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SMALL BUSINESS FINANCING TRENDS
The Past, Present and Future

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Old-fashioned Innovation
The Decline of Small Business Lending

- When did this decline start?

**Figure 2. Small Loan Share of All Nonfarm, Nonresidential Loans**

Source: Federal Deposit Insurance Corporation; authors’ calculations.

From blog – [www.clevelandfed.org](http://www.clevelandfed.org) Economic Commentary, August, 2013
Pre-Great Recession

• What was going on?

  – Decline in the number of small/community banks; between 1985 and 2005, the number of small/community banks was cut in half (From approximately 14,500 to under 7,500 – according to FDIC).

  – 75% of the decline was a result of mergers and acquisitions; the remainder was a result of banks “growing” out of this group and of course, there were failures as well.
The Great Recession
(December, 2007 – July, 2009)

• Lending to Small Businesses

  – Small businesses (historically) depend almost exclusively on bank financing.

  – In response to the recession and regulatory changes, banks increased collateral requirements.

  – As a result of the recession, fewer small businesses exhibited strong cash flow.

  – Banks faced the challenge of sorting through problem credits, handling OREO properties, dealing with increased delinquencies, etc. The number of troubled customers seemed to increase exponentially without warning.
Happy Days Are Here Again?

“Less restrictive standards for commercial and industrial loans led to the increase in lending to small businesses.”
What might the other reasons be?

• Signs of improving economy have motivated more small businesses to expand (buying new equipment, expanding, etc).
• Record low interest rates have encouraged small business owners to “bank shop”; the stronger businesses have benefited the most from the rate environment.
• Small Business Administration (SBA) has aggressively marketed low doc (streamlined) programs to participating lenders.
• A few words on the Secondary Market...
OK... Where are we heading from here?

• The trend of reduced small business lending along with the long term effects of the Great Recession, make it unlikely that small business lending will increase at a dramatic rate in the near future.

• It is likely that the SBA will have to continue to adopt programs that will encourage banks (of all sizes) to lend to small businesses.

• Interest Rate Risk makes the water even murkier...

• Will policy makers be able to find middle ground moving forward that will assist in continued economic recovery?
Questions???

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