LATINO-OWNED BUSINESSES: INVESTMENT AND CREDIT USAGE IN COMPARISON TO OTHER RACIAL/ETHNIC GROUPS

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Why is this topic important?  
Demographic Projections

- Latinos will triple their population numbers by 2050, and double their share (16%) of the overall population—comprising @ 30% of the population; or one in three members of population.

- By 2050, Latino youth are projected to outnumber White youth at @ 43.8 million

- 2010 is the tipping year for the minority shift in population, with more babies born among minority groups than among the White population (aging population)

- By mid-century there will **not** be a numeric majority group—intergroup relations, however, are likely to continue to remain problematic (if not worsen due to White Americans becoming increasingly threatened)
Shift includes the aging out of the Baby Boomers (78.2 million) over next two decades

- Will increase dependency of seniors on adult workers
- Will leave a major void in the labor force and the economy -- just in sheer numbers

Latinos, both foreign and native-born, remain outside the core fabric of the nation’s institutions (education, economy, etc.)

Future of the nation is dependent on the wellbeing of Latinos
As expected from the demographic shift, Latino business ownership increased nationally between 2002 and 2007—According to the U.S. Census Latino-owned businesses increased by 43.7% to 2.3 million during that 5-yr period.

- This is more than twice the national business growth rate of 18.0%.
- Still only comprise 8.3% of U.S. business firms

Census data show that Latino-owned businesses generated $345.2 billion in sales in 2007, up 55% from 2002.

- This is approximately 1/3 of the $978 billion in buying power by Latino consumers (of the US consumer power of $10 trillion)

U.S. Census Bureaus, Survey of Business
The number of 44,206 Latino-owned businesses with receipts of $1 million in 2007 reflected an increase of 51.6% between 2002 and 2007.

Nation’s firms with receipts of $1 million are approximately 5.3%; among Latinos, they comprise approximately 2.0%
Barriers Facing Latino Entrepreneurs

- Despite the rapid growth, the literature shows that Latino business owners experience a mix of barriers, including:
  - Low levels of human and financial capital
    - Education and wealth
    - Language barriers (esp. among foreign born)
  - Limited business start-up information
  - Working class backgrounds or low levels of parental entrepreneurship
  - Limited access to credit
Limited Access to Credit

Several reasons are given for limited access to credit, including:

- **Age**: Latino business owners tend to be younger than their dominant-group counterparts.

- **Lack of assets**: Unlike dominant-group entrepreneurs, minority business owners often become entrepreneurs because they are excluded from mainstream labor markets. Therefore they are often poorer and have fewer assets to present as collateral.

- **Discrimination**: Research shows that subtle racial discrimination is still in existence in both the loan approval and interest rate decision-making processes. Latino and other minority businesses may be perceived as less likely to be successful and therefore greater credit risks.
Most businesses are funded with owner savings, loans from family members, and sometimes personal credit cards.

Latino business owners often lack formal business training or experience, limiting their ability for successful operation as compared to other businesses, particularly within certain industries.

Instead, Latino business owners rely on “trust” networks developed within local communities to compensate for lack of access to formal credit services and business savvy.

*Source: Contreras and Griffith (2009)*
Contributions of Latino-Owned Businesses

- Although businesses are owner-operated or managed, few depend solely on their families for staffing needs, consequently they are a source of employment for members of surrounding communities.
- Businesses are as likely to be owned/operated by women as men.
- Reliance on trust networks to overcome lack of access to formal credit services limits Latino business owners movement into industries that require greater up-front capital investments.

*Source: Griffith, Contreras, and Kissam (2009).*
The following slides review the funding sources utilized by Latino-owned businesses in the U.S.

Both investment sources and credit usage are included.

Latino-owned businesses are compared with other racial/ethnic groups.

Start-up funding as well as funding used over the first 5 years of operation are shown.

The analysis is based on data from the Kauffman Firm Survey, provided by the Kauffman Foundation.
The Kauffman Firm Survey

- The Kauffman Firm Survey (KFS) is a panel study of 4,928 businesses founded in 2004 and tracked over their early years of operation. The survey focuses on:
  - the nature of new business formation activity;
  - characteristics of the strategy, offerings, and employment patterns of new businesses;
  - the nature of the financial and organizational arrangements of these businesses; and
  - the characteristics of their founders.

Source: www.kauffman.org
## Baseline Data Descriptions of Firms* by Race/Ethnicity

<table>
<thead>
<tr>
<th>Race and Ethnicity</th>
<th>2004</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>White</td>
<td>78.5%</td>
<td>80.2%</td>
</tr>
<tr>
<td>Black</td>
<td>9.3%</td>
<td>8.5%</td>
</tr>
<tr>
<td>Asian</td>
<td>4.4%</td>
<td>4.6%</td>
</tr>
<tr>
<td>Other</td>
<td>2.3%</td>
<td>1.9%</td>
</tr>
<tr>
<td>Hispanic</td>
<td>5.5%</td>
<td>5.2%</td>
</tr>
</tbody>
</table>

**Other race category includes mixed race and American Indians**
Types of Investment Sources

- **Formal investments**: investments in the business by other companies, venture capitalists, and government agencies (quite a mix)
- **Informal investments**: investments in the business by friends, family, or spouses for a share in the business
- **Owner investments**: money any owner put forth for an ownership share in the business
Business Credit Sources at Start Up

- **Formal credit sources**: business or corporate credit cards issued in the name of the business, business loans from a commercial bank, a business line of credit from a bank or other financial institution, loans from government agencies or loans from other businesses.

- **Informal credit sources**: money borrowed from non-bank financial institutions, from family or friends of any of the owners, from employees who are not owners of the business, from another owner of the business or a partner, from any other individuals not associated with the management of the business, or any other unspecified informal sources in the name of the business.

- **Owner money**: personal money from owner(s) used to fund the business.
Types of Personal Credit Sources

- **Personal formal credit**: personal credit cards for business-related purposes, personal loans from a bank or other financial institution (such as mortgage or home equity loan used for the business) taken out on behalf of the business in an owner’s name, and business or corporate credit cards issued in the owner’s name.

- **Personal informal credit**: personal money borrowed from friends, family, spouses, other individuals not associated with the management of the business, or any other unspecified sources.

- **Owner money**: personal money from owner(s) used to fund the business.
Review of Credit Findings

- Latino-owned businesses used fewer formal investment sources than any other race/ethnic group except Blacks and used more informal investment sources than their own money to start up a business.
- Latino-owned businesses used fewer formal credit sources in the name of the business than any other race/ethnic group except Blacks and used more informal credit sources than any other group.
- Latino-owned businesses used more personal formal and informal credit sources than any other race/ethnic group.
KFS Data from 2004-2008
Includes investment sources, business credit sources, and personal credit sources used in 2004 analysis
Sources of Investments Over Time

- Formal Investments
- Informal Investments
- Business Formal Credit
- Business Informal Credit
- Personal Formal Credit
- Personal Informal Credit
Trend Findings

- Latino-owned businesses experienced more volatility in their use of formal investment sources than any other race/ethnic group.
- Latino-owned businesses used fewer formal credit sources as compared to Whites and Asian/Native Hawaiians until 2006, when there was an increase followed by a quick decline.
- Latino-owned businesses used the most business informal credit services than any other race/ethnic group at startup.
Overall Findings for Latino-Owned Businesses

- Used fewer formal credit services at start-up, only Blacks used less; improves over time
- Used more informal credit services than any other race/ethnic group at start-up; proves unstable over time
- Used more personal formal credit services than any other group except Asians/Native Hawaiians at start-up
- Used more personal informal credit services than any other race/ethnic group at start-up
Acquiring the Tools of the Trade and Capital Constraints

- Firms need capital to finance day-to-day operations: investments in equipment, inventory, and the like particularly important to long-term success
- Low-income minorities face multiple capital constraints: low personal wealth and limited access to credit or limited borrowing power
- Restricted access to capital strongly suggests that expanded loan access would help Latinos and other minority entrepreneurs
Microenterprise Lending Programs (MLPs): popular since the 1990s, but largely unsuccessful for several reasons

1. Low demand for loans
2. Low loan volume has exacerbated steep administrative costs
3. High default rates
4. Overall high costs relative to benefits
5. Doesn’t get at the root problems prohibiting Latinos and other disadvantaged groups from firm entry
Differentiation among industry groups in terms of financial and human-capital intensiveness

Capital constraint is not a significant barrier to entry into low-capital intensive industries, which are most often targeted for entry by subsidized loan program clients

Individuals possessing net worth of $150,000 or more are more likely to become small business owners in high-capital intensive firms

Thus, small loans (MLPs) to poor aspiring entrepreneurs is not likely to impact their entry into capital-intensive industries
Financial investments are crucial to success of any business venture.

Bankers are the primary source of debt financing; however, capital is more accessible to White entrepreneurs than Latinos or Blacks.

Overall, while MLPs may help some race/ethnic minorities enter into low-capital intensive industries, it is vital that they also access larger, formal bank loans to gain entrance into high-capital intensive industries.

Policy approaches should target specific markets and their unique challenges.

*Source: Bates et. al (2010)*
Beyond these Data

- Cultural alignments
  - Institutional incorporation
    - Require change among agencies and institutions
      - Full extent of change still unknown
  - Knowledge poverty among Latinos
    - Requires outreach and training
Beyond these Data Cont’d

- Build agency capacity to deliver services
  - Limited understanding of barriers facing Latino entrepreneurs
    - Need for systematic research in terms of source and nature of obstacles
  - Limited capacity of agencies to work with Latino entrepreneurs beyond stereotypes
    - Need for diversity building capacity among agencies and personnel
Interventions are needed to improve Latino access to business loans and credit, but they have to be accompanied by research to determine what works—body of knowledge is slowly emerging.

Few current data sources address these issues. Therefore, the collection of new data on Latino access to business loans and credit is needed, both from the business owners’ and lenders’ perspective.

In addition, more research is needed to investigate the concentration of Latino business owners in low-capital intensive industries and what can be done to improve their entrance into high-capital intensive industries.
Don’t let your agency be among those that doesn’t contribute to the national challenge of integrating Latinos.
Select References

   http://www.census.gov/econ/sbo/


Latino Entrepreneurship
Support? Hinder? Or Ignore?
Sources

- Francisco Hernandez: Graduate Report
- Himar Hernandez: Main Street Presentation
- Town/Craft: Roundtable Report
- New Iowan Centers
“New” Immigrants Becoming Established
• Ankeny, Ottumwa, Bloomfield, Columbus Junction, Ankeny, Des Moines, Perry, Clarion, Denison, Red Oak and Marshalltown
• Total of 14 Business owners

• Food Marts, Restaurants, Clothing stores, Construction Co.
• On-site interviews

• 1,536 firms (2002)
• 2,455 (2007)

• Mostly small family run businesses (1,173)
• <8 employees with <25K payroll/person
MANAGING Tough Times

Iowa is an English as Official Language State

• Latino entrepreneurs are not yet fully informed of and benefiting from programs available
• Comprehensive approach to a systemic problem

• Labor workforce potential
• Purchasing power
• State and local taxes
• Increase Iowa’s competitive edge

Iowa is an English as Official Language State
Over the past several decades rural communities in Iowa (as in many other states) have experienced economic decline and therefore loss of population.

Due to agricultural economic sectors that require “low skills” workers and communities in which costs are low, immigrant population grows.
Immigrant impact in rural communities

Iowa’s foreign-born population increased by over 34 percent between 2000 and 2006. During that period Iowa gained 31,000 immigrants, bringing the total number of foreign-born residents to over 122,000.
Why is there growth in the Midwest?

Iowa faces large rural immigration

Migration to rural places

Mexico; Farmers can’t compete with American corn

Iowa; corn prices NAFTA

Migration
• Latino culture relies on informal networks vs. formal

**FORMAL**
- Chambers
- Main Street
- Service clubs
- Main stream

**INFORMAL**
- Families
- Place of origin
- Friends
- Former co-workers
Leadership implications:
• You will not find leaders in the usual places
  • They usually are not asked to be involved in organizations
  • Their potential is often to recognized or considered
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Leadership

Before…
Leadership

After…
Why should preservation organizations be involved with the Hispanic community?

96% of the Latino businesses in Iowa are located in or surrounding historic districts.
Latino Businesses

- Retail 62%
- Restaurant 20%
- Car/Mechanics 5%
- Manufacturing 2%
- Communication 1%
- Finances/Insurance/Legal 2%
- Construction 5%
- Other 3%
Preservation Challenges:

• Lack of knowledge of historic background
• Lack of knowledge of incentives (money and community)
• Lack of communication
• Preservation organizations need to promote value for preserving and/or rehabilitation.
The use of space outside the businesses
What happened here?

A lesson learnt by Main Street and a Latino business owner
Formal Organizations

Few organizations in the state of Iowa

Des Moines area is most organized.

Organization is sparse in more rural areas.

Disconnect often between business outreach programs and Latino entrepreneurs and businesses.
• Organize Latino business groups to:
  - discuss business & comm. matters
  - source of financing (small loans)
  - mentoring

• Run a more effective outreach to:
  - develop good & trusting relationships
  - educate Latinos
  - promote unity among all ethnic groups
Some Last Thoughts

- Building the bridge… outreach and pilots are needed
- Recommendations for the National Trust & Historic Preservation and Main Street organizations…
  - Whose history?
  - Whose culture?
  - Whose business?
- Need to learn from best practices
- Need for business development outreach
- Need to connect to banking and financial communities
- Need to integrate with community design
Related article “hot off the press” this morning from The Des Moines Register…