SBA: The Backbone That is Driving US Small Businesses

Overview

American attorney and author Elizabeth Edwards once said, "*She stood in the storm, and when the wind did not blow her way, she adjusted her sails*." Her message points to survival instinct, a quality aptly demonstrated by American small businesses over the last two decades. These firms have shown unfathomable fortitude and deep resilience while navigating systemic crises. Full recovery takes time, and in this phase, like iconic American artist Ginger Rogers, who consistently managed to control and balance fast footwork with the same step speed as her illustrious dancing partner Fred Astaire, the Small Business Administration (SBA) has been a trusted partner standing firm behind small businesses and keeping them afloat in challenging times.

The SBA's history dates to the Great Depression of the 1930s when concerns about the devastating effects of a stock market crash on a war-ravaged economy were paramount. US banks suffered catastrophic losses, resulting in severe liquidity shortages nationwide. Among the hardest hit were small business lending markets, which essentially froze and starved the whole small business ecosystem for liquidity. Small businesses, which were important for the economy, became severely undercapitalized. After several decades of efforts by policymakers, the US government formally passed the Small Business Act in 1953 and authorized the SBA to manage and address the concerns of small businesses. The act specifies that the SBA's mission is to promote the interests of small businesses in the private marketplace. Since then, the SBA has played a crucial role in the US economy while guaranteeing billions of dollars to small businesses each year. The SBA currently has several types of lending programs, including loan guaranty, to increase small businesses' access to capital.

The Small Business **Act of 1953** is the declared policy of the US government to help and protect the interests of small businesses.

What is a Small Business?

The definition varies by size and industry. The SBA (interim rule) defines small businesses as those that do not have more than USD 15 million in tangible net worth and USD 5 million in average net income after federal taxes (excluding any carryover losses) for the two full fiscal years before the date of the application[1].

Small Businesses – Change Drivers

33.2 million small businesses in the US

97.3% of exporters (= 264,366 businesses)

In the US, 99.9% of all enterprises are small businesses

Small Business Lending Market

Approximately **USD 1.4 trillion** in 2020[3]

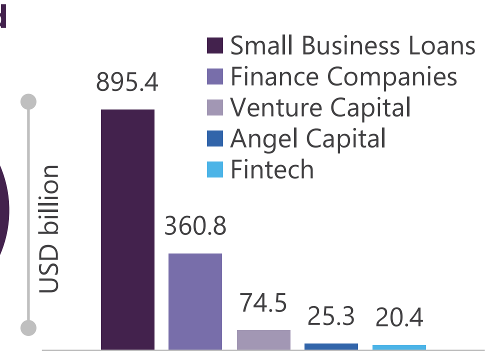
As per a March 2023 report, small businesses in the US accounted for[2]....

43.5% of GDP

62.7% of net new job creation since 1995

46.4% of private sector employees (= 61.7 million)

39.4% of the private sector payroll (= USD 2.9 trillion)



Source: [1]Small business act 1958 (*Enacted August 5, 2022)*; [2] www.advocacy.sba.gov, what's new with small business;[3] www.fdic.gov

Need for SBA Loans in US

Small businesses are the engines of economic growth in the US, accounting for ~43.5% of the country's GDP. The country had 33.2 million small businesses in 2022, making up 99.9% of all US businesses. These small businesses employed ~61.7 million Americans, i.e., ~46.8% of the total US private sector workforce[4], making their survival critical for the economy. Therefore, by building better small business lending ecosystems, SBA helps improve the overall resilience and long-term prospects of the US economy.

What Makes Small Businesses Financially Vulnerable?

- Any drastic changes in business dynamics impact small businesses disproportionably.
- Since the beginning of the COVID-19 pandemic, millions of small businesses have been pushed to the brink of closure, with their financial distress underscoring the underlying financial fragility. Most small businesses operate with slim profit margins, and any disruptions in cash flows can seriously affect their financial viability.
- Their balance sheets lack financial flexibility. Most of their finances go toward maintaining the required inventories. It not only pressurizes their cash-conversion cycle but also increases their cost of servicing debt.
- Due to their small scale and limited financial track record, these players have low bargaining power. Therefore, they tend to rely heavily on financial support from the government for their working capital needs.

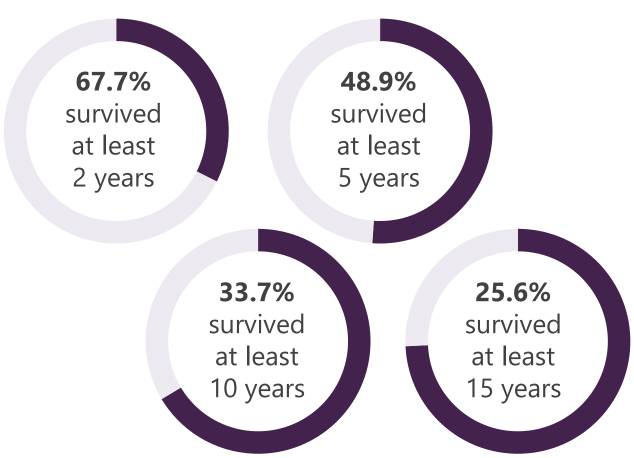
Why are SBA Loan Assistance Programs Important for Small Businesses?

- In the US, small businesses have considerable unmet credit needs as lenders scarcely offer the right lending solutions to them. These businesses often lack sufficient collateral to pledge and require long loan repayment periods. This is why they suffer from high rates of loan rejection by lenders.
- Availability of short-term liquidity is vital for small businesses, and addressing near-term cash management and improving financial resiliency is crucial for their survival. Immediate access to short-term financing, subsidized loans, relief or grants, and expert assistance can enhance their financial health.
- Therefore, the SBA has developed a strong framework to address specific issues of small-business lending in the US. It plays a critical role in making bank loans accessible to small businesses that lack business credit history or track records of their revenue generation.

Small Business Survival Rates[5]

Small businesses face a huge set of challenges, which often leads to a high rate of failure. They have difficulty in obtaining bank loans as credit needs and borrowing sources differ widely within the sector. They also lack expertise to compete in the market or resources to expand strategically and grow their revenues.

According to US government data, average survival rates for small businesses during 1994–2020 were as follows



Sources of Small Business Funding[6]

Financing comes from either internal sources (family, friends, or personal savings) or external sources (bank loans).

In 2019, prior to the pandemic, around **77%** of small businesses used business earnings as their primary source of funding.

In 2020, during the pandemic, **73%** of small single-location employer firms received financial assistance from the **SBA Paycheck Protection Program (PPP).**

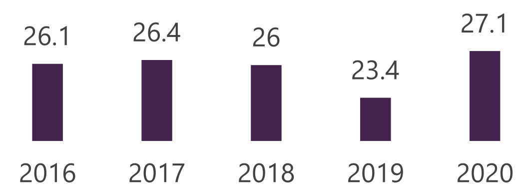
Source: [4] https: / / cdn.advocacy.sba.gov, [5&6] Small Business Finance, FAQ, sba.gov

SBA Loans – Market Size and Supply and Demand Dynamics

- The US small business credit market stood at ~ USD 1.4 trillion.
- Small business loans (SBLs), i.e., loans of USD 1 million or less, are a crucial component of the lending portfolios of the majority of US banks. These loans contribute significantly to the banks' portfolio of commercial and industrial (C&I) loans.
- Lenders of all sizes are important providers of SBLs. Banks provide approximately 44% of small business financing, significantly higher than online lenders (22%) and credit unions (6%)[1].
- In the US, non-community banks provide a larger proportion of overall small business loans than community banks; however, community banks tend to lend primarily to small businesses. In 2020, community banks had a share of 25.6% of SBLs, while non-community banks had a share of 74.4% in 2020[2].
- The demand for SBLs grew significantly during 2017–2020. Total SBLs amounted to USD 895 billion in 2020, a jump of 38.9% compared with 2019. The main contributor was the PPP, which was meant to stabilize US small businesses. However, the PPP was closed in May 2021.
- Lenders with total asset sizes of USD 1–10 billion were the most active during the pandemic, recording the highest jump (65.8%) in the value of SBLs outstanding during 2019–2020.

Trends in SBLs

Volume of SBLs (Million)



Share of SBLs in Total Business Loans

	2019	2020
Total Business Loans (USD trillion)	3.4	3.9
Share of SBLs (%)	18.9%	22.7%

SBA Helped Restore Credit Flow to Small Businesses and Stabilize US Economy

SBLs Outstanding by Loan Category (USD billion)

	2017	2018	2019	2020
Total SBLs	618.9	632.5	644.5	895.2
C&I Total SBLs	337.0	352.8	368.1	625.2
CRE Total SBLs	281.8	279.6	276.4	270.0

SBLs Outstanding by Loan Size (USD billion)

	2017	2018	2019	2020
<0.10	10.4	10.0	8.5	7.4
0.10–0.49	90.5	86.4	82.2	87.4
0.5–0.99	55.6	54.0	51.9	70.7
1.00–9.90	133.0	127.0	129.9	215.4
10.00–49.90	85.6	106.9	114.5	162.0
>50.00	243.7	248.2	257.4	352.4

Source: [1&2]FDIC, Office of Advocacy, U.S. Small Business Administration, Recent Developments in the Small Business Credit Market, July 2022. Note: C&I – commerce and industry; CRE – commercial real estate

Building Blocks of SBA Lending Model

- To support the ecosystem of small businesses, SBA administers an umbrella of lending programs by using three building blocks – a well-designed lending process, a wide range of loan programs to create resilient businesses, and a sound governance model to track, monitor, and report lending performance.
- The SBA lending model broadly covers disaster assistance *(to address economic damage)*, business loan credit subsidies *(including loan forgiveness and debt relief payments)*, and all other programs *(for immediate help to small businesses)*.

Strategic Objectives of SBA (2022–2026[1])

- Support small businesses and innovative startups through equitable and customer-centric design and delivery of loan programs
- Develop and build resilient businesses and a sustainable economy
- Implement robust stewardship of resources for an effective impact

SBA Programs Cover Financial and Other Needs of Small Businesses[2]

Capital Access Programs	7(a) Loan Guaranty 504 / CDC Loan Guaranty	Microloan Program Paycheck Protection Program	International Trade and Export Promotion Programs *(Export Express loan, Export Working Capital loan, and International Trade loan)*
Disaster Loans Programs	Disaster Loans to Businesses and Nonprofit Organizations Disaster Loans to Homeowners, Renters, and Personal Property Owners	Personal Property Loans Real Property Loans Physical Disaster Loan	Economic Injury Disaster Loans COVID-19 Economic Injury Disaster Loan and Grant Programs
Contracting Programs	Prime Contracting Programs Sub-Contracting for Small Disadvantaged Businesses	The 7(j) Management and Technical Assistance Program	Surety Bond Guarantee Program Goaling Program, Office of Small and Disadvantage businesses
Capital Investment Programs	The Small Business Investment Company Program	Small Business Innovation Research Program	Small Business Technology Transfer Programs Growth Accelerators Initiative
Other Programs	Regional and District Offices, Office of Inspector General, and Restaurant Revitalization Fund	Executive Direction Programs, The National Women's Business Council, The Office of Ombudsman, and Faith-Based Initiatives	

Key Features of Major SBA Lending Products[3]

7(a) Loan Guaranty	**Maximum Loan Amount:** USD 5 million **Maturity:** 5–7 years for working capital, up to 25 years for equipment and real estate, and up to 10 years for all other loans **Use of Proceeds:** Fixed assets, working capital, financing of startups, or purchasing an existing business
Microloan Program	**Maximum Loan Amount:** USD 50,000 **Maturity:** Up to 7 years **Use of Proceeds:** Working capital and acquiring materials, supplies, furniture, fixtures, and equipment.
504 / CDC Loan Guaranty	**Maximum Loan Amount:** Maximum 504 / CDC loan participation in a single project is USD 5 million and USD 5.5 million for manufacturers and specified energy-related projects, and the minimum is USD 25,000 **Maturity:** 10 years for equipment and 20–25 years for real estate; unguaranteed financing has a short term **Use of Proceeds:** Fixed assets only, i.e., no working capital
SBIC	**Maximum Leverage Amount:** An SBIC* can apply for up to 300% of its private capital requirements; however, it typically gets approval for up to 200%. The maximum permitted funding is USD 175 million per SBIC and USD 350 million for two or more SBICs together. **Maturity:** SBA-guaranteed debenture participation certificates can have a term of up to 15 years. **Use of Proceeds:** To purchase small business equity securities, make loans, and purchase debt securities from small businesses
Paycheck Protection Program	**Maximum Leverage Amount:** The lesser of (1) USD10 million or (2) 2.5 times the average total monthly payments by the applicant for payroll costs incurred during the one-year period before the date on which the loan is made plus the outstanding balance of any 7(a) loan (made on or after January 31, 2020) that is refinanced into the PPP loan **Maturity:** Maximum 10 years; the act also provides for loan deferment and forgiveness under specified conditions

Source: [1]FY 2022-2026 Strategic Plan for Publication, www.sba.gov; [2&3]Small Business Administration: A Primer on Programs and Funding, March 2022;; Note: *SBIC – Small Business Investment Company, CDC – Certified Development Company

Most Active Banks in SBA Lending Ecosystem

- In US, the major providers of SBLs include commercial banks, savings institutions, credit unions, and finance companies.
- The leading small business lenders typically include large banks. The top 10 most active originators of SBA loans based on the average loan size are Live Oak Bank, Newtek, Huntington, Celtic, Byline, Readycap, Wells Fargo, BayFirst National Bank, KeyBank, and Cadence**.** These banks use their nationwide footprints to help small businesses at every stage of the SBA loan journey. They are actively engaged in all SBA lending programs, including SBA 7(a) and 504 programs.
- In the US, SBA 7(a) loan is the largest and the most common type of SBA financing. There are over 1,600 SBA-certified lenders engaged in offering 7(a) lending solutions to small businesses. These loans are used for working capital, refinancing debt, expanding to another location, and purchasing real estate or equipment.
- The other common SBA loan type is the 504 loan, which helps businesses to expand through land or building acquisition, construction, or equipment purchase. Under the 504 loan structure, CDCs typically provide 40% of the loan and banks up to 50%. There are around 192 SBA-approved financial institutions in the US for 504 loans.
- In fiscal 2022, the approved SBA loan amount under the 7(a) and 504 loan programs was USD25.7 billion and USD9.2 billion, respectively.

Top SBA Lenders in US in 7(a) Loans, 2022[1]

Rank[2]	Loan Count	Loan Approval (USD million)	Average Loan Size (USD '000)	Leading SBA Lenders
1	1,157	1,696	1,466	Live Oak Banking Company
2	1,677	1,013	604	Newtek Small Business Finance
3	5,675	998	176	The Huntington National Bank
4	707	646	914	Celtic Bank
5	350	422	1,207	Byline Bank
6	807	409	506	Readycap Lending
7	1,933	396	205	Wells Fargo Bank
8	974	328	337	BayFirst National Bank
9	803	314	391	KeyBank National Association
10	906	301	333	Cadence Bank

Source: www.sba.gov

Outlook

The 33-million-strong, vibrant small business sector has become the driving force of the US economy. With an emphatic contribution to the world's largest GDP, small businesses can induce a multiplier effect across the trillion-dollar US economy. However, with heavy losses sustained during the global pandemic, the ability of small businesses to access lending continues to be one of the most pressing policy issues in the US. The SBA has outlined its strategy and developed a vast array of programs to solve capital access gaps, and lenders should also play an active role in exploring and identifying ways to help underserved small businesses.

Evalueserve's SBA lending services help the world's leading SBA lenders to make faster and better underwriting decisions

How Evalueserve Helps SBA Lending Clients

We support SBA lenders in portfolio management and new loan underwriting. Our services have created efficiencies for relationship managers and credit managers and enabled them to focus on client management and new business origination.

Our Services for SBA Lending Clients

- New money underwriting
- Guarantor financial spreading (PFS, PTR, CBR)
- Financial statement spreading (actual and projection)
- Annual reviews
- Demographic analysis
- Loan sheet update
- Debt service summary analysis
- Sensitivity analysis

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