

Discussion Session A: Small Business Lending

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Entrepreneurial optimism....

Or pessimism?

- Evidence of credit rationing away from LMI communities. Is CRA doing an adequate job? (Laderman & Reid)
- Optimistic entrepreneurs are associated with higher financial risk. Did over lending occurred when lending was cheap? (Dai & Ivanov)
- Credit availability not main hindrance for small firms. Are policies aimed at small business lending missing the target? (Montoriol-Garriga & Wang)

Laderman and Reid

The Community Reinvestment Act and Small Business
Lending in Low and Moderate-Income Areas during
the Financial Crisis



CRA and Small Business Lending

- Why might there be credit rationing away from LMI communities and African-American residents?
- Why housing booms and increased small business lending?
- Fewer banks: supply or demand?



Why might there be credit rationing away from LMI communities / African Americans?

- Education
- Rent versus own (collateral)
- Optimism (confidence) (Dai & Ivanov)
- Opportunities (demand)
- Economic growth
- Next step: add in some factors that might affect African-American (and LMI resident) credit approval.
 - Get to the source of the issue. Can we make improvements there?



Why housing booms and small business lending?

- Boom: growth
 - Housing booms and new business creation
- Bust: contraction
 - Foreclosures and closing businesses
- Supply and demand
 - Different relationship in good times versus bad?
 - Growth: high demand, ample supply
 - Contraction: low demand, supply unclear
 - Financial system capital shock: high demand, low supply
- Next step: Longer time series with 3+ states

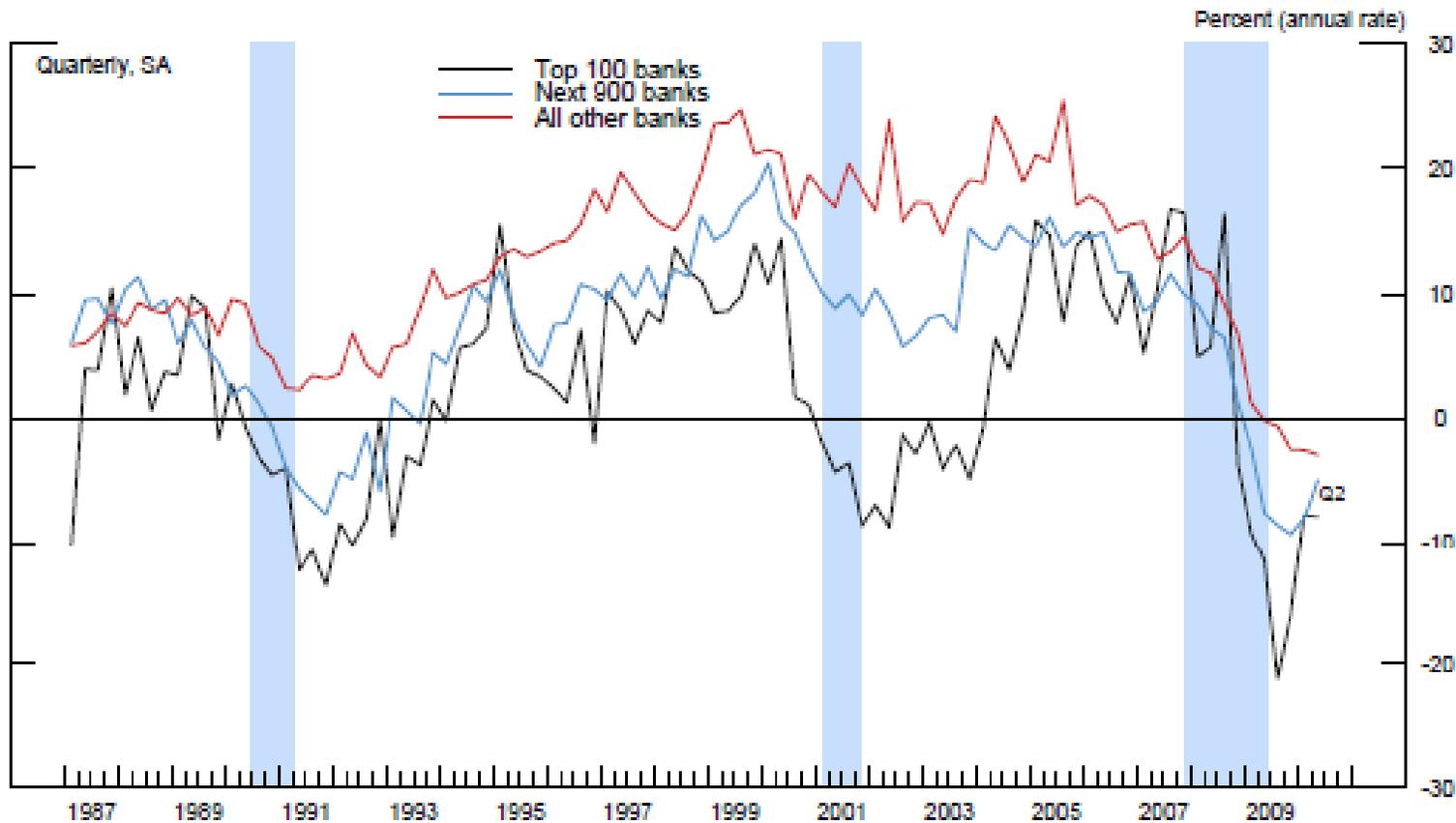


Fewer banks: supply or demand?

- Fewer CRA banks in sample (consolidation)
 - Sample selection issue?
- In this crisis, small banks have stepped in
- Move away from small bank lending to large bank lending – could this crisis have shifted some lending back to small banks?

Smaller banks: higher loan growth

Growth in CRE and C&I loans by bank size, broken out by TINYSEAS



Note: Breakout is defined by asset size.

Dai and Ivanov

Entrepreneurial Optimism, Credit Availability and
Cost of Financing: Evidence from U.S. Small
Businesses



Optimism

- What leads to optimism?
- Why are optimistic firm owners less likely to pay trade credit late?
- How successful are optimists?



What leads to optimism

- Gender, race, education and experience
- Others? Some are measurable, others not
- Is optimism associated with other characteristics that could affect success?
 - Type of business
 - Local business conditions
 - Support (family/friends)
 - Talent
 - Employees (firm size)
 - History of entrepreneurs in family



Why are optimistic firm owners less likely to pay trade credit late?

- Trade credit versus use of other sources of funding
 - Results on trade credit mixed in recent survey years
 - Perhaps more optimistic firm owners pay with other method?



How successful are optimists?

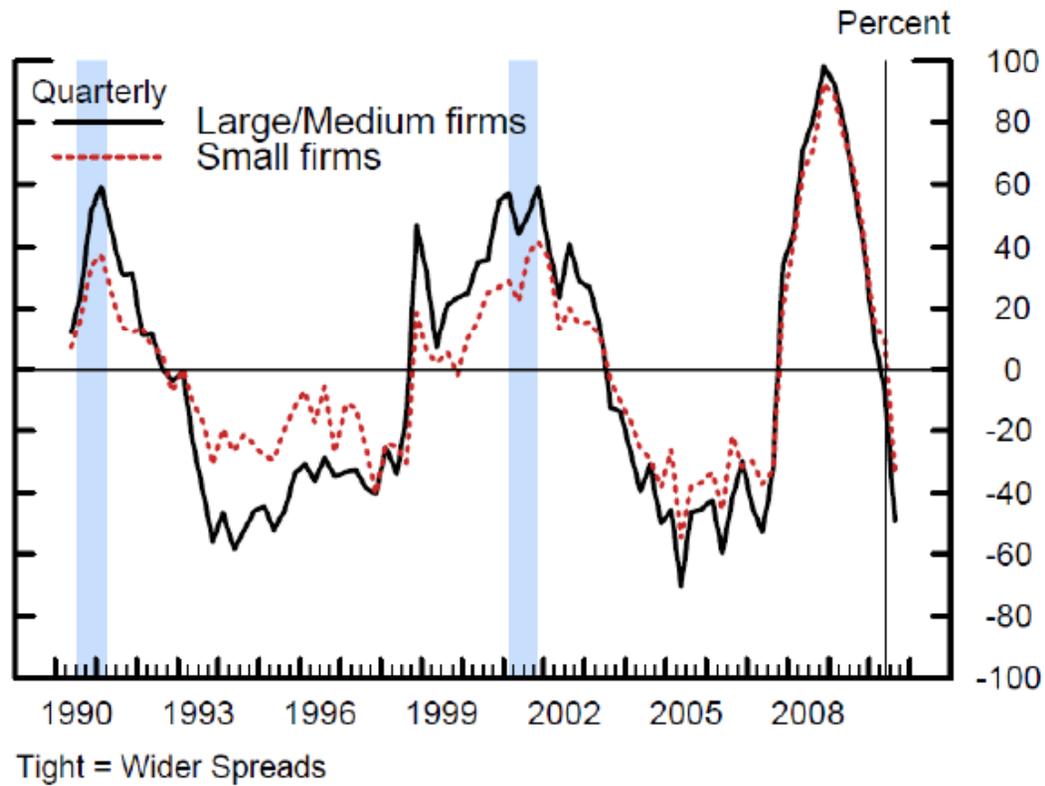
- The real measure of how success: whether a firm is around 5 years from now
- SSBF does not tell us that

Montoriol-Garriga and Wang

Small Business in the Great Recession

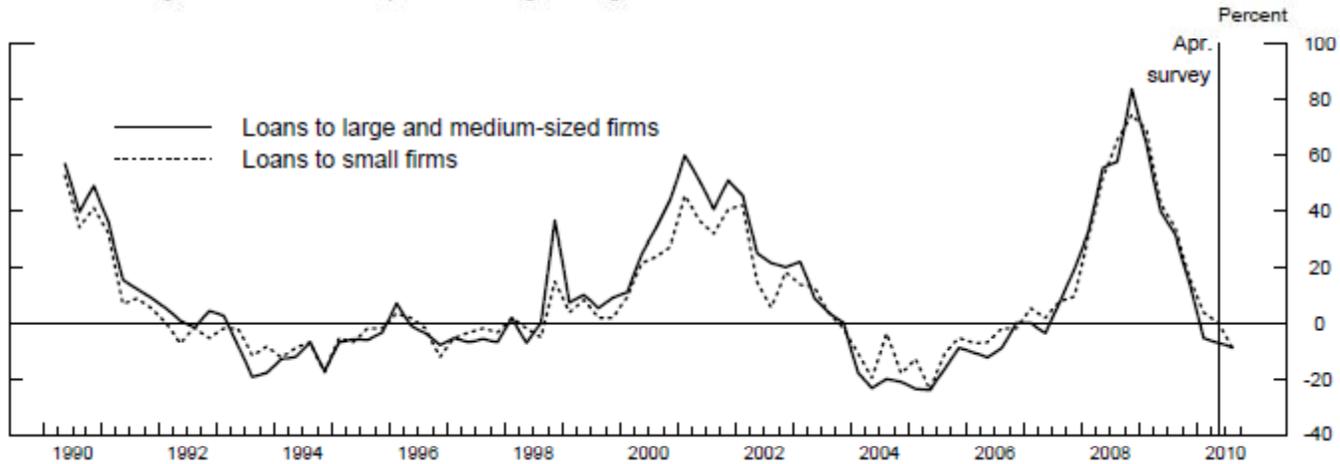
Spreads look similar....

Spreads of Loan Rates Over Cost of Funds

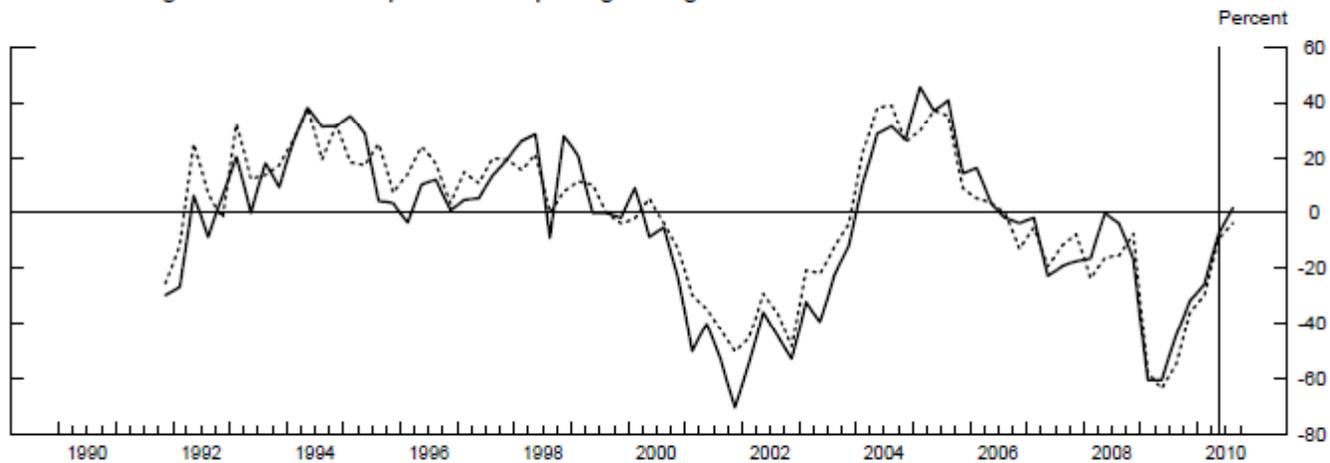


As do standards and demand....

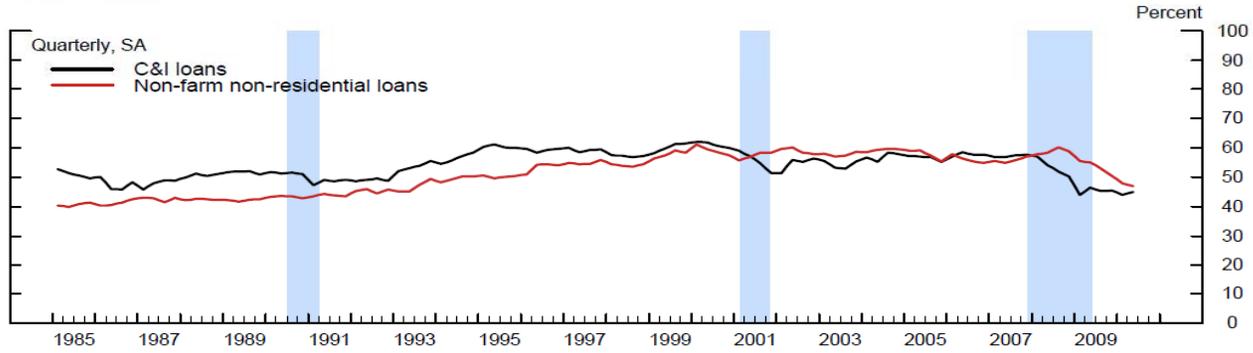
Net Percentage of Domestic Respondents Tightening Standards for Commercial and Industrial Loans



Net Percentage of Domestic Respondents Reporting Stronger Demand for Commercial and Industrial Loans

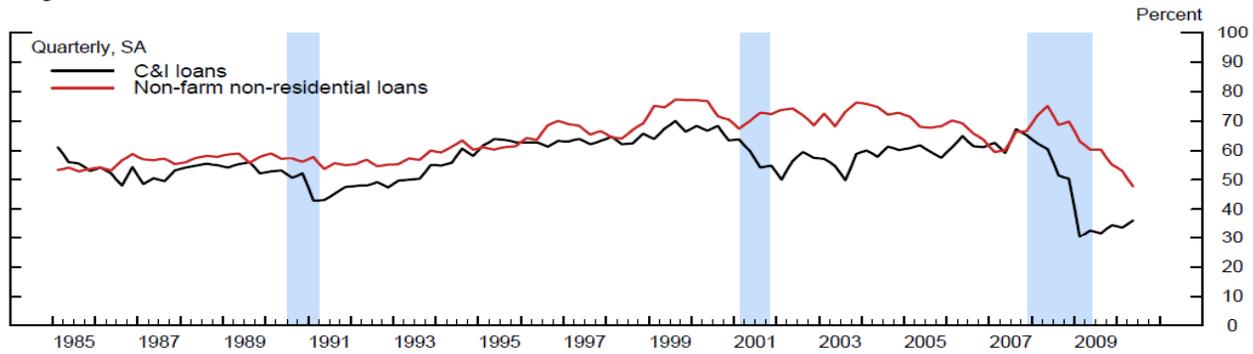


Small Banks



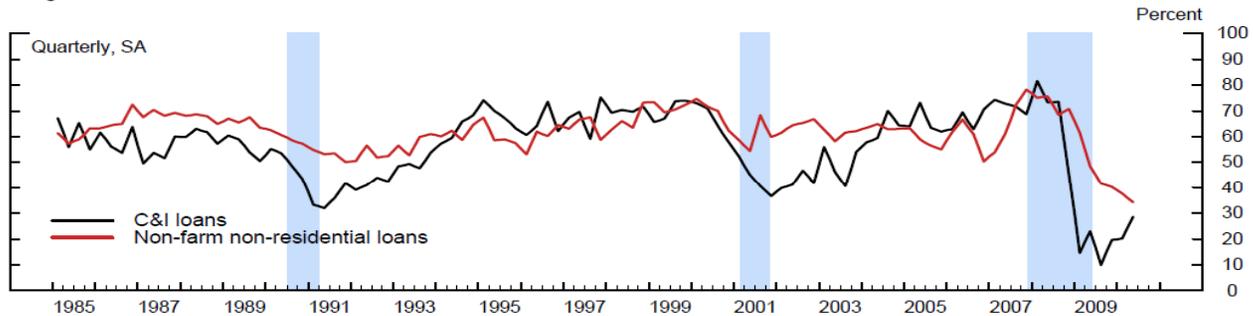
But differences among small, medium and large banks

Regional Banks



...Does this matter in times of crisis?

Large Banks



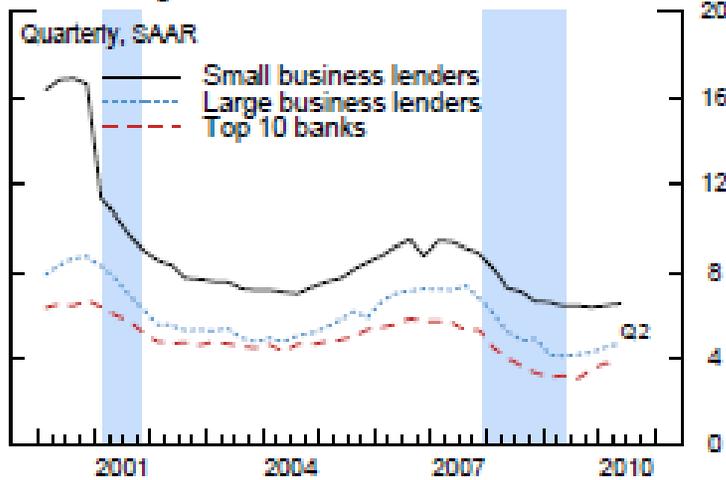


Credit availability not main hindrance for small firms?

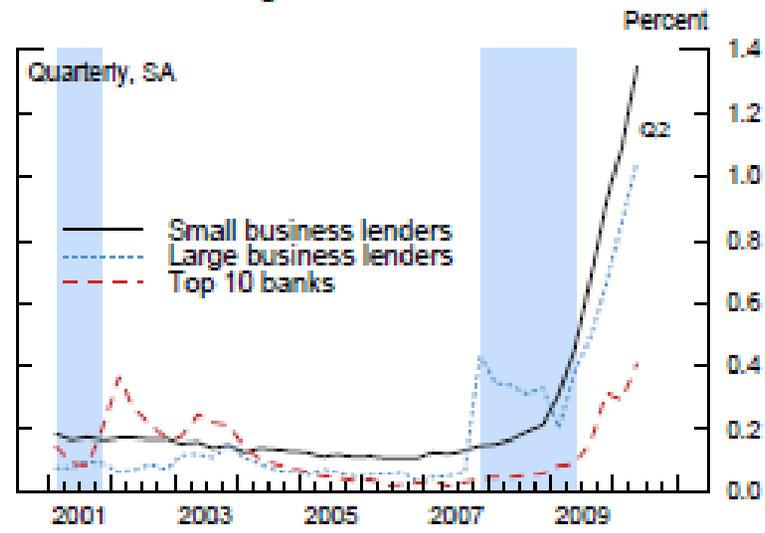
- Market dislocation during the crisis
- Why small firms might need a bit more help
- Caveats on STBL
- ...finally, while small loans carry a higher rate, might that come with some benefits to the firm?

Small loans carry a higher rate, but that might come with some benefits to the business

Ratio of Interest Income on C&I Loans to Outstanding C&I Loans



Loan Restructuring



Note. Restructured business loans / total business loans.
These data are available as of 2001 Q1.