Small Business Credit Survey: 2019 Report on Employer Firms

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REPORT ON EMPLOYER FIRMS 2019

SMALL BUSINESS CREDIT SURVEY

Trends in Small Businesses Lending

- Since the recession, banks have extended less credit to small firms than they did pre-recession.
- Large banks have expanded their share of the small-dollar credit market, relative to small banks.
- The dollar value of small business loans has risen slowly since the recession, while credit card lending has risen faster.
- A variety of online alternative lenders have introduced new lending products and services to small businesses.

Source: Brian S. Chen, Samuel G. Hanson, and Jeremy C. Stein, "The Decline of Big-Bank Lending to Small Business: Dynamic Impacts on Local Credit and Labor Markets." Harvard Business School. 2017. http://www.frbsf.org/economic-research/files/el2011-32.pdf; "Small Business Lending After the Financial Crisis: A New Competititve Landscape for Community Banks," Julapa A. Jagtiani and Cathy Lemieux. *Economic Perspectives*, Vol. 40, No. 3, 2016., Federal Reserve Bank of Chicago.

Small Business Credit Survey: Purpose

- Gives policy makers and lenders a better understanding of the needs of small businesses to inform incentive, protections, and lending product development.
- Provides small businesses and technical assistance providers with information to make informed decisions about credit strategies.
- Offers researchers more information to begin to discern what will help these businesses grow more, grow faster, and grow the economy.

SBCS Background and Methodology

- Small Business Credit Survey (SBCS) started in 2014.
- A small business is a firm with 500 or fewer employees.
- It is conducted every fall beginning in September.
- Respondent pool is based on a convenience sample.
- Data is weighted by firm age, geography, industry and employment size.
- All 12 Federal Reserve Banks began participating in 2016.
- Approximately 12,455 employer and non-employer firms responded to the 2018 survey.

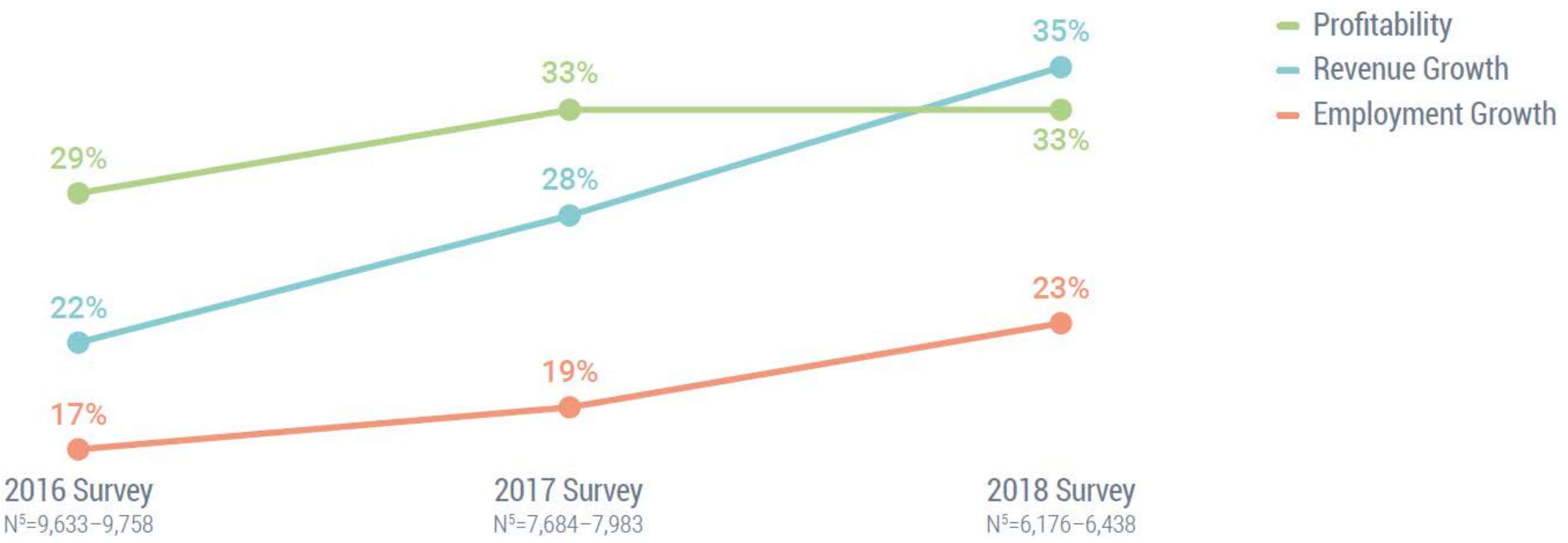
Key Findings – All Employer Firms

- Both revenue and employment growth improved from 2017.
- Share of profitable firms remained the same.
- Outlook for 2019 is more tempered.
- While credit demand increased marginally in 2018, the share of firms receiving credit remained essentially flat.
- Startup firms and firms with high credit risk continued to have financing shortfalls.
- Online lenders saw applications increase by approximately one-third from the prior year.
- Applicants remain dissatisfied with the interest rates and terms offered by online lenders relative to traditional lenders.

Source: Small Business Credit Survey, Federal Reserve Banks

The share of firms reporting revenue and employment growth increased from 2017, but the share of firms operating at a profit remained flat.

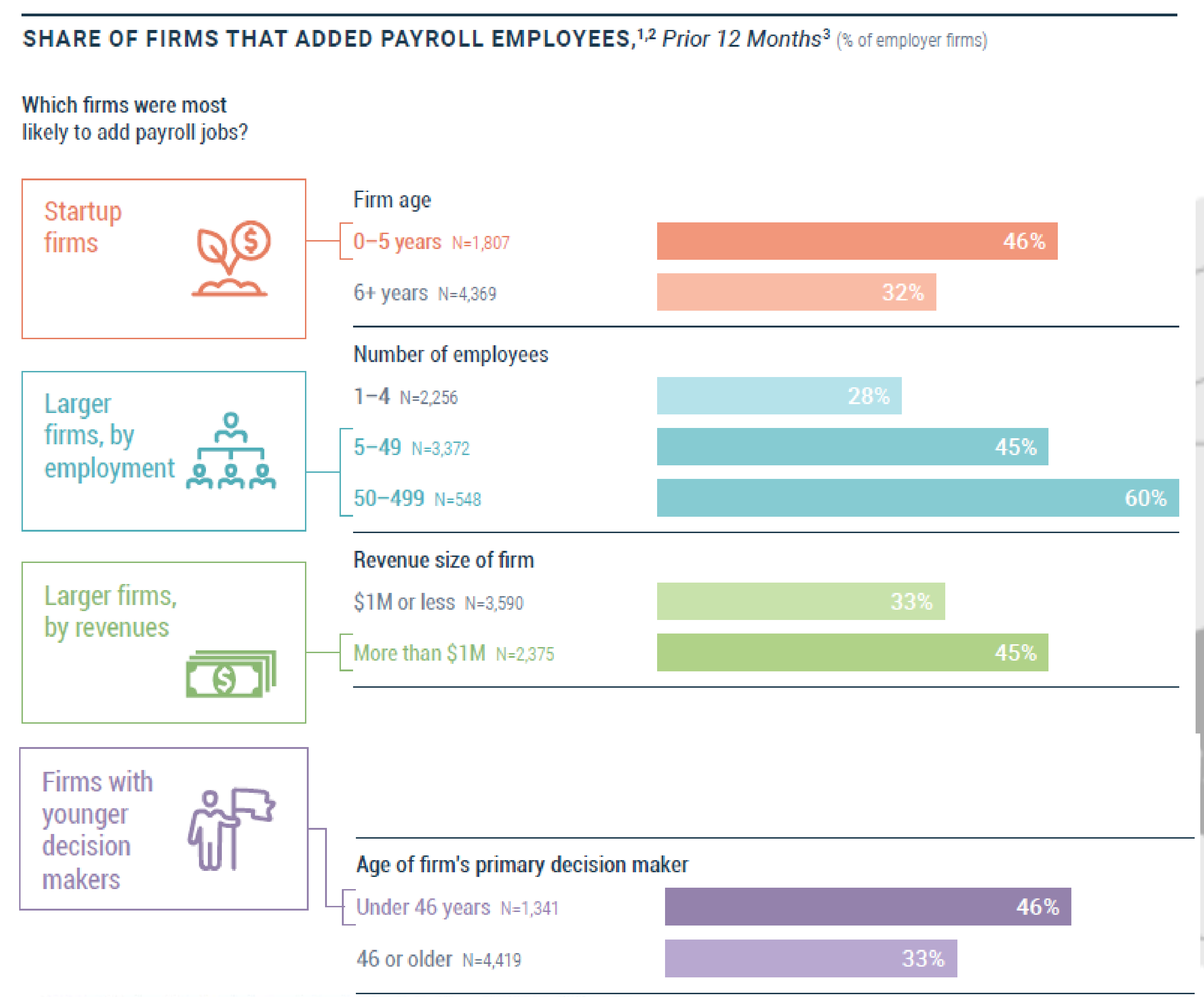
EMPLOYER FIRM PERFORMANCE INDICES,[3,4] *Prior 12 Months*[2] (% of employer firms)



1 *Percentages may not sum to 100 due to rounding.*
2 *Approximately the second half of the prior year through the second half of the surveyed year.*
3 *For revenue and employment growth, the index is the share reporting growth minus the share reporting a reduction. For profitability, it is the share profitable minus the share at a loss.*
4 *Time series values shown here differ from the 2018 report as a result of improvements to the weighting scheme. See Methodology for details.*
5 *Questions were asked separately, thus the number of observations may differ slightly between questions.*

Source: Small Business Credit Survey, Federal Reserve Banks

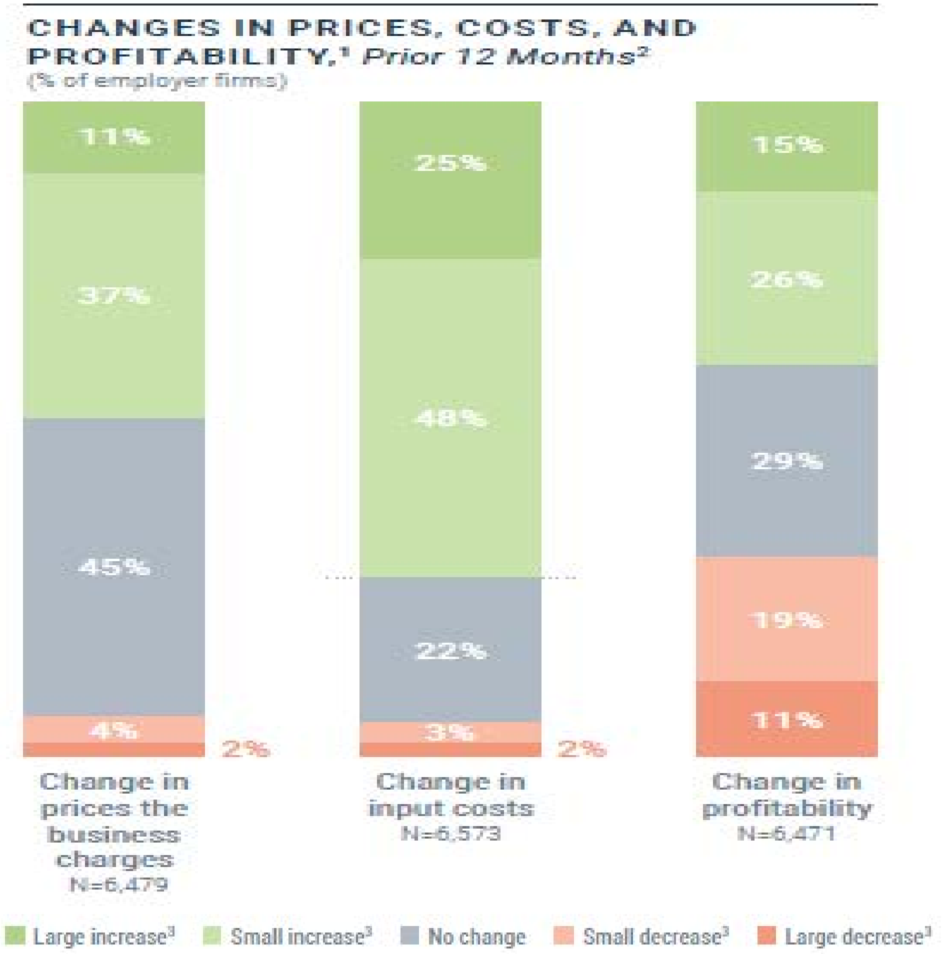
Employment gains were strongest among startups, firms with five or more employees, firms with more than $1M in annual revenues, and firms with younger decision makers (46 years of age or younger).



1 The characteristics shown in darker bars in the chart are related to employment growth at a significance level of 0.05 using logistic regression. See Methodology for more detail.
2 Additional variables were tested for statistical significance, including credit risk, gender, and race/ethnicity including Asian. None of these factors were significantly related to a firm's likelihood of adding payroll employees.
3 Approximately the second half of 2017 through the second half of 2018.

Source: Small Business Credit Survey, Federal Reserve Banks

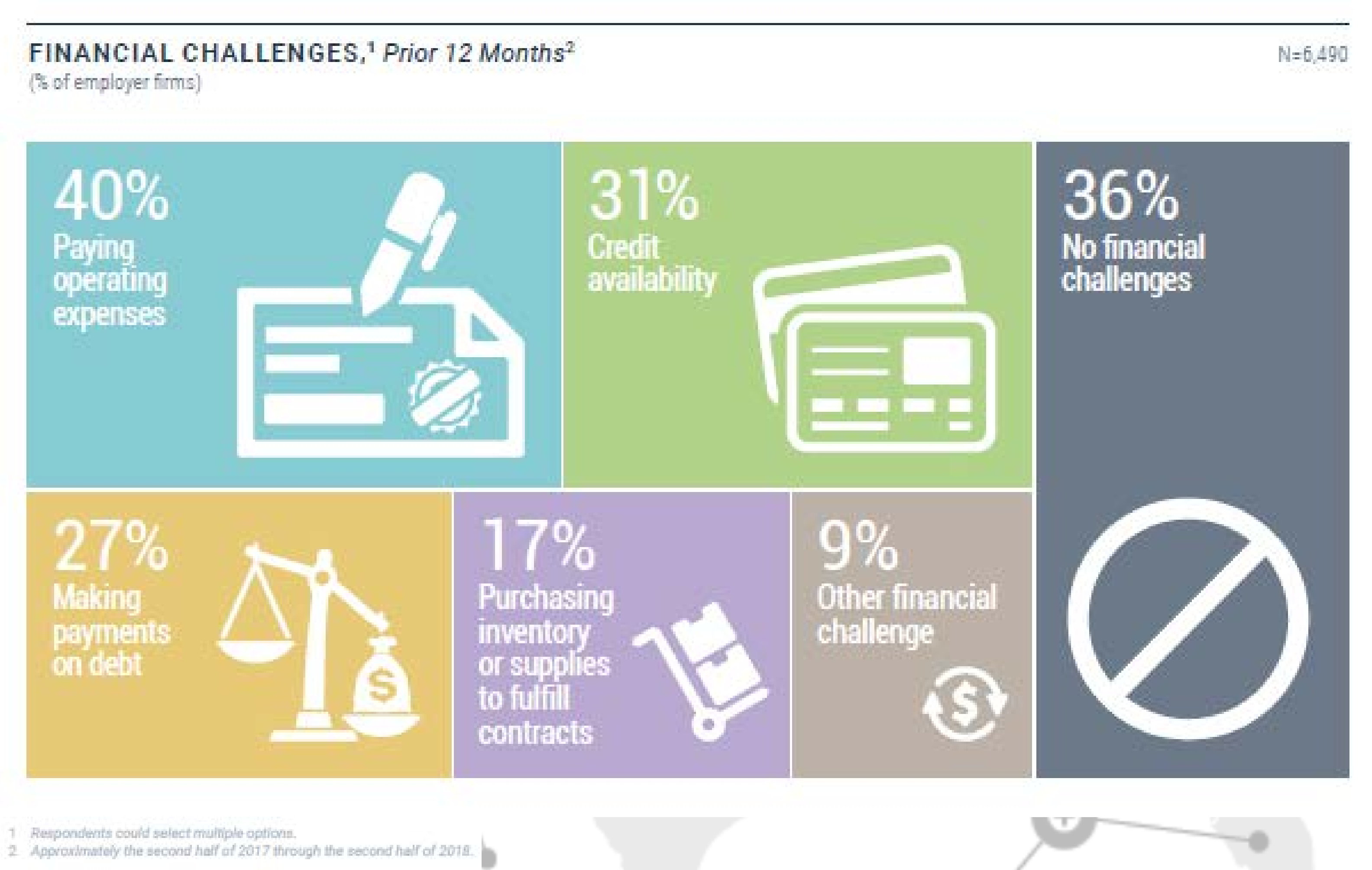
A majority of firms (73%) saw input costs increase in the prior 12 months.



1 Percentages may not sum to 100 due to rounding.
2 Approximately the second half of 2017 through the second half of 2018.
3 'Large' refers to a change of 4% or greater. 'Small' refers to a nonzero change that is less than 4%.

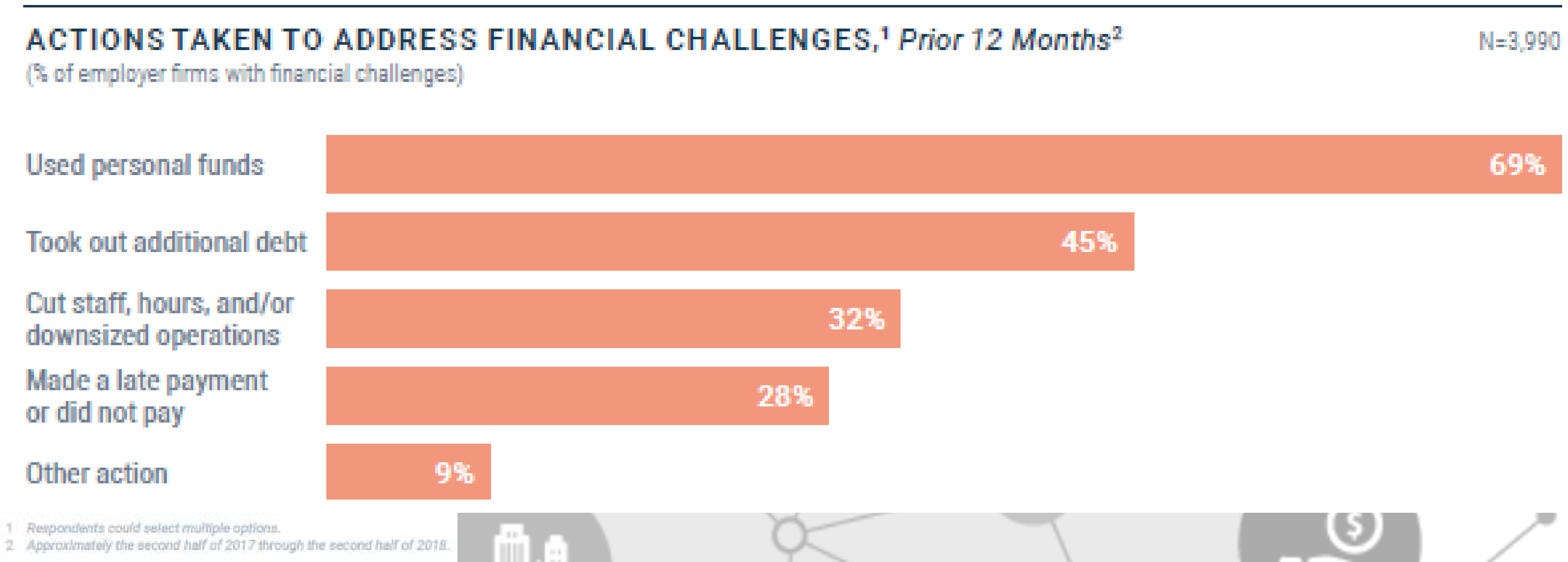
Source: Small Business Credit Survey, Federal Reserve Banks

Nearly two-thirds of firms (64%) continued to experience financial challenges, including difficulties with managing operating expenses, scarcity of credit, and challenges making debt payments.

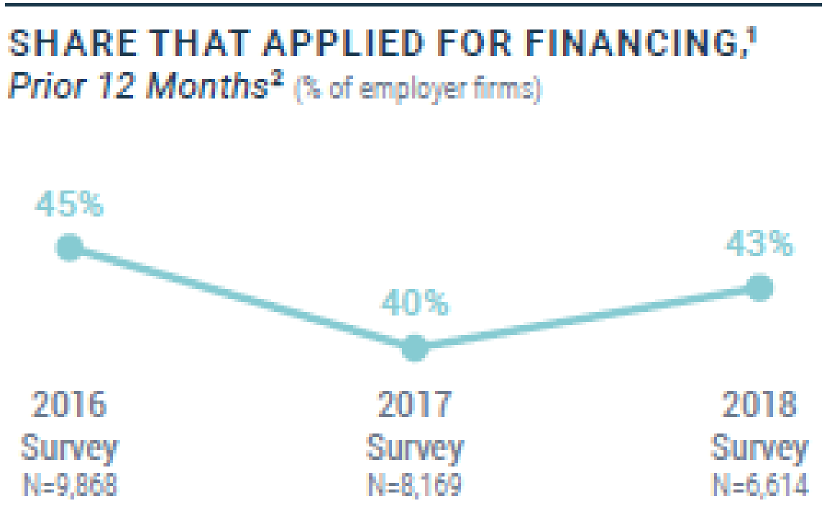


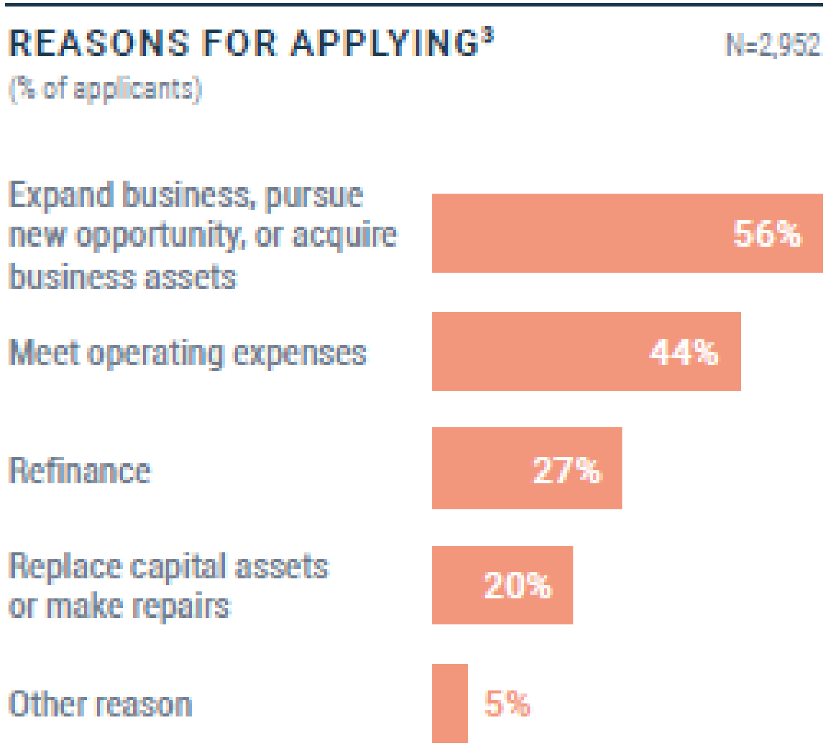
Source: Small Business Credit Survey, Federal Reserve Banks

Over two-thirds of these firms (69%) relied on personal finances to cover their costs, while 45% of firms took out additional debt.



Respondents showed consistent year-over-year demand for new financing, with 43% of firms applying for new capital in 2018, similar to 40% in 2017.



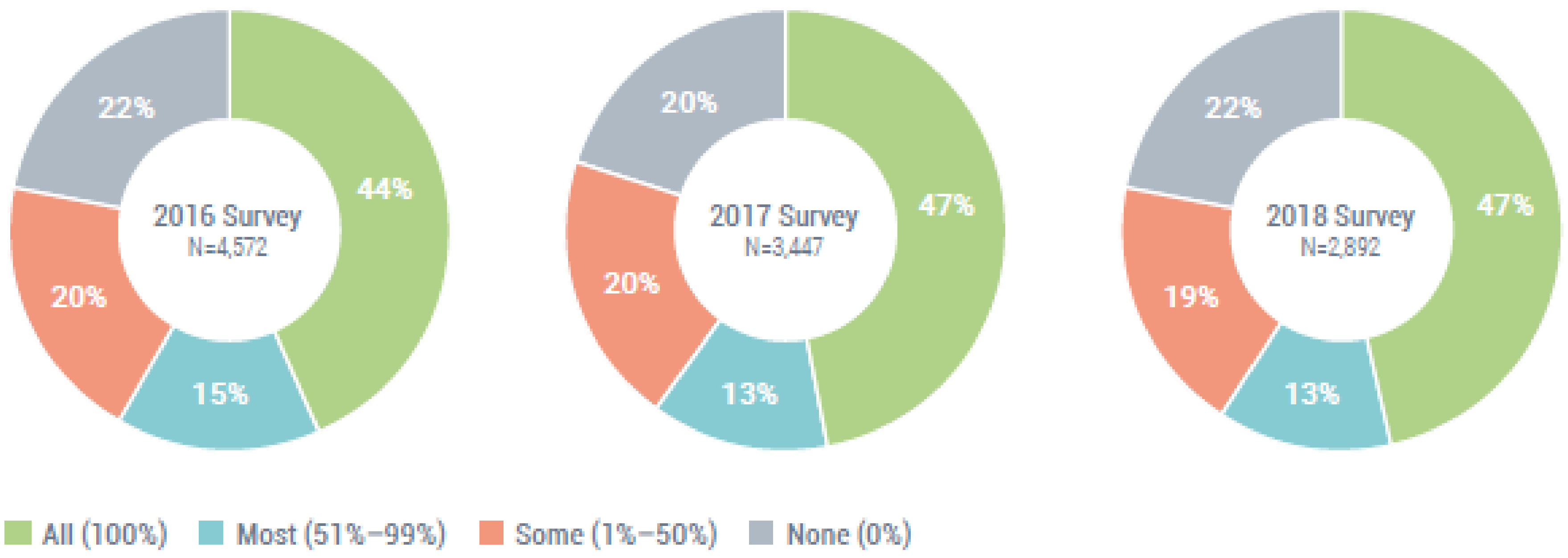


1 Due to improvements in weighting methodology, sample counts have changed from the 2018 report. However, time series estimates for this variable have not substantially changed from the 2018 report. See Methodology for details.
2 Approximately the second half of the prior year through the second half of the surveyed year.
3 Respondents could select multiple options. Respondents who selected 'other' were asked to explain their reason for applying. They often indicated that they were looking to start a business or to obtain a credit line in case they needed it.

Source: Small Business Credit Survey, Federal Reserve Banks

Nearly half of applicants (47%) received the full amount of funding they requested, similar to the 2017 survey.

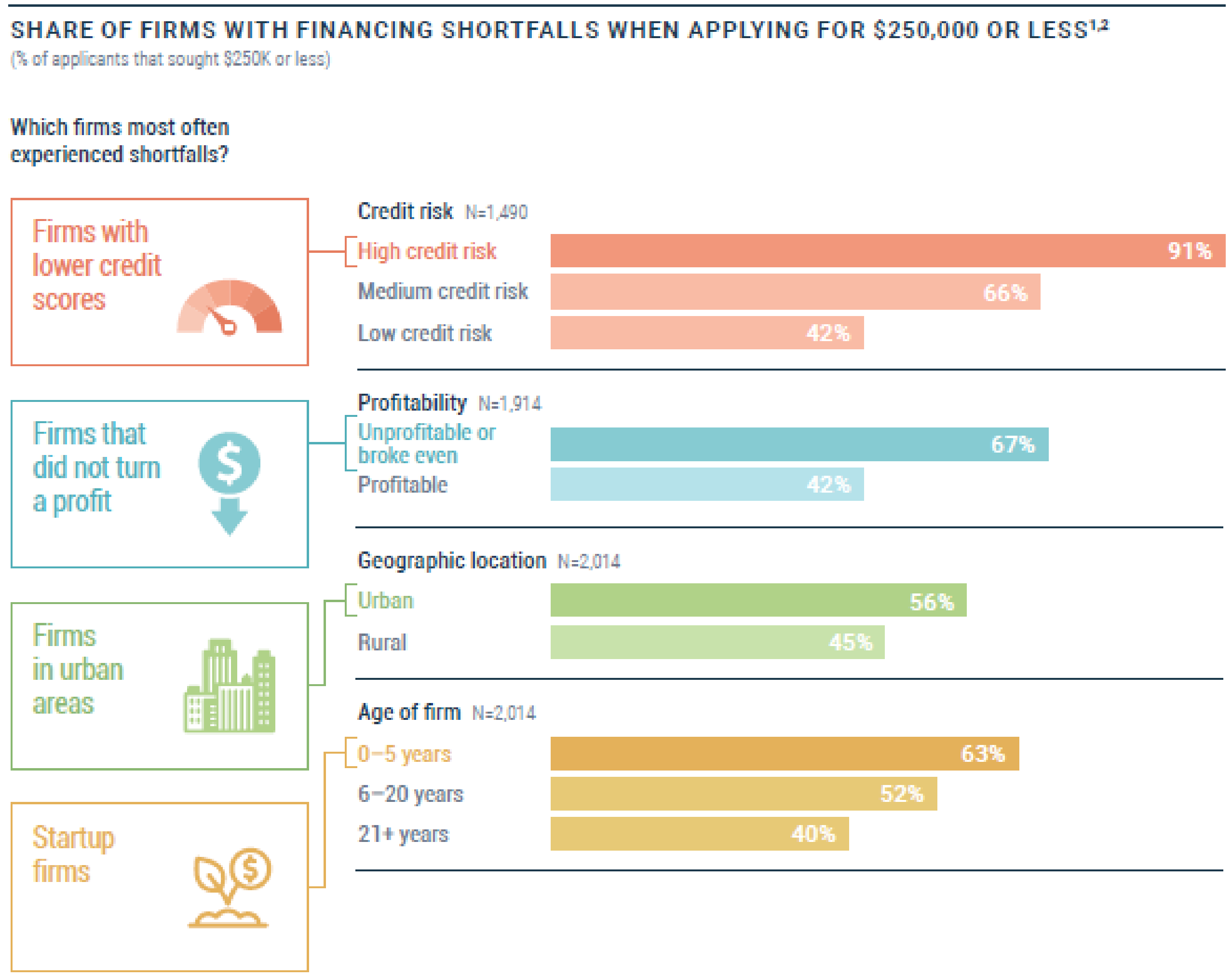
TOTAL FINANCING RECEIVED[1,2,3,4] (% of applicants)



1 Percentages may not sum to 100 due to rounding.
2 Share of financing received across all types of financing. Response option 'unsure' excluded from chart.
3 Self-reported business credit score or personal credit score, depending on which is used. If the firm uses both, the higher risk rating is used. 'Low credit risk' is a 80–100 business credit score or 720+ personal credit score. 'Medium credit risk' is a 50–79 business credit score or a 620–719 personal credit score. 'High credit risk' is a 1–49 business credit score or a <620 personal credit score.
4 Time series values shown here differ from the 2018 report as a result of improvements to the weighting scheme. See Methodology for details.

Source: Small Business Credit Survey, Federal Reserve Banks

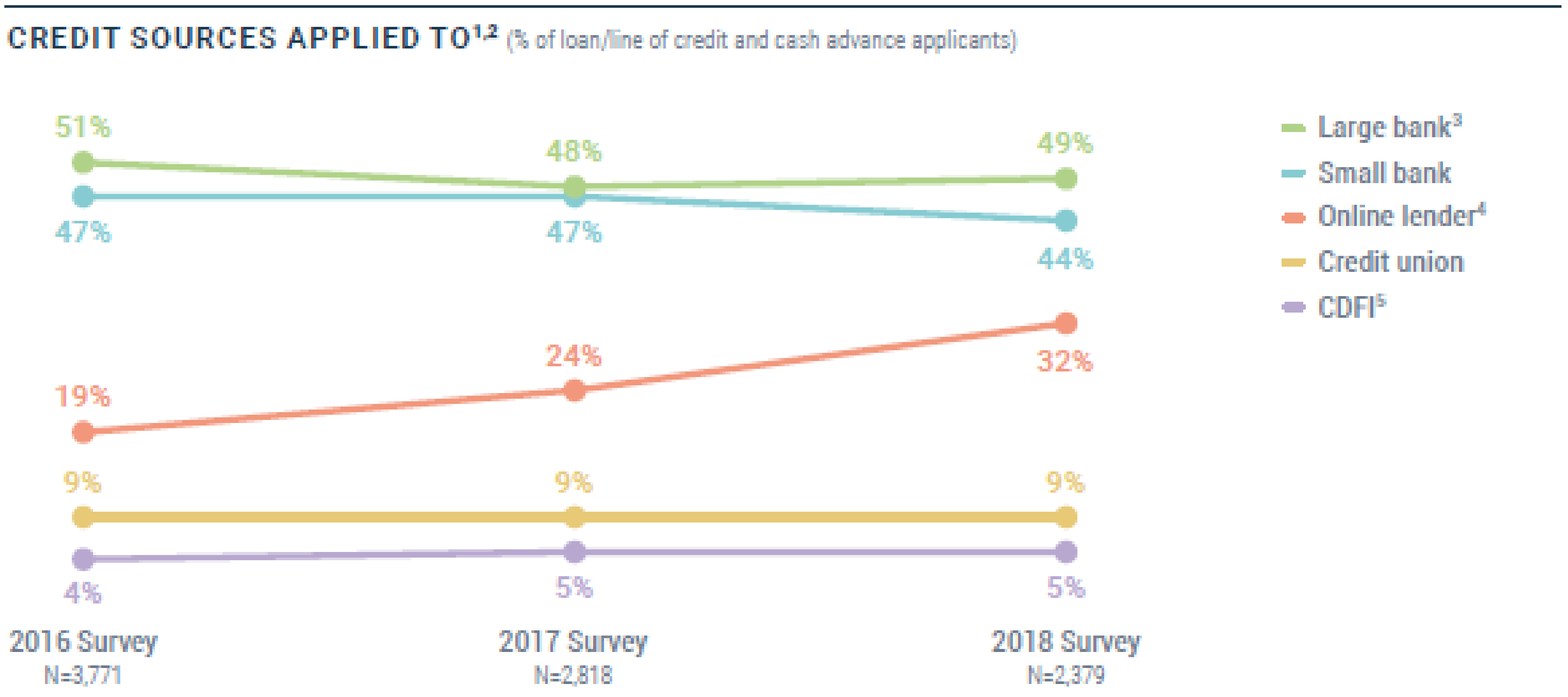
Financing shortfalls were particularly pronounced among firms with weak credit profiles, unprofitable firms, younger firms, and firms in urban areas.



1 Based on prior 12 months. Approximately the second half of 2017 through the second half of 2018. The following factors were not statistically significant predictors of funding shortfalls for firms seeking $1–$250K in financing: minority business ownership, women business ownership, industry, size (employees and revenue).
2 The characteristics shown in darker bars in the chart are related to financing shortfalls at a significance level of 0.05 using logistic regression. See Methodology for more detail.

Source: Small Business Credit Survey, Federal Reserve Banks

Applications to online lenders continued their growth trend with 32% of applicant firms turning to such lenders in 2018, up from 24% in 2017, and 19% in 2016.



1 Respondents could select multiple options.
2 Time series values shown here differ from the 2018 report as a result of improvements to the weighting scheme. See Methodology for details.
3 Respondents were provided a list of large banks (those with at least $10B in total deposits) operating in their state.
4 'Online lenders' are defined as nonbank lenders including Lending Club, OnDeck, CAN Capital, PayPal Working Capital, Kabbage, etc.

Source: Small Business Credit Survey, Federal Reserve Banks

Applicants expected online lenders would make faster funding decisions, would be more likely to provide funding, and would not require collateral.

TOP FACTORS INFLUENCING WHERE FIRMS APPLY[1,2] (% of loan/line of credit and cash advance applicants at source)

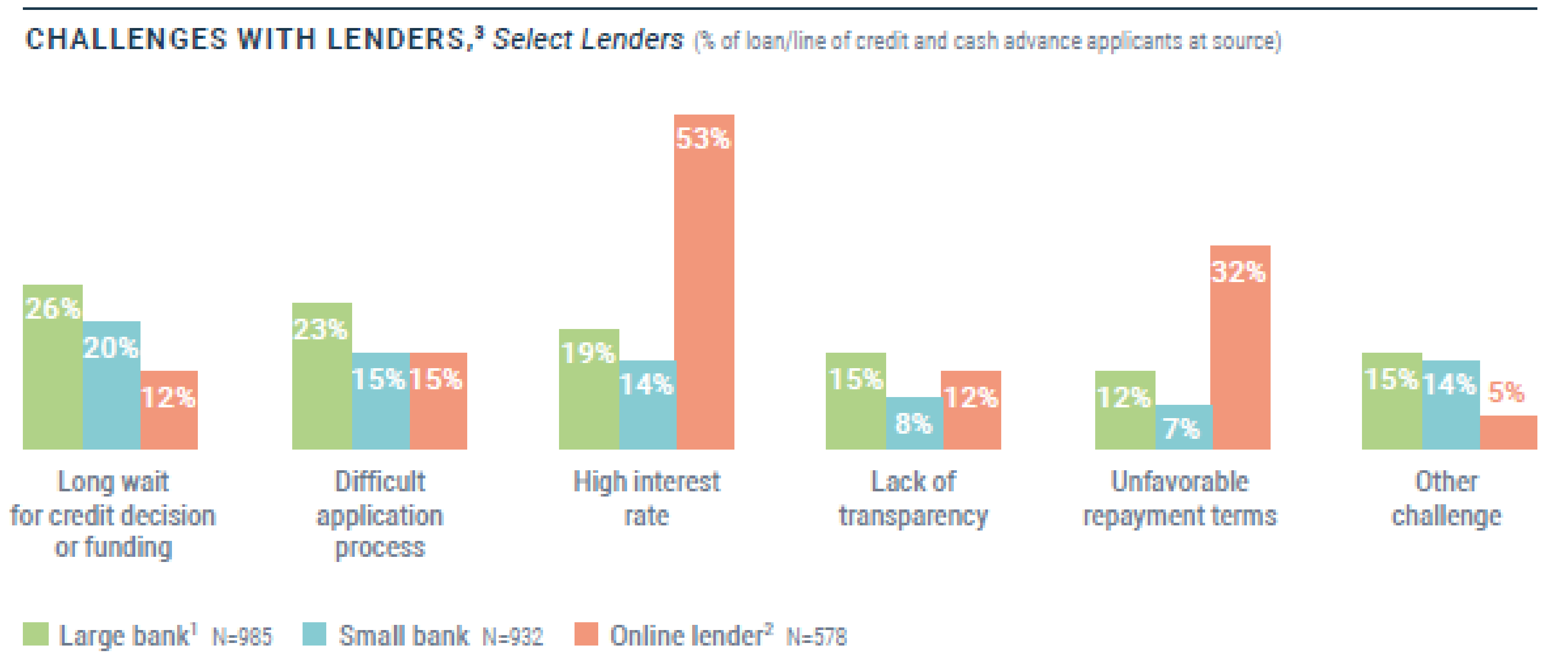
Source	Largest Factor	2nd Largest Factor	3rd Largest Factor
Large bank[3] N=1,011	58%	37%	29%
Small bank N=958	65%	40%	30%
Online lender[4] N=585	63%	61%	45%

Existing relationship with lender · Speed of decision or funding · Chance of being funded · Cost or interest rate · No collateral was required

1 Select lenders shown. See Appendix for more detail.
2 Respondents could select multiple options.
3 Respondents were provided a list of large banks (those with at least $10B in total deposits) operating in their state.
4 'Online lenders' are defined as nonbank lenders including Lending Club, OnDeck, CAN Capital, PayPal Working Capital, Kabbage, etc.

Source: Small Business Credit Survey, Federal Reserve Banks

Bank applicants were most dissatisfied with wait times for credit decisions. Online lender applicants were most dissatisfied with high interest rates.

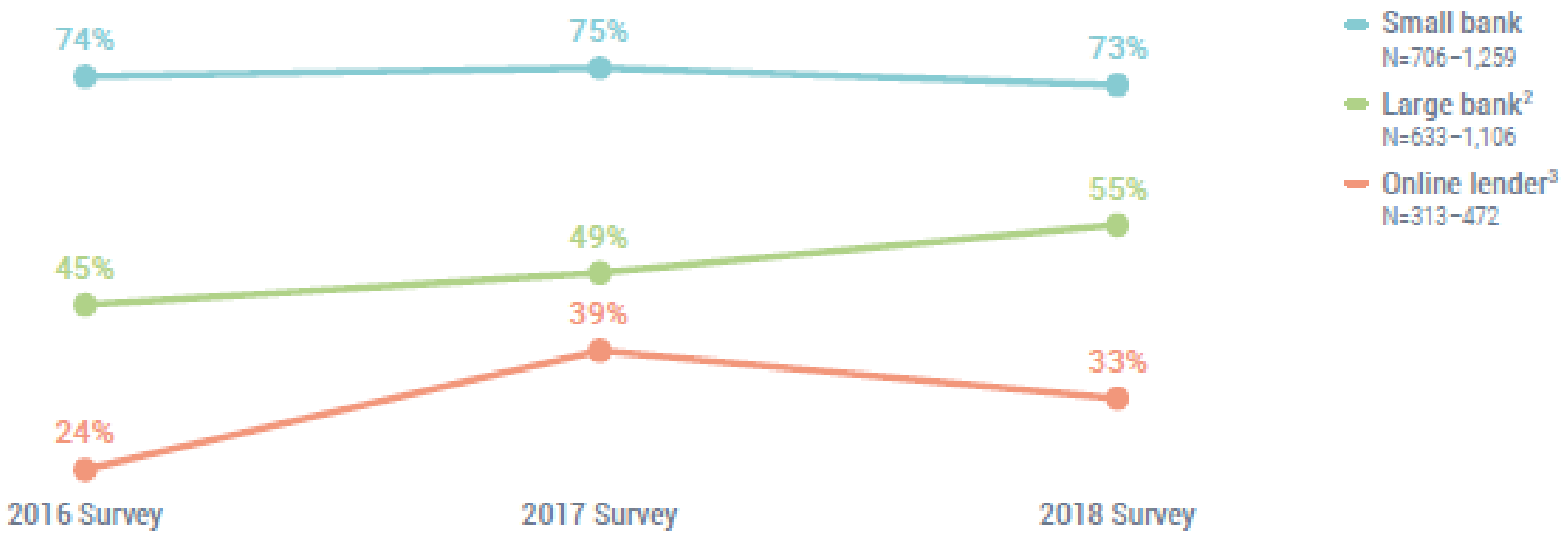


1 Respondents were provided a list of large banks (those with at least $10B in total deposits) operating in their state.
2 'Online lenders' are defined as nonbank lenders including Lending Club, OnDeck, CAN Capital, PayPal Working Capital, Kabbage, etc.
3 Respondents could select multiple options.

Source: Small Business Credit Survey, Federal Reserve Banks

Applicant satisfaction is consistently highest at small banks.

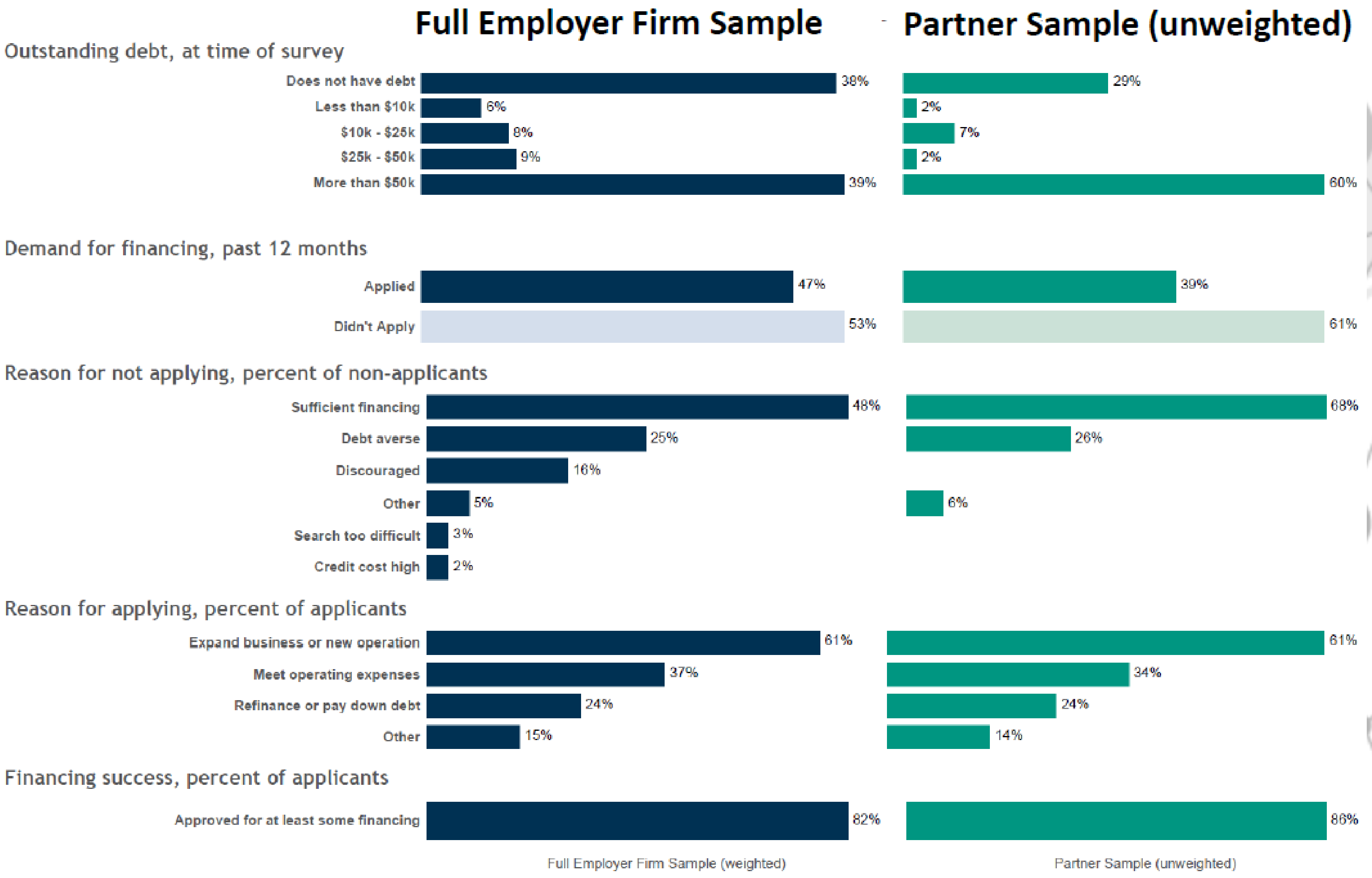
NET SATISFACTION OVER TIME[4,5] (% of approved loan/line of credit and cash advance applicants at source)



1 *Percentages may not sum to 100 due to rounding.*
2 *Respondents were provided a list of large banks (those with at least $10B in total deposits) operating in their state.*
3 *'Online lenders' are defined as nonbank lenders including Lending Club, OnDeck, CAN Capital, PayPal Working Capital, Kabbage, etc.*
4 *Net satisfaction is the share of firms satisfied minus the share of firms dissatisfied.*
5 *Time series values shown here differ from the 2018 report as a result of improvements to the weighting scheme. See Methodology for details.*

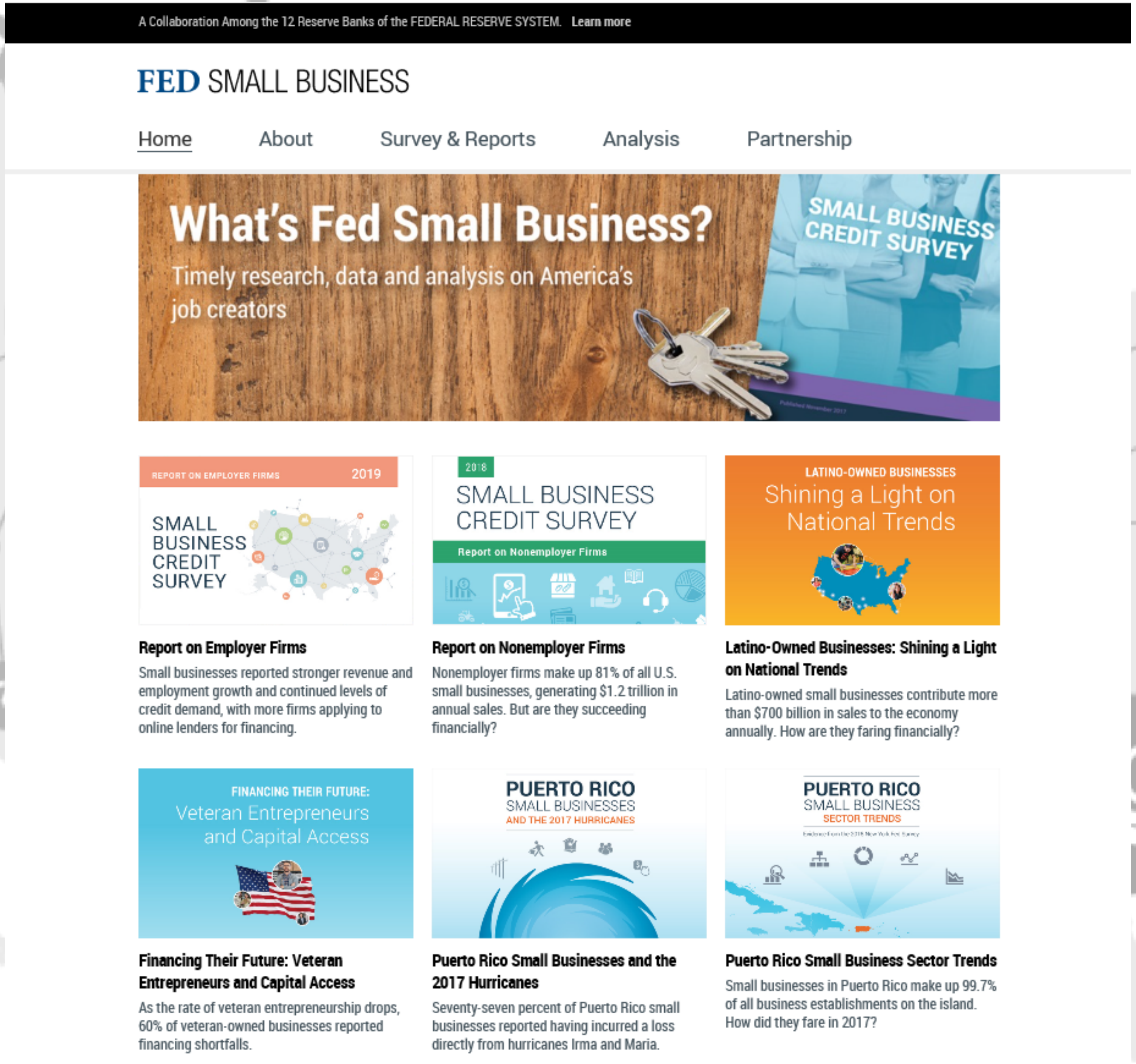
Source: Small Business Credit Survey, Federal Reserve Banks

Distribution Partner Benchmark Report



Source: 2015 Small Business Credit Survey; Federal Reserve Banks of Atlanta, New York, Boston, Cleveland, Philadelphia, Richmond, and St. Louis

Check Out Our Small Business Website: http://www.fedsmallbusiness.org



Next Steps

- Future 2019 report releases:
  - Nonemployer firms
  - Minority-owned firms
  - Firms operating in low- and moderate-income communities
  - Update to "How Do Firms Respond to Hiring Difficulties?" memo
- Data collection for the **2019** round of the Small Business Credit Survey kicks off in September.
- Federal Reserve Bank of Richmond is working to **expand** its survey partner recruitment in 2019.
- Find out more information: https://www.richmondfed.org/community_development/resource_centers/small_business (**Small Business**)

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