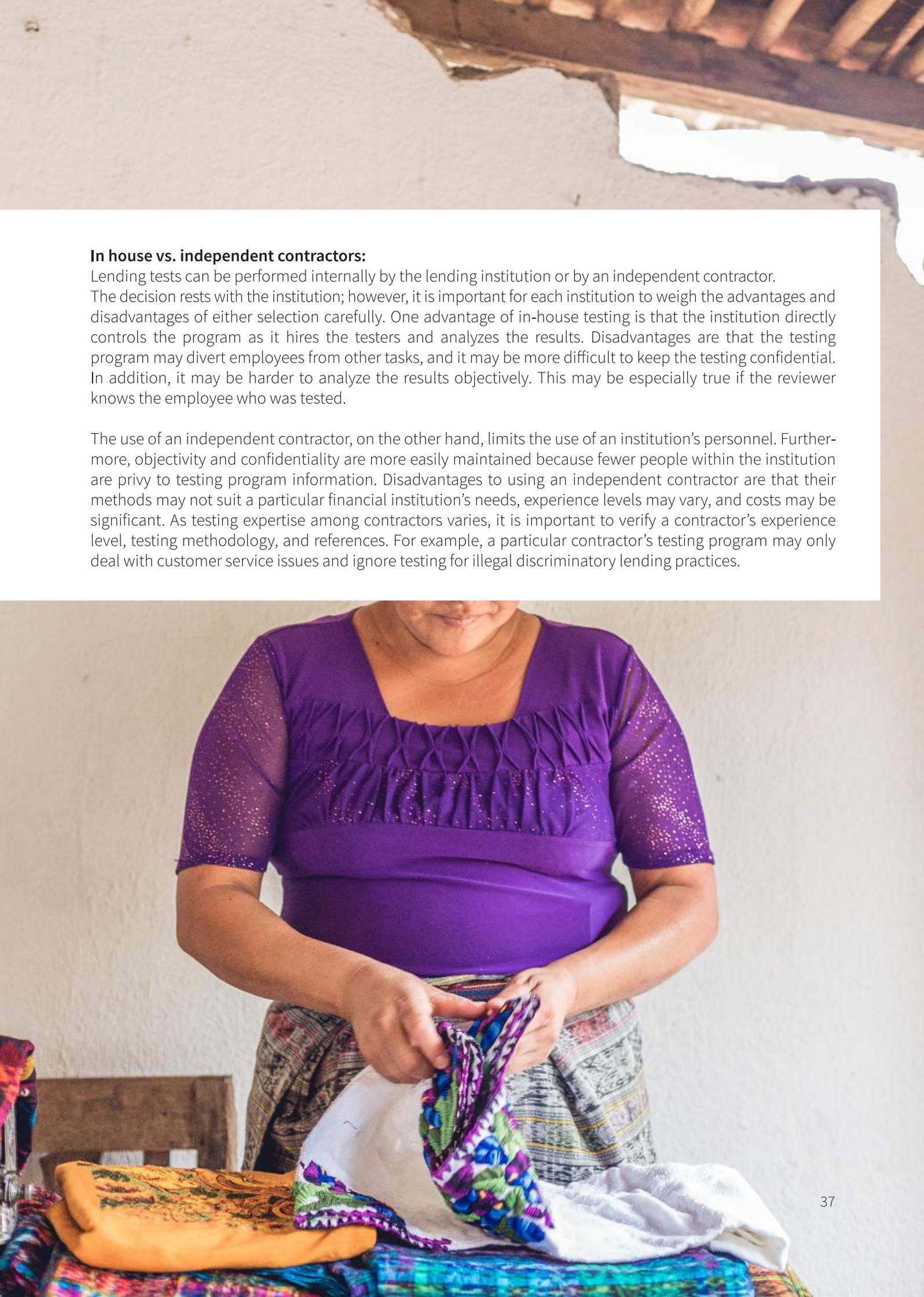
Example: To test for discrimination based on race, a white tester and a black tester separately visit a lending institution to ask about applying for the same type of loan. They would be provided with similar background information such as family size and employment. The black tester would generally have a slightly higher income and less debt in order to appear better qualified than his or her white counterpart. Otherwise, the individuals selected as testers should be similar in all significant respects except for the variable being tested (e.g., race, gender, familial status, etc.). Their experiences would then be compared to determine if the individual in the protected class may have been the victim of discrimination. Importantly, in paired tests, the testers usually do not have knowledge of each other or the purpose of the test. Conducting the test in this manner helps ensure the validity of the test by minimizing the potential for bias in recording experiences.

**Multilayered testing or “sandwich” testing uses three testers, only one of whom is a protected class member. As with paired testing, the testers should be similar except for the variable being tested.**

Example: In testing for discrimination based on sex, the first tester would be male, the second tester female, and the third tester male. Marital status would be the same for all three, and the female tester’s qualifications would be slightly better than those of the male testers. This test structure limits nongender variables leaving gender as the most likely basis for potential differences in treatment. In sandwich testing, as in paired testing, the testers separately ask about similar financing requirements.

**Complaint testing, unlike the sandwich or paired scenarios, uses a single tester to evaluate the experience of an actual loan applicant who believes that an illegal discriminatory event has occurred. The tester assumes characteristics similar to the complainant’s and attempts to obtain information about the same loan product.**

Example: The complainant is Hispanic and believes that his loan application was denied based on his national origin. A white tester would be assigned slightly worse financial and employment qualifications than those of the complainant. The complainant’s experiences at the institution would be compared to the white tester’s experiences to determine if there were any differences in treatment. If the tester is offered a loan or receives better treatment and more information, then the complainant may have been discriminated against on the basis of national origin. In all three types of testing, paired, multilayered, and complaint, the testers prepare an objective, factual written account of their experiences on a standardized report form.



**In house vs. independent contractors:**

Lending tests can be performed internally by the lending institution or by an independent contractor. The decision rests with the institution; however, it is important for each institution to weigh the advantages and disadvantages of either selection carefully. One advantage of in-house testing is that the institution directly controls the program as it hires the testers and analyzes the results. Disadvantages are that the testing program may divert employees from other tasks, and it may be more difficult to keep the testing confidential. In addition, it may be harder to analyze the results objectively. This may be especially true if the reviewer knows the employee who was tested.

The use of an independent contractor, on the other hand, limits the use of an institution's personnel. Furthermore, objectivity and confidentiality are more easily maintained because fewer people within the institution are privy to testing program information. Disadvantages to using an independent contractor are that their methods may not suit a particular financial institution's needs, experience levels may vary, and costs may be significant. As testing expertise among contractors varies, it is important to verify a contractor's experience level, testing methodology, and references. For example, a particular contractor's testing program may only deal with customer service issues and ignore testing for illegal discriminatory lending practices.

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