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Financing SMEs in Canada: Barriers Faced by Women, Youth, Aboriginal and Minority Entrepreneurs in Accessing Capital Phase 2: Gap Analysis and Recommendations for Further Research



**Research Paper prepared for the Small Business Policy Branch
Industry Canada as part of the
Small and Medium-sized Enterprise (SME) Financing Data Initiative
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EXECUTIVE SUMMARY

The objective of this project was to evaluate the accessibility of financing of Canadian small and medium-sized enterprises (SMEs) for particular business-owner profiles. Emphasis was placed on evaluating whether women, youth, aboriginals, visible minorities and language groups (collectively referred to as Profile Groups) faced more barriers to accessing small business financing than the SME population in general. Phase 1 comprised a comprehensive review of the Canadian literature on SME financing for these groups, supplemented with U.S. and international literature where relevant. Phase 2 provides further analysis and evaluation of this literature, in order to respond to the three objectives outlined for this phase of the project:

- Identify any business owner characteristic-related barriers to financing that are evident on the basis of existing data;
- Identify data gaps that need to be filled in future data collection. A gap analysis model will be developed depicting any gaps in data available;
- Recommend data collection methodology to fill identified information gaps.

The findings of Phase 2 indicate that:

Based on information collected during Phase 1, the hypothesis of business owner characteristic-related barriers to financing cannot be validated on the basis of existing data;

Barriers to SME financing do exist, and vary significantly according to business type, age, stage and industry with owners facing different barriers accordingly. Data does not exist to demonstrate whether the Profile Groups face greater barriers than the general SME population when stratified according to the categories noted above;

Significant gaps exist in the current research data pertaining to business owner characteristic-related barriers to financing in particular, and to SME financing in general;

Additional research is needed to fill these gaps, and analysis of barriers faced by any business owner profile will be relevant only if there is sufficient baseline data on access to financing for SMEs in general for comparative purposes;

Future research in this area should ideally be national in scope, and should be designed to collect SME financing data that can be disaggregated according to a variety of criteria identified as relevant in Phase 1 of this project. This research should include data collection related to firm characteristics (e.g., age, stage, sector, industry, geographic location); related to type of financing sought (e.g., debt financing, equity financing); and related to business-owner profile characteristics (e.g., gender, ethnicity, age).

INTRODUCTION

The purpose of this project was to address whether certain business owner profiles (women, youth, Aboriginal, visible minorities and language groups) faced greater barriers in accessing financing for entrepreneurial ventures than the SME population in general. Phase 1 comprised a literature review of existing research and reports on this topic. Phase 2 identifies the barriers to financing noted in the literature on each of the Profile Groups, but also highlights the significant gaps which exist in this research. Based on this gap analysis, Phase 2 concludes with a framework for future research and data collection that would address these gaps, and provides insights into barriers faced by SMEs in accessing financing. This framework would be robust enough not only to address questions of barriers faced by the identified Profile Groups, but also to yield broader insights into barriers faced by other segments of the Canadian SME population.

The contents of this report can be divided into three broad sections. The first section provides background and contextual information, including a summary of findings from Phase 1 and Phase 2 research, an analysis of gaps in the existing research that are relevant to an examination of the impact of business-owner profiles on access to SME financing, and an overview of SME financing. The second section focuses specifically on the gaps identified in the research for particular business owner profiles: women, youth, Aboriginals, and visible minorities and language groups. This section also highlights any barriers noted in the literature that might affect access to SME financing. The final section proposes a framework for research that will help to fill the gaps noted above, and to provide adequate data to identify the barriers that particular Profile Groups may face in accessing SME funding in Canada.

Summary of Findings

Examination of existing, available data indicates that while each of the Profile Groups may face particular barriers to financing, there are also significant barriers to financing encountered by various profiles of SMEs in general. For example, SME size, industry sector, geographic location, and stage of business development all have significant effects on financing available to individual SMEs. As such, while the focus of this project remains on evaluating financing barriers faced by various Profile Groups, for analytical purposes it is useful to contextualize these findings by situating them within the broader context of SME financing.

The literature reviewed during Phase 1 indicates that the specific barriers faced by each Profile Group are more dependent on factors such as the overall risk associated with the venture, stage of the venture, type of financing, and industry, than on business owner characteristics - such factors as gender, age or minority status. This is particularly true for businesses that are in the later stages of development.

More mature businesses are generally perceived as a lower risk for financing, and thus financing arrangements can be made on the strength of the existing business rather than owner characteristics. For earlier stage financing, where the business is less mature and the risks higher, the investment is being made as much in the owner/founder as the business proposition itself. The implication of this is that there are significant barriers to accessing financing for early stage SMEs, but the existing data does not support a direct correlation between barriers to SME financing and the particular Profile Groups .

However, there may be indirect linkages that affect the Profile Groups more than the general SME population (although it should be stressed that there is not enough empirical data to clearly support this conclusion). For example, all of the profile groups reviewed were primarily starting new or microbusinesses in traditional, low growth industries (e.g., service and retail). As the low growth rates and higher risks associated with these industries make them less appealing to potential financiers, it may appear as though the Profile Groups are facing barriers that others are not, but the financing data summarised for each group based on owner characteristics may mask other factors affecting access to financing for SMEs in general. It is possible that the Profile Groups may be affected by this, but there is no clear evidence that ‘underfinancing’ is related to their personal characteristics, rather than the overall nature of financing for less established SMEs.

The data suggests that SMEs competing in non-traditional and high growth industries face similar barriers to any other company in that sector, small and young companies face similar barriers regardless of ownership characteristics; and access to equity financing is very difficult if the SME owner lacks established networks. It is worth noting again the possible existence of indirect barriers (e.g., there may be many reasons it is more difficult for members of Profile Groups to become part of the established funding networks) but the existing data on SME financing is not comprehensive enough to draw definitive conclusions about this.

Gap Analysis

It is important to distinguish between two different types of gaps identified in the research data: gaps in the research literature; and gaps in availability or accessibility of financing for the Profile Groups. Both of these distinct types of gaps are discussed in this section.

There are few national level Canadian studies that evaluate the range of SME types and also provide data that can be disaggregated according to any of the Profile Groups .

There is ample evidence that business owners face different barriers depending on the industry, business type, age, stage, and type of financing required. As such, it is critical to have reliable baseline data on the barriers faced by SMEs as a whole that can be disaggregated according to these categories, in order to provide a relevant comparison point for examining whether certain business owner profiles face greater barriers because of their gender, age, or ethnicity. The existing baseline data for SMEs as a group is inadequate to provide a starting point for this.

The various studies that were reviewed for Phase 1 and 2 of this project were published over a 7 year period, and may be drawing on data that is considerably older than this. In addition, each has its own focus, reference group, and objectives, and as such, each study employs specific research methodologies targeted to its objective(s). As well, some of the studies have a regional or provincial focus rather than national. The majority of the studies reviewed for this project focused on the SME sector as a whole, and were not designed in a way that would allow for disaggregation of data to examine barriers to financing by type of industry, stages or maturity of business. These factors make it difficult to draw accurate, broadly-based conclusions regarding barriers to SME financing from the cross-section of Canadian literature available.

As many of the referenced studies dealt with barriers to financing for only one of the business-owner profile groups (with women being the predominant focus of research) it is difficult to draw broad conclusions about the

accessibility of financing by comparing the existing research across the Profile Groups. It is even difficult to do intra-group comparisons based on existing research, as the methodologies, scope of research, sample size and research focus varied significantly from study to study.

From a research perspective, much of the published literature on barriers to SME financing lacks rigour. For example, of the 37 studies found pertaining to SME financing barriers, only 6 both utilized a control group and used Canadian data. Of these, all focused on women, so there is no comparable existing published data focusing on barriers faced by other Profile Groups. Only a handful of the articles used in this study were published in peer-reviewed journals; the majority were reports conducted by or for particular types of organizations (e.g., banks, small business organizations, groups representing particular interests). In a few cases, one data set has been used to produce two or more research papers in this area (e.g., BDC, 1997 and BDC, 1998; Caldwell and Hunt, 1998; Aboriginal Business Canada, 2001). This is of particular concern for drawing conclusions regarding financing when so few papers have been published on topics such as barriers to SME financing for aboriginals.

Finally, any research of this type is limited in its access to those businesses which were not able to access any funding and were therefore unable to move even to the start-up stage. This is a real loss when trying to evaluate barriers to financing and whether particular groups face greater barriers than others. Methodologically, however, it would be very difficult to identify this group for survey purposes, as financial institutions and other funding sources are unlikely to release information regarding unsuccessful candidates, and those who are unable to start SMEs would be difficult to find without very large scale sampling.

Trends Worth Noting

As noted in Phase 1 of this report, all business ventures require capital in order to initiate, maintain and/or expand operations. Capital may be acquired via debt or equity financing and may take the form of any number of financial instruments.

Debt instruments used by SMEs may include bank term or demand loans, private loans, operating lines of credit, credit cards, leases, supplier credit contracts, and government-backed loan programs. Equity investments in SMEs are typically reflected through ownership of one or more classes of shares in the venture. These investments may include personal investment by the entrepreneur, private investment by friends and family (love money), angel investments, venture capital investment and in cases of publicly traded companies, public market equity. In the case of established companies, retained earnings may also be re-invested in the venture.

A survey by Thompson, Lightstone and Company (1998) noted that half of all SMEs in Canada use debt financing from financial institutions to finance their business, which means that half are using other financing alternatives, likely some form of equity financing. Typically, debt financing places more emphasis on business experience, financial credit rating and the track record (if applicable) of existing businesses. In comparison, equity financing may place more emphasis on the personal characteristics of the business owner.

Different types of equity financing come with varying rates of accessibility. For example, access to personal investment and love money is largely dependent on the personal characteristics of the entrepreneur and the economic strata the entrepreneur occupies. Angel investors tend to invest in businesses working ‘close to home’ and in the sector these individuals made their money in; as such there may be broad disparities in the availability of ‘angel investments’ depending on geographic location and sectoral focus. Venture capitalists typically invest in initiatives perceived to have ‘high growth’ potential (e.g., information technology, biotechnology); therefore entrepreneurs not starting businesses in these knowledge-intensive areas are not likely to be able to access venture capital equity financing.

In general, it is harder to access funding for earlier stages of SME development (e.g., seed money, start-up capital) than for later stages (e.g., working capital or expansion funds). As the CFIB (2001) notes, SMEs in existence less than 10 years have a much higher likelihood of being underfunded than those in existence 10+ years.

Entrepreneurial ventures in low-growth sectors (e.g., service and retail) typically have fewer financing options available than those in high growth sectors (high technology, life sciences). As low-growth industries tend to have lower profit margins, there are also fewer dollars available for reinvestment in these businesses. Thompson, Lightstone and Company (1998) note that retained earnings are a common form of equity financing for SMEs with 51% employing this strategy. Lack of retained earnings to reinvest may have a significant impact on rates of business growth, and limit future growth opportunities.

Other factors which affect the accessibility of financing for SMEs include business size (with micro-businesses typically having less access to financing than larger SMEs) and geographic location. Urban entrepreneurs are likely to have a larger pool of financing options to draw on than rural entrepreneurs, particularly those dwelling

in communities without easy access to financial institutions. Similarly, SME financing options are affected by proximity to the ‘central areas’ for particular industries, particularly in cases where angel investors or venture capital is sought. In these cases it is critical for an entrepreneur to be geographically located in ways that provide access to the networks of investors providing financing in various sectors. For example, the high technology networks in Canada tend to be clustered around the Ottawa area, and thus the financing options for high-tech start ups will be more prevalent there than in other regions of Canada.

Research on Financing for SMEs

In terms of research on the SME sector as the whole, the following table summarizes some of the key aspects of studies examined which looked at financing issues for the SME sector. (The numbers in the left hand column identify where full copies of each article can be found in the binders which accompany this project). A more complete summary of research findings is presented in Appendix A of this report. It should be noted that there may be more research in this area than is represented here. Because the focus of this project was on particular Profile Groups, emphasis was placed on identifying studies that dealt with one or more of these profile groups rather than the SME sector as a whole.

	Reference	Methodology	Type of Financing	Sector	Stage
9	CBA, 2001.	Interviews	All	All	All
11	CFIB, 2001.	Membership survey	All	All	All
17	Groupe Secor, 2000.	Survey	Debt	All	All
21	Industry Canada, 1998..	Review of program	Debt	All	All
32	Statistics Canada, 1994.	Stats Canada data	All	All	All

While this research provides an overview of issues related to SME financing over the last decade, there are also some significant gaps which make these findings difficult to use as a comparison point for examining barriers to financing faced by particular Profile Groups. These studies do not provide any detailed differentiation about access to SME financing depending on business age, sector, size and other firm characteristics that are identified in the literature as relevant for examining access to financing.

An important gap appears to be a lack of acknowledgement regarding the stratification of financial access within the SME sector, and the collection of data which can be disaggregated in order to assess the impact of factors such as business size, age, and stage. In addition, the relatively small number of studies makes it difficult to draw substantive conclusions about the present state of SME financing, and the issues new small and medium-sized businesses are currently facing.

Although the studies are all national in scope, the sample sizes and research methodologies vary to such a degree that it would be difficult to compare the results of these studies. The studies do provide a snapshot of issues facing the SMEs from a variety of perspectives. For example, the Groupe Secor (2001) study was conducted at the institutional level, and the majority of participants were members of the financial services industry, whereas the Canadian Federation of Independent Business study (2001) collected data through a membership survey. While both provided interesting and timely insights into issues related to SME financing, the scope of research of each was so different they are not directly comparable.

The following sections examine the research literature specific to the particular groups profiled in this study: women, youth, Aboriginals, visible minorities and language groups.

RESEARCH ON SME FINANCING FOR WOMEN

The chart below shows that over the past decade a fair bit of research has been conducted on the effects of gender on access to financing for SMEs. Several of these studies are Canadian, but this section has also been supplemented by drawing on a few key international studies and the substantial body of existing research from the United States. In spite of this, several authors of the following studies note the absence of rigorous research on issues related to gender and SME financing.

	Reference	Methodology	Type of Financing	Region	Sector
2	Allen, K.R., 1996.	Interviews, NFWBO	All	US	All
3	Angus Reid Group, 2000.	Focus group, interviews	All	Canada	All
6	BDC, 1997.	Interviews		Canada	All
7	BDC, 1999.	Same data as Ref 6		Canada	All
10	CFIB, 1995.	Survey	Bank debt	Canada	All
12	Cliff, J.E., 1998.	Interviews	Growth	Vancouver	All
13	Coleman, S., 2000.	Survey	Debt	US	All
15	Fabowale, L., et al, 1995.	Survey	Debt	Canada	All
16	Greene, P.G., et al 2001.	US VC annual surveys	VC	US	All
18	Haines, G.H., et al, 1999.	Bank loan files	Debt	Canada	All
19	Haynes, G.W., & Haynes, D.C.,	NSSFBS surveys	Debt	US	All
22	Lynch, L., 2001.	NFWBO survey	All	US	All
24	NFWBO, 1998.	Survey	All	16 countries	All
25	NFWBO, 1999.	Survey	All	Canada	All
26	NFWBO, 2000.	NFWBO study	Equity	US	All
29	OECD, 2000.	Compilation of	All	International	All
33	Thompson, Lightstone & Company, 1998	Same data as Ref 9	All	Canada	All
35	Walker, D. & Joyner, B.E., 1999.	Conceptual framework		US	All

In terms of research gaps, there are both broad and specific gaps in the existing research. In the broader context, these studies do not differentiate or stratify data based on firm characteristics (e.g., size, age, sector) and as such, vital differences between different types of SME financing are masked. In addition, the methodology employed in these studies varies widely, as does the sample size and scope of research and type of financing examined, and all of these differences make it difficult to compare findings across studies to draw broad conclusions about the accessibility of SME funding for women in Canada. While one study (Greene et al., 2001) examined the intersection of female entrepreneurs and venture capital, other studies took a far more general approach.

Although all of these studies touch on issues related to financing for female-owned SMEs, in many cases the question of finance accessibility is not the central one, and as such, the issues are often addressed indirectly rather than directly. For example, studies conducted by the BDC (1997, 1999) focus more on characteristics of women entrepreneurs, and Cliff (1998) focuses on growth rates of women-owned firms. While both make reference to the accessibility of capital for these businesses, it is a secondary issue rather than a primary one. Although there initially appears to be a considerable body of research related to financing women-owned SMEs, if the scope were restricted to Canadian studies that directly examined the question of women's access to financing the actual

number of useful studies would be much smaller.

In spite of lack of direct comparability of these studies, the overall conclusion reached (with the odd exception) is that there is no evidence to support the hypothesis that women face greater barriers in accessing SME financing because of their gender. Under this relatively straightforward conclusion, however, the research highlights notable differences in the way women approach and run their small and medium-sized businesses. Many of these are directly or indirectly related to SME financing and deserve further exploration in the context of SME financing for women. For example, Cliff (1998) and Coleman (2000) highlight different preferences of female entrepreneurs such as a tendency to be less likely to use external sources of credit, or to make deliberate choices to limit growth rates and size of their firms. However, both note no overt evidence of discrimination in access to financing, but rather that access is affected by choices made about firm characteristics, with financing being less accessible for smaller businesses than larger ones.

It is worth noting that the perception of bias towards women continues to exist in spite of lack of evidence for this bias in the research literature. With respect to debt financing, Fabowale et al. (1995) note that while their research showed no evidence of differential access to credit between male and female entrepreneurs, women were far more likely to report feelings of being treated disrespectfully by financial institutions. While several studies identified no differences in loan rates for comparably qualified male and female applicants, this begs the broader question as to whether women are able to compete equally with their male counterparts. Lack of access to debt financing is compounded by women-owned businesses having lower sales volumes, less capacity, less capital, less collateral and the owners have less business management experience than male-owned businesses (Fabowale et al., 1995).

For example, Haines, G.H. et al., (1999) note that female entrepreneurs are more likely than male entrepreneurs to be below the 'threshold of bankability' that lenders require, but argue that this in itself does not indicate gender discrimination. The OECD (2000) notes gender-based differences between male and female owned SMEs, with women tending to run small and micro-businesses, and to cluster in the service sector. The same study notes that women entering the SME sector tend to have less entrepreneurial experience than men, may be juggling the demands of their business with family responsibilities, and often have different cultural and social values, in addition to 'less conventional' thinking about small business. In terms of access to financing for women-owned SMEs, this raises broader (and thornier) questions as to 1) whether banks are basing access to financing on a model that is based on the assumption that women entrepreneurs will be very much like their male counterparts, and 2) whether a new model may be more relevant for evaluating finance needs for female entrepreneurs.

With respect to equity financing, an Industry Canada (1999) report notes that female entrepreneurs work most frequently in the service sector (61.5%), followed by retail and wholesale trade (17.5%), agriculture (9.5%) and finance/insurance (5%). As these tend not to be high-growth sectors, it is unlikely that these entrepreneurs will have much access to financing through venture capital or angel investments.

By comparison, Allen (1996) found that female entrepreneurs in high-growth industries are very similar to their male counterparts in these areas and are correspondingly likely to have more financing options open to them than women in low-growth sectors. In spite of this, Greene et al. (2001) found that less than 5% of U.S. venture capital was invested in firms owned by women. This likely reflects the fact that only a small percentage of women are starting businesses in high growth sectors that attract venture capital, the fact that women's entry into these sectors is relatively recent, and also the fact that they have a lack of access to networks that would provide access to venture capital.

RESEARCH ON SME FINANCING FOR YOUTH

As the chart below illustrates, research on the topic of SME financing for Canadian youth is neither extensive nor deep.

	Reference	Methodology	Type of Financing	Region	Sector	Stage
30	R.A. Malatest & Associates	Several methods		BC	All	All
4	ACOA, 1995.	Best practices		Atlantic	All	All
20	HRDC, 1998.	Stats Canada data		Canada	All	All
27	Omnifacts Research, 2000.	Focus groups		Atlantic	All	All
28	OAYEC, 2000.	Interviews	All	Ontario	KBI	All
37	Yearwood, E., 2000.	Various sources	All	US	All	All

Besides the paucity of published information, there are two other gaps of note in this literature. First, none of these studies were published in peer-reviewed journals; all were instead conducted by government agencies or by consulting companies on behalf of government agencies. The second notable gap is the regional nature of these studies. Of the 5 Canadian studies examined with a focus on Youth, only one was national in scope, with the others being regional or provincial in scope.

Similar to many of the studies on women-owned SMEs, the focus of most of these studies is a general one on ‘young entrepreneurs’ and their characteristics and experiences, rather than a more specific focus on the challenges this particular Profile Group may be facing in accessing funding for their business ventures. While each report touches on some aspects of access to capital, they do so as an indirect part of the broader picture of youth entrepreneurship, rather than as a direct and specific issue. As is the case with every Profile Group reviewed in this study, the literature on young entrepreneurs does not make distinctions between firms’ characteristics (e.g., age, size, sector) and effects on access to capital for this group.

While the various studies note that young entrepreneurs are typically defined as those between the ages of 16-29 (and some programs include those up to the age of 35) there was little distinction made between ‘self-employment’ and ‘small business’ development, and as such little discussion regarding the very different financing needs of each group. In addition, there was no real evaluation of the different business support needs of youth using young entrepreneurship programs as seed money for a summer business, and older individuals looking for start-up funding for entrepreneurial ventures. The reliance on family resource (love money) was mentioned, but not examined in any depth.

The diversity of this group results in a similarly diverse set of barriers faced by the youth population attempting to secure SME financing. With respect to debt financing, it is difficult for many youth to access this source of financial capital due to the fact that many are too young to have a substantive credit history, or to have collateral sufficient to secure loans or lines of credit. Because of their age, they are also unlikely to have the type of business experience or track record that financial institutions would look for in assessing creditworthiness. In addition, some potential entrepreneurs may be carrying student debts which will also make it harder to secure debt financing for new ventures. These barriers to debt financing were captured in the findings of the OAYAC (2000)

study of young entrepreneurs where it was noted that 66% of study participants had mixed or negative experiences with financial institutions.

These age-related barriers are exacerbated by the typical firm characteristics of businesses started by youth. A 1998 HRDC report states that 77% of youth ventures are owned and operated by a single person, placing these businesses very firmly in the 'microbusiness' category. 75% of youth-owned businesses were in the service sector, a low-growth area. These particular firm characteristics have implications for the access of business capital, as most of these ventures are in the early stages of growth (looking for seed money or start-up funds); have limited tangible assets and low profit margins. These characteristics also limit the availability of angel investors and venture capital as sources of equity financing.

Malatest (2000) note that lack of access to start-up funds is a significant issue for this group. There is anecdotal evidence (Yearwood, 2000) to suggest that the largest source of funding for youth entrepreneurs is love money from friends and family. In cases where young entrepreneurs are looking to start businesses in the information technology sector, barriers to debt financing still appear to exist, likely for the reasons listed above. OAYEC (2000) statistics showing that 46% of new business ventures were financed through personal savings, 38% through love money, and only 28% through loans or lines of credit, and 9% through youth business loans. Statistics for venture capital funding were not given, leading to the possibility that young entrepreneurs do not have adequate access to this source of funding. This may be due to lack of experience in their sector, geographic location, lack of opportunities to network or a combination of the above.

RESEARCH ON SME FINANCING FOR ABORIGINALS

As is the case with SME financing for young entrepreneurs, the research focusing on SME financing for Aboriginals is also quite limited.

	Reference	Methodology	Sample size	Type of Financing	Region	Sector
1	Aboriginal Business Canada,	Reference 8 data	2,511	All	Canada	All
3	Angus Reid Group, 2000.	Focus group,	97	All	Canada	All
8	Caldwell, D. & Hunt, P.,	Survey	2,511	All	Canada	All
30	R.A. Malatest & Associates	Several methods	400		BC	All
33	Thompson, Lightstone &	Same data as Ref 9	3,190	All	Canada	All

Not only is the number of Canadian studies related to Aboriginals and SMEs small, but two of the five studies included here include aboriginals as part of a much larger study. In the case of the study undertaken by the Angus Reid Group (2000), while the focus of the research was national, it includes interviews with only 14 Aboriginals from three provinces (Quebec, Ontario, and Manitoba), and the results of the study include fewer than two pages specific to particular issues faced by Aboriginal peoples.

In addition, two of the other studies draw on the same primary data source; the Aboriginal People's Survey provides the data for the reports of Aboriginal Business Canada (2001) and Caldwell and Hunt (1998).

Based on the findings for this study, the research does not exist to verify a direct bias against Aboriginals by financial institutions. It may be similar to the situation with female entrepreneurs, in that fewer Aboriginals meet the 'threshold bankability' requirements (in part due to laws which restrict reserve lands being used as collateral) and it is more difficult to access capital through traditional bank loans and programs. Significantly more research would be required to address this complex issue with any depth.

Overall, the research on Aboriginal SMEs is general rather than specific, and focuses primarily on characteristics and experiences of Aboriginal-owned small and medium-sized businesses, rather than directly examining barriers to financing that this Profile Group faces. The one exception to this is the report from Aboriginal Business Canada (2001) which has a small section on the financing challenges faced by Aboriginal peoples. The report describes an Aboriginal perception of inadequate access to capital, and remarks that this may result from lack of collateral and underdeveloped relationships with financial institutions. This same report also notes that Aboriginal businesses tend to be less profitable on average than Canadian SMEs as a whole, and that they tend to be concentrated in the primary sector which may affect access to financial capital.

Caldwell and Hunt (1998) determined that 56% of Aboriginal entrepreneurs felt they had inadequate access to debt and equity financing for their businesses. With respect to debt financing, barriers noted by Aboriginals include lack of collateral (40% of respondents); legislation prohibiting the use of on-reserve assets as collateral (30%); lack of local financial institutions to work with (27%); and lack of firm profitability (22%).

With respect to equity financing, the concentration of Aboriginal businesses in low-growth sectors such as primary

industries (e.g., logging, farming, mining); recreation and personal services (e.g., casinos, photography); construction and retail/wholesale trade limits, the accessibility of angel investment or venture capital financing.

Aboriginal-owned businesses tend to be small scale, with only 12% requiring more than \$100,000 in capitalization, while over 60% required less than \$25,000 (Caldwell and Hunt, 1998). As mentioned earlier in this report, accessing financial capital for newer, smaller ventures in low-growth sectors is particularly difficult.

Caldwell and Hunt (1998) report that 58% of survey participants believe that lack of personal resources is a barrier to securing SME financing, while 36% noted the lack of venture capital availability. Other barriers identified were the absence of community investment funds (31%) and the inability of friends and family to invest (16%). Access to personal investment and love money is particularly limited for on-reserve Aboriginals due to legislation prohibiting use of on-reserve assets as collateral. All of these factors will be exacerbated in instances where Aboriginals are geographically located in rural and/or remote areas where accessibility to SME financing is typically more limited than in urban and central areas.

RESEARCH ON SME FINANCING FOR MINORITY GROUPS (VISIBLE MINORITIES AND LANGUAGE GROUPS)

Attempting to find research related to SME financing for visible and language minorities in Canada proved to be very challenging. The following is a sample of studies found that related in some way to the topic.

	Reference	Methodology	Region	Sector	Stage
14	Dana, Leo-Paul, 1997.	Literature review	Canada	All	All
23	Marmen, L, 1999	Stats Canada data	Canada	N/A	N/A
31	Rath, J., 2000.	Several methods	Internation	All	All
33	Thompson, Lightstone & Company, 1998	Same data as Ref 9	Canada	All	All
34	US SBA Office of Advocacy, 1999.	US stats sources	US	All	All
36	Williams, C., 2000.	Various sources	US	All	All

Of these six studies, it should be noted that only half are Canadian, and of these, two (Marmen, 1999 and Dana, 1997) do not even touch on issues related to SME financing. As such, it is difficult to even formulate tentative hypotheses regarding the accessibility of SME financing for these Profile Groups. Both of these articles would provide useful contextual and background information for future research in this area, but neither provides substantive information as to the access these Profile Groups currently have to SME capital.

Future research on linguistic or ethnic minorities groups would benefit from a clearly articulated definition of who comprises these groups. For example, in this project the term ‘language group’ is used to refer to not only to Anglophone and Francophones who are linguistic minorities in various regions, but also includes local linguistic minorities across the country. In this case, the barriers faced by ‘non-official’ language minorities may be very different than those faced by official language groups. Similarly, it would be helpful to define ethnic minorities and the scale at which minority status is being applied. For example Asians may comprise a minority population when compared to the population of Canada, but not so in many parts of urban British Columbia. Because of the complexity of evaluating linguistic and ethnic minority status, clear definitions will help define the parameters of future research in this very under researched area.

A few of these articles contain useful finance-related insights and data. The SBA Office of Advocacy (1999) notes some differences in the financing of minority-owned SMEs (e.g., they are less likely to use credit than SMEs on average; they are less likely to access credit through a commercial bank than the SME sector overall) but does not offer up explanations as to why this might be. Thompson, Lightstone and Company (1998) identify some differences of note in Canada with reference to visible minorities (e.g., SMEs are more likely to be clustered in manufacturing and retail sectors than SMEs overall; they have a higher overall reliance on family, friends and employees for investment capital) but does not delve into the reasons behind these findings, or directly address the question of access to financial capital for this Profile Group.

In terms of the accessibility of debt and equity financing, as there is such wide variability in the populations across these Profile Groups, their financing needs will be equally variable. Without data to provide insights into types of ventures these entrepreneurs are likely to engage in, it is difficult to identify barriers they may face. However, some general guidelines can be inferred from the results of the previous Profile Groups. Availability of debt financing will depend on the characteristics of particular entrepreneurs. Those with strong credit histories and

extensive business track records will have a much easier time accessing loans and lines of credit than those without collateral or good credit ratings.

Similarly, with respect to equity financing, minority entrepreneurs working in low-growth areas will be less likely to attract angel investment or venture capital financing. They may also have difficulty accessing the networks for this funding, depending on their geographic location, their previous experience and their language fluency. Some may have good access to personal savings and resources from friends and family, but this will be highly variable across minority populations. As noted above, the diversity within these profile groups requires more focus on particular sub-strata of these groups in order to provide meaningful data on barriers to SME financing.

FRAMEWORK FOR FUTURE RESEARCH

As the analysis highlights, there are significant gaps in existing research on barriers to SME financing in general, and barriers faced by specific business-owner profiles in particular. Because of this, it is difficult to determine whether the Profile Groups examined in this study faced greater (or lesser) barriers to a comparable SME population in general.

In order to collect data to address this issue specifically, it is critical to have adequate baseline data on SME financing to compare against the experiences of Profile Groups. Ideally, this will be in the form of a data set that can be disaggregated by relevant criteria, in particular data related to firm characteristics (e.g., age, stage, sector, industry, geographic location); data related to type of financing sought (e.g., debt financing, equity financing); and data related to business-owner characteristics (e.g., gender, ethnicity, age).

Based on the findings of Phase 1 and 2 of this project, national-level survey-based research is recommended, sampling across randomly selected members of the existing SME population. The results can be captured in database format allowing for a variety of cross-cuts on the collected information including business owner characteristics.

A sample size of approximately 10,000 SMEs is recommended, which should be large enough to ensure that data will be collected for at least 1,000 SMEs in each business owner sub-category. The findings of this survey research will provide a comprehensive, up-to-date picture of the state of the SME financing situation, a picture that does not currently exist.

It should be noted this survey addresses only SMEs which are already in existence. While it would be desirable to collect information about ‘non-participants’ as well (e.g., those who were unable to secure any form of financing for an entrepreneurial venture, or, those who did not attempt to due to other considerations - eg. student loans that need to be repaid) it would also be very expensive and time consuming to broaden the sample to ensure the inclusion of a significant number of ‘non-participants’ in this survey.

For this survey, collection of data in three main areas is suggested: firm characteristics; type of financing sought and received; and business owner profile. Data on the following variables is recommended for inclusion:

(Note: the categorization of data within sub-categories (e.g., age ranges) is somewhat arbitrary and should be adjusted as necessary to accommodate existing data sets or categorizations.)

Firm Characteristics:

Age

- < 2 years
- 2-5 years
- 5-10 years
- > 10 years

Size (# of employees)

- Self only
- 2-5 employees
- 5-25 employees
- 25-100 employees
- > 100 employees

Size (degree of capitalization)

- <\$50,000?
- \$50,000 - \$250,000?
- \$250,000-\$1,000,000
- >\$1,000,000

Type of funding obtained

- Seed money
- Start-up
- Working capital
- Expansion capital

Sector

- Primary (agriculture, natural resources)
- Secondary (manufacturing)
- Tertiary (services and retailing)
- Quaternary (knowledge-based industries)

Average annual growth rate over the last 3 years

- <5%
- 5-15%
- 15-30%
- >30%

Geographic Location

- Province of business
- Population of Community
 - < 10,000
 - 10,000 – 50,000
 - 50,000 – 250,000
 - 250,000 – 1,000,000
 - >1,000,000

Note: If over the history of the company all have been maintained, the questionnaire will have to be designed to capture each stage.

Financing Types:

Debt Financing

- Of the following, which types of debt financing have been sought?
 - Bank loan
 - Private loan
 - Operating line of credit
 - Credit card
 - Leases
 - Supplier credit contracts
 - Government-direct investment
 - Government-backed loans

- Of the following, which types of debt financing have been received?
 - Bank loan
 - Private loan
 - Operating line of credit
 - Credit card
 - Leases
 - Supplier credit contracts
 - Government-direct investment
 - Government-backed loans

Equity Financing

- Of the following, which types of equity financing have been sought?
 - Personal investment
 - Investment from friends and family (love money)
 - Angel investment
 - Venture capital investment
 - Institutional (eg. Pension fund, large company)
 - Bank

- Of the following, which types of equity financing have been received?
 - Personal investment
 - Investment from friends and family (love money)
 - Angel investment
 - Venture capital investment
 - Institutional
 - Bank

Business Owner Characteristics:

Gender

- Male
- Female

Age

- <20 years
- 20-30 years
- 30-50 years
- >50 years

Ethnicity

- English Canadian
- French Canadian
- Aboriginal
 - On-reserve
 - Off-reserve
- Other (please specify)

Language Group

- English
- French
- Other (please specify)

Extent of Previous Business Experience before financing indicated

- <1 year
- 1-5 years
- 5-10 years
- >10 years

Others as relevant.

Interrogating the Database

If the above information is collected in database format, it can be sorted in a variety of ways that will not only address the questions that were the original drivers of this research project, but also extend significantly beyond the original scope of this project.

This information would provide baseline data on the accessibility of financing for SMEs across Canada, and allow researchers to test the hypotheses raised in the research literature and in this project. It emerges repeatedly that firm characteristics (e.g., size, age, industry, sector, geographic location) play a significant role in determining an entrepreneur's access to funding, and in the case of debt financing, are more important than the characteristics of the business owner. However, the state of Canadian research in this area is not comprehensive enough to prove or disprove this hypothesis.

Without adequate baseline data for the SME sector as a whole, it is very difficult to determine whether the barriers faced by Profile Groups are greater or lesser than those faced by others in the sector. To answer this question, data are required not only for the experiences of the Profile Groups, but also on the entire SME sector for comparative purposes. As an example, data collected may show that women-owned businesses receive only 10% of venture capital in Canada. Knowing that venture capitalists fund only certain types of entrepreneurial ventures (typically knowledge-based industries with a high potential for growth) this figure is only meaningful when compared to the percentage of women-owned businesses that meet the criteria to be eligible for venture capital.

With respect to particular Profile Groups, the database could be sorted and cross-cut in a variety of ways. Queries could be made to identify all SMEs owned by particular Profile Groups and these results could then be cross-referenced to other variables to the desired level of specificity. As an example, data cuts could be done to identify:

- SMEs owned by women, and of this population:

- SMEs owned by Aboriginal women;
 - Searching for/receiving debt financing
 - Searching for/receiving equity financing
- SMEs owned by women under the age of 30;
- SMEs owned by women in knowledge-based industries;
 - % receiving venture capital
- SMEs owned by women with >5 employees;
 - In low-growth sectors
 - In high-growth sectors
- Others cross-cuts as of interest (other suggestions below)

Based on the findings of the literature review and the gap analysis, the following areas of investigation are recommended for specific Profile Groups.

Women:

- Disaggregation of data re: expected growth of business (e.g., % starting businesses in low-growth vs. high-growth sectors);
- Extent of business experience on access to debt and equity financing;
- Disaggregation of data according to business size (e.g., micro-business, small business, medium-sized enterprise) and impact of business size on funding;
- Experiences with financial institutions (e.g. range of debt financing options sought vs. those received);
- Others?
- Other issues of interest, which would require further data, likely collected through qualitative means such as focus groups:
 - Impact of family responsibilities on female entrepreneurs
 - Attitudes towards business growth and type of financing sought.

Youth:

- Extent of business experience on access to debt and equity financing;
- Impact of lack of equity or collateral and available financing options;
- Concentration on early stage businesses and impact on financing available;
- Concentration of youth in micro-business ventures and impact on financing;
- Impact of age on SME financing options (e.g., differences between those <20 years, and those 20-30 years of age);
- Experience with financial institutions (e.g., range of debt financing options sought vs. those received);
- Other issues of interest, which would require further data, likely collected through qualitative means such as focus groups:
 - Impact of student debt loads on SME financing options;
 - Impact of economic strata/social capital on accessibility of 'love money';

Aboriginals:

- Differences between accessibility of SME financing between on-reserve and off-reserve Aboriginals;
- Impact of Aboriginal business concentration in low-growth sectors on access to SME financing;
- Sectoral breakdown of Aboriginal businesses (e.g., primary, secondary, tertiary and quaternary) and impact on financing options;
- Concentration of Aboriginal ventures in small-scale businesses, and effects on access to financing;
- Geographical differences (e.g., rural/urban; centre/periphery) and impacts on SME financing;

Visible Minorities and Language Groups:

- Similar to issues raised above, but tailored to suit specific interests (e.g., differences between official language minorities and other language groups);

A sample of other issues that may emerge and interesting for follow-up (based on comments in the research literature or in discussions for this project):

- Does it hold true that debt financing is more dependent on firm characteristics such as size and sector than on characteristics of business owners?
- Are business-owner characteristics more important for equity financing than firm characteristics?
- What role does geography play in the accessibility of SME financing (e.g., what differences appear between rural and urban areas? Between centre and periphery areas?)
- What is the impact of economic strata and social capital on access to love money (investment from friends and family?) How does this affect the Profile Groups?
- What type(s) of SMEs are most likely to successfully access financing? Which are least likely? How does this intersect with the business choices of Profile Groups?
- What impact does the choice of sector (e.g., primary vs. tertiary) have on the accessibility of SME funding? What are the clusterings of Profile Groups with respect to these sectors?

SUMMARY RECOMMENDATIONS

- Significant gaps exist in the current research data pertaining to business owner characteristic-related barriers to financing in particular, and to SME financing in general;
- Barriers to SME financing do exist, and vary significantly according to business type, age, stage and industry with owners facing different barriers accordingly. Data does not exist to demonstrate whether the Profile Groups face greater barriers than the general SME population when stratified according to the categories noted above;
- Based on information collected during Phase 1, the hypothesis of business owner characteristic-related barriers to financing cannot be validated on the basis of existing data;
- Additional research is needed to fill these data gaps, and analysis of barriers faced by any business owner profile will be relevant only if there is sufficient baseline data on access to financing for SMEs in general for comparative purposes;
- Future research in this area should be national in scope, and should be designed to collect SME financing data that can be disaggregated according to a variety of criteria identified as relevant in Phase 1 of this project. This research should include data collection related to firm characteristics (e.g., age, stage, sector, industry, geographic location); related to type of financing sought (e.g., debt financing, equity financing); and related to business-owner profile characteristics (e.g., gender, ethnicity, age).

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Appendix A: Summary of Research Findings

	Reference	Business Owner Group	Methodology	Sample size	Type of Financing	Region	Sector	Stage/ Size
1	Aboriginal Business Canada, 2001.	Aboriginal	Reference 8 data	2,511	All	Canada	All	All
2	Allen, K.R., 1996.	Women	Interviews, NFWBO membership survey	1,400	All	US	All	All
3	Angus Reid Group, 2000.	Aboriginal, women, youth	Focus group, interviews	97	All	Canada: rural/urban	All	All
4	ACOA, 1995.	Youth	Best practices summary			Atlantic	All	All
5	BC Stats, 2000.	All SME's	Stats Canada data			BC	All	All
6	BDC, 1997.	Women	Interviews	438		Canada	All	3-99 employees
7	BDC, 1999.	Women	Same data as Ref 6	438		Canada	All	3-99 employees
8	Caldwell, D. & Hunt, P., 1998.	Aboriginal	Survey	2,511	All	Canada	All	All
9	CBA, 2001.	All SME's	Interviews	3,190	All	Canada	All	All
10	CFIB, 1995.	Women	Survey	10,903	Bank debt	Canada	All	All
11	CFIB, 2001.	All SME's	Membership survey	10,024	All	Canada	All	All
12	Cliff, J.E., 1998.	Women	Interviews	229	Growth	Vancouver	All	Growth
13	Coleman, S., 2000.	Women	Survey	4,000	Debt	US	All	All
14	Dana, Leo-Paul, 1997.	Minority	Literature review			Canada	All	All
15	Fabowale, L., et al, 1995.	Women	Survey	14,980	Debt	Canada	All	All
16	Greene, P.G., et al 2001.	Women	US VC annual surveys	16,412	VC	US	All	All
17	Groupe Secor, 2000.	All SME's	Survey	13	Debt	Canada	All	All
18	Haines, G.H., et al, 1999.	Women	Bank loan files	1,393	Debt	Canada	All	All
19	Haynes, G.W., & Haynes, D.C., 1999.	Women	NSSF B surveys	2,284	Debt	US	All	All
20	HRDC, 1998.	Youth	Stats Canada data			Canada	All	All
21	Industry Canada, 1998..	All SME's	Review of program		Debt	Canada	All	All
22	Lynch, L., 2001.	Women	NFWBO survey	1,194	All	US	All	All
23	Marmen, L., 1999	Language minorities	Stats Canada data			Canada	N/A	N/A
24	NFWBO, 1998.	Women	Survey		All	16 countries	All	All
25	NFWBO, 1999.	Women	Survey	1,166	All	Canada	All	All
26	NFWBO, 2000.	Women	NFWBO study		Equity	US	All	All

	Reference	Business Owner Group	Methodology	Sample size	Type of Financing	Region	Sector	Stage/ Size
27	Om nifacts Research, 2000.	Youth	Focus groups	8		Atlantic	All	All
28	OAYEC, 2000.	Youth	Interviews	47	All	Ontario	KBI	All
29	OECD, 2000.	Women	Compilation of international data		All	International	All	All
30	R.A. Malatest & Associates Ltd., 2000.	Youth / Aboriginal	Several methods	400		BC	All	All
31	Rath, J., 2000.	Minority	Several methods			International	All	All
32	Statistics Canada, 1994.	All SME's	Stats Canada data		All	Canada	All	All
33	Thompson, Lightstone & Company, 1998	All, women, aboriginal, Vis Min	Same data as Ref 9	3,190	All	Canada	All	All
34	US SBA Office of Advocacy, 1999.	Minority	US stats sources		All	US	All	All
35	Walker, D. & Joyner, B.E., 1999.	Women	Conceptual framework			US	All	All
36	Williams, C., 2000.	Minority	Various sources		VC	US	All	All
37	Yearwood, E., 2000.	Youth	Various sources		All	US	All	All