

Third-Quarter Small Business Survey

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Small Business Survey highlights

Small businesses¹ in the construction and real estate industries are still experiencing difficulty obtaining the credit they need. They continue to submit more applications on average than do businesses in other industries but receive less credit overall. Several small business owners in construction and real estate noted that banks report an inability to fulfill their requests because the banks are responding to pressure by bank regulators not to take on any more loans related to spec housing, land, or development.

Small businesses seem to be experiencing more success obtaining credit through community and regional banks, with these banks approving more credit applications than large national banks. Repeat firms in the survey reported higher success rates at community and regional banks in the third quarter.

Young businesses (those less than four years old) tried slightly harder on average to obtain credit but were not less successful at obtaining credit than the sample as a whole. They did not favor community and regional banks over large national banks but, like the sample as a whole, were more successful at these banks.

Of the surveyed firms seeking credit, 66 percent had their financing needs met mostly or in full while 17 percent received no credit at all from their applications. Firms on average applied through 3.6 channels, and many requests did not end with credit fulfillment. Lenders denied 13 percent of the reported credit applications, while requesters refused one-third of credit offer responses because of unattractive credit terms. Half of the firms indicated that tight lending practices were an obstacle to credit, and several noted in comments sections that higher interest rates made it difficult for them to borrow.

Among the 237 firms that completed both the second - and third-quarter surveys, the net percent of firms anticipating increases (net of those anticipating decreases) to capital expenditures, sales, and number of employees inched up in the third quarter.

The number of discouraged borrowers declined in the third quarter, as measured by the percent of firms that did not borrow **only** because they anticipated denial or expected unfavorable credit terms. The decline was especially prominent among firms **not** in the construction or real estate industries. The percent of discouraged borrowers also declined among the 237 repeat firms in the survey.

Firms that have historically relied on personal credit (credit cards or home equity line of credit) were much more likely to receive no financing. The effect was compounded when also limited to firms that relied more heavily on credit to conduct business operations.

¹ We define small businesses as those with fewer than 500 employees.

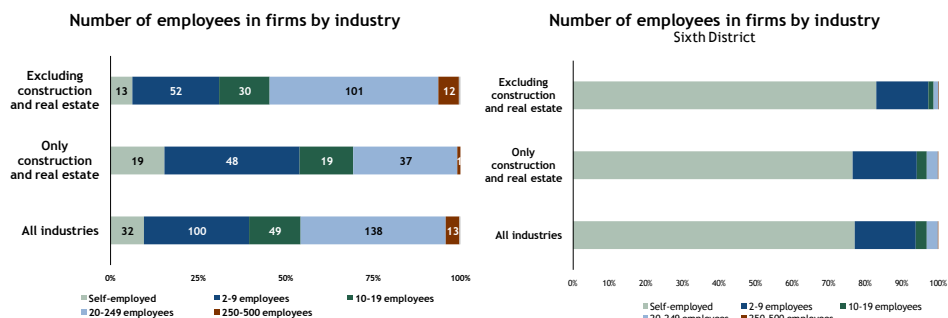
Description of survey sample

Comparison to the Sixth District

The Atlanta Fed conducted the third-quarter survey of small businesses online in October 2010. The Bank distributed the survey through its REIN network, a network consisting of mostly mature businesses more than 10 years old, all conducting operations in Florida, Georgia, Tennessee, Alabama, Mississippi, or Louisiana. There were 336 responses, 237 of which also completed the survey in the second quarter. The differences between the Sixth District and the survey sample are noted here.

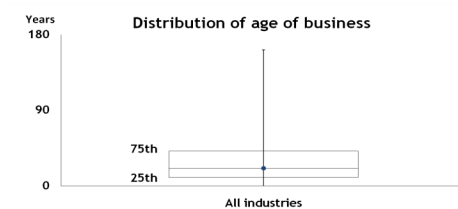
Number of employees

Approximately 10 percent of the survey sample report being self-employed. Three-quarters of small firms in the Sixth District are self-employed.



Age of business

The median firm in the survey sample is 21 years old, and half are between 11 and 41 years old.



Industry distribution

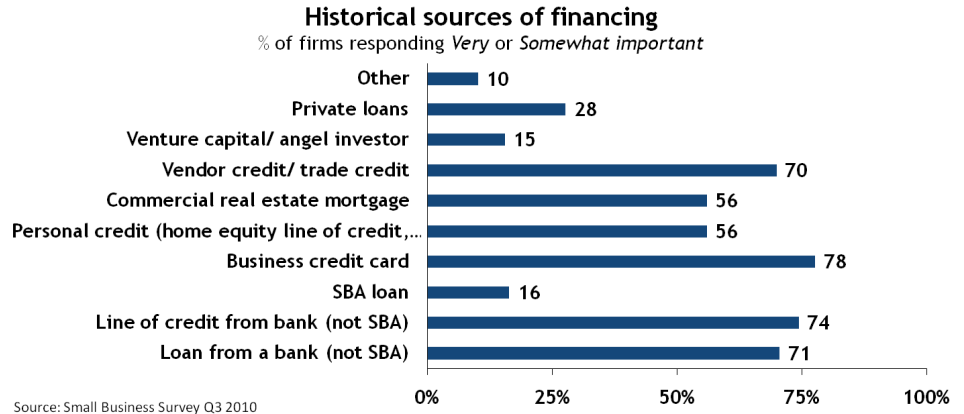
The distribution of survey participants across industries is not that unlike the makeup of industries in the Sixth District. There are two notable sectors where the survey is overweighted and one sector that is underweighted. The survey is overweighted with real estate and manufacturing firms and underweighted by the health care and social assistance industry.

Sector	Sixth District	Survey sample
Other	14	3
Construction	13	15
Professional, scientific, and technology	12	15
Real estate and rental/leasing	10	23
Administrative/support and waste management/remediation services	9	3
Health care or social assistance	8	1
Retail trade	8	7
Transportation and warehousing	5	1
Finance and insurance	4	5
Accommodation and food services trade	3	3
Arts, entertainment, and recreation	3	1
Wholesale trade	3	6
Educational services	2	1
Manufacturing	2	13
Agriculture, forestry, fishing and hunting	1	1
Information	1	2
Management of companies and enterprises	0	0
Mining	0	0
Utilities	0	0

Historical factors in financing

Historical sources of financing

Three-quarters of small businesses surveyed indicated that they have historically relied on loans or lines of credit from a bank. Business credit card and vendor or trade credit are also common sources of financing. Only 16 percent of firms indicated Small Business Administration loans as very or somewhat important for financing their business.



Importance of personal credit and lack of financing

Firms that considered personal credit to be historically very important for financing were more likely to receive no credit over all their applications: 27 percent, compared to 8 percent of firms that said personal credit was somewhat or not important.

Credit availability

Financing uses

When asked to rank the affect of credit availability on business decisions, firms on average said it most affected their decision to diversify business operations and least affected their decision to increase inventories.

Dependence on credit for hiring

108 firms, or about one-third, indicated that credit availability substantially (4 or 5 on the scale of 1 to 5) affects their decision to hire or rehire employees.

Surprisingly, the firms that relied heavily on credit to hire employees were not predominately startups. The average firm age was 22, with half between 6 and 25 years old.

Firms that heavily rely on credit to hire employees and that have historically relied on personal credit had an especially difficult time obtaining credit. These 53 firms were much more likely to reject credit offered due to unfavorable credit terms, and 39 percent of the firms seeking credit received none of the credit requested over all their applications. They were much likelier to cite tighter lending practices as an obstacle to credit and to be a discouraged borrower.

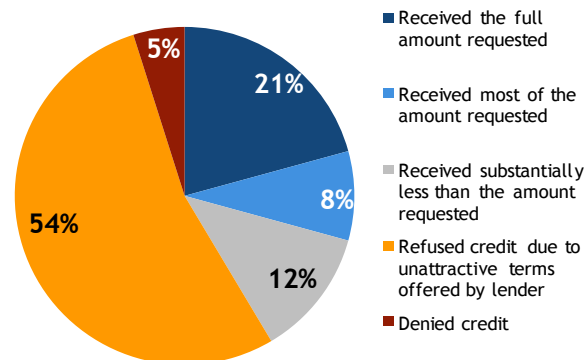
In general, how much does credit availability affect your decisions to...?

On a scale of 1 to 5



Extent to which financing needs were met

Firms that historically relied on personal credit and rely heavily on financing to hire employees—
% of all applications

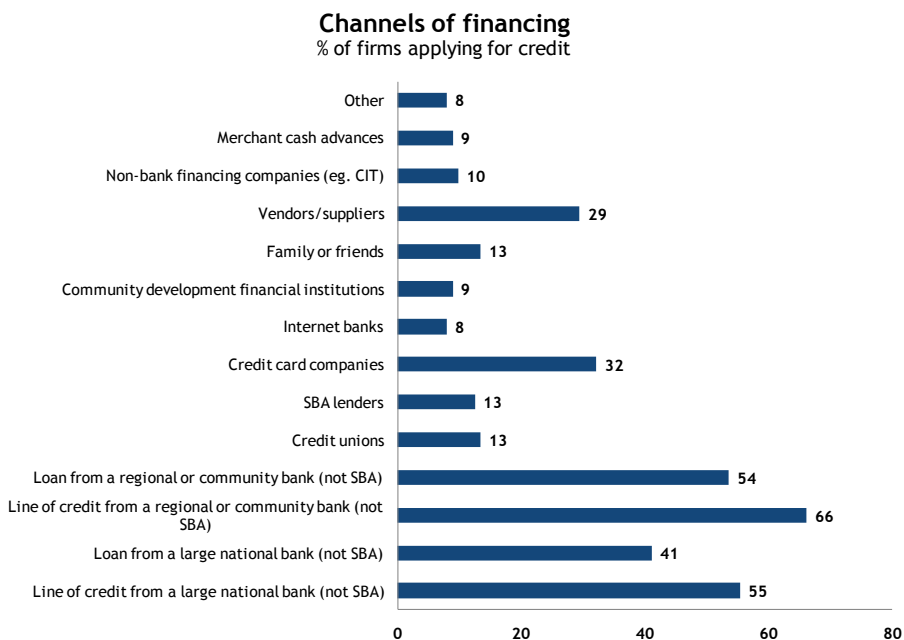


Overall applications and financing success

Channels of financing

One-third of firms sought credit in the previous three months through an average of 3.6 channels. Echoing the types of financing used historically, the most used channels of financing in the previous three months were large national banks, regional and community banks, credit card companies, and vendors/suppliers.

Banks were the most tapped source of financing by far: 93 percent of applying firms sought a line of credit or a loan from a bank. Of these, 29 percent applied exclusively at a community or regional bank, 16 percent applied exclusively at a large national bank, and the remaining 55 percent applied at both.

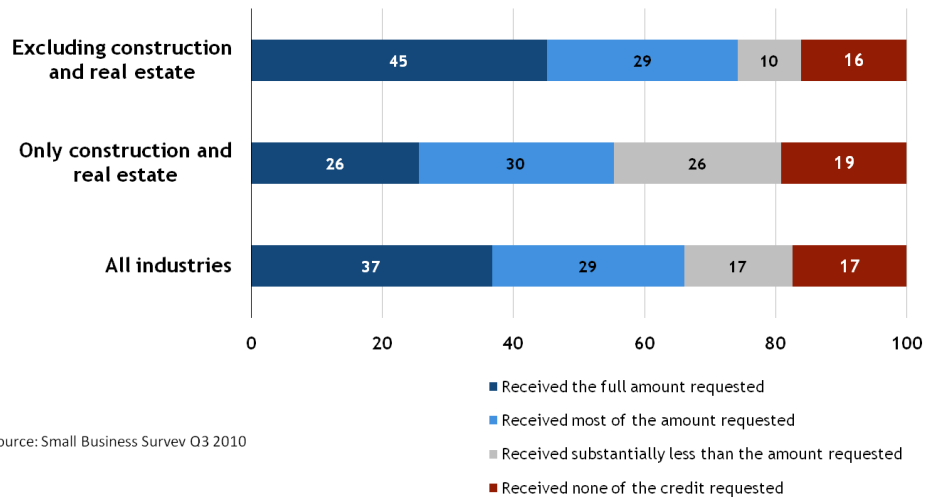


Sources of financing

Success of applications

45 percent of applications were denied or were ultimately refused by the borrower due to high interest rates or other less-favorable credit terms. Despite such a large percentage of *applications* ending with either denial or refusal, only 17 percent of applying *firms* indicated that across all their credit applications they received none of the credit requested. Moreover, 66 percent of all firms indicated that over all their applications, their financing needs were met mostly or in full. However, firms in the construction and real estate industries tended to fare worse when applying for credit; only 56 percent of these companies had their financing needs met mostly or in full.

Extent to which overall financing needs were met
% of firms



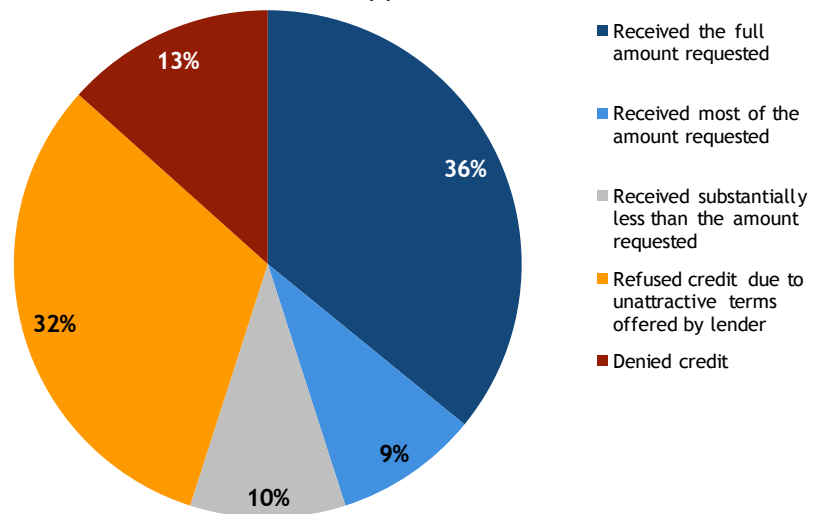
Change from Q2

The overall financing needs of small businesses improved by some measures in Q3: the percent of firms that received all or most of the credit requested increased by 6 percent for all firms, by 5 percent for firms in the real estate or construction industry, and by 10 percent for firms in all other industries. However, among the 58 firms that applied in both the second and third quarters, the distribution of financing received was essentially unchanged.

Firms that obtained no credit

Of all firms that applied for credit, 19 (17 percent) indicated they obtained none of the credit requested. Still, 11 of these 19 anticipate applying again in the next six months while six of the 19 indicate they are discouraged from reapplying due only to either unfavorable credit terms or expected denial. Most of these firms (89 percent) cite tighter lending standards as an obstacle to credit; on average, they are slightly younger than the sample as a whole (15 versus 21 years). The channels used were not unlike the sample, with banks being used most frequently. However, many historical types of financing were cited more often among this group, and, on average, the group put more weight on credit availability than the rest of the sample put on their decision to hire employees.

Extent to which financing needs were met—
% of *all* applications



Approval rates across financing channels

Applications at community and regional banks

Nearly all (93 percent) of the firms that sought credit applied for a loan or line of credit from a bank. Regional and community banks were more popular than large national banks, receiving about 25 percent more applications.

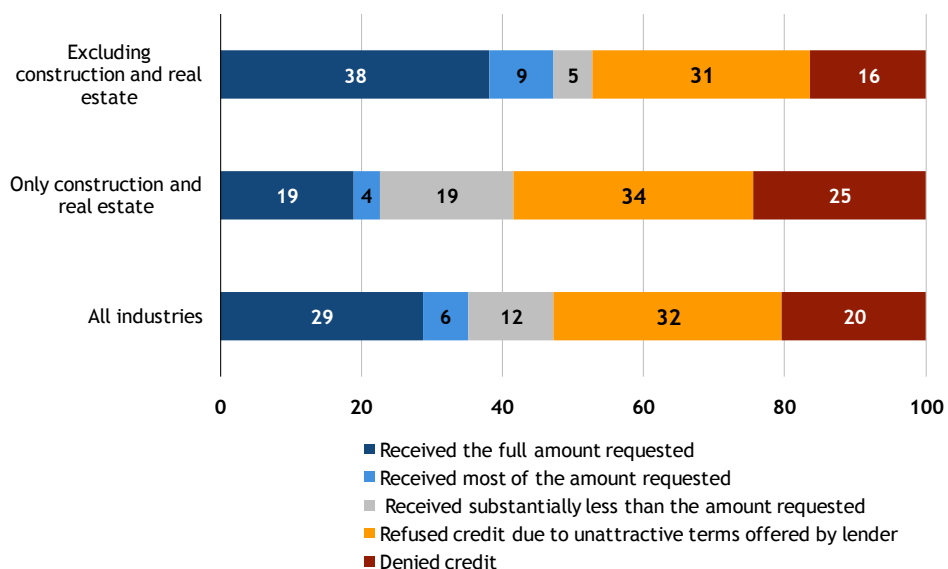
Regional and community banks also denied far fewer applications than did large national banks. The large banks denied 20 percent of applications; community and regional banks denied only 4 percent. The difference is especially pronounced for construction and real estate firms. Only 23 percent of applications by construction and real estate firms were met with full or most of the amount requested at large national banks, compared to more than twice that amount at community and regional banks.

The higher success of credit applications at community and regional banks is also true among firms applying to both types of banks for the same type of credit. For example, 37 percent of firms that were denied or refused a loan from a large national bank received a loan from a community or regional bank, but only 7 percent of firms that were denied or refused a loan from a community or regional bank were successful at a large national bank. A similar result was found when looking at firms that applied for lines of credit at both types of banks. These findings suggests lower credit standards or more willingness to lend to small businesses at community and regional banks.

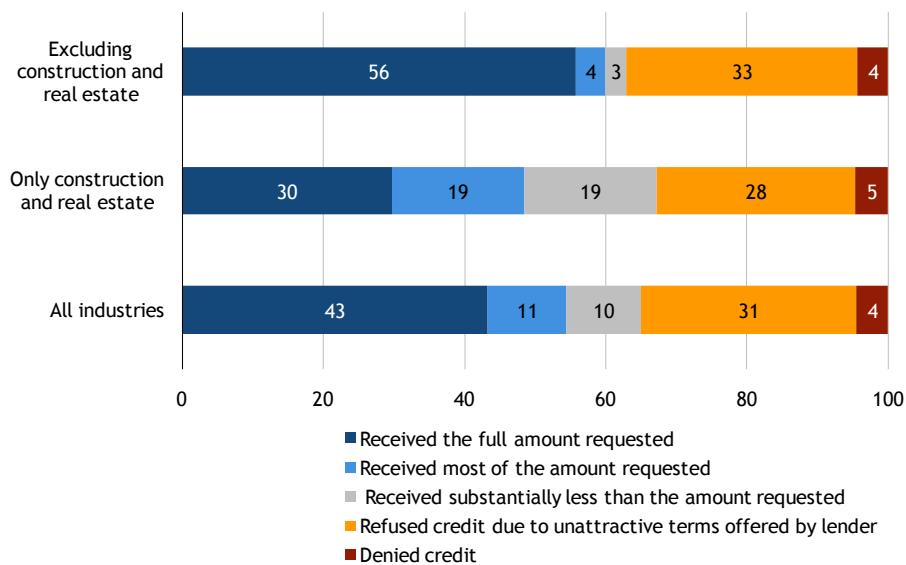
Improvement from Q2

In Q2, community and regional banks were much more likely to fulfill applications than were large national banks; this difference is more pronounced in Q3. While there was little to no change in for large national banks from Q2 to Q3, community and regional banks had a 9 percent increase in the number of applications for which they granted loans mostly or in full among repeat firms that applied for credit in both quarters.

**Extent to which you were able to meet your financing needs—
Large national bank (loan and line of credit)**
% of applications (all industries= 108 applications)



**Extent to which you were able to meet your financing needs—
Community or regional bank (loan and line of credit)**
% of applications (all industries= 134 applications)



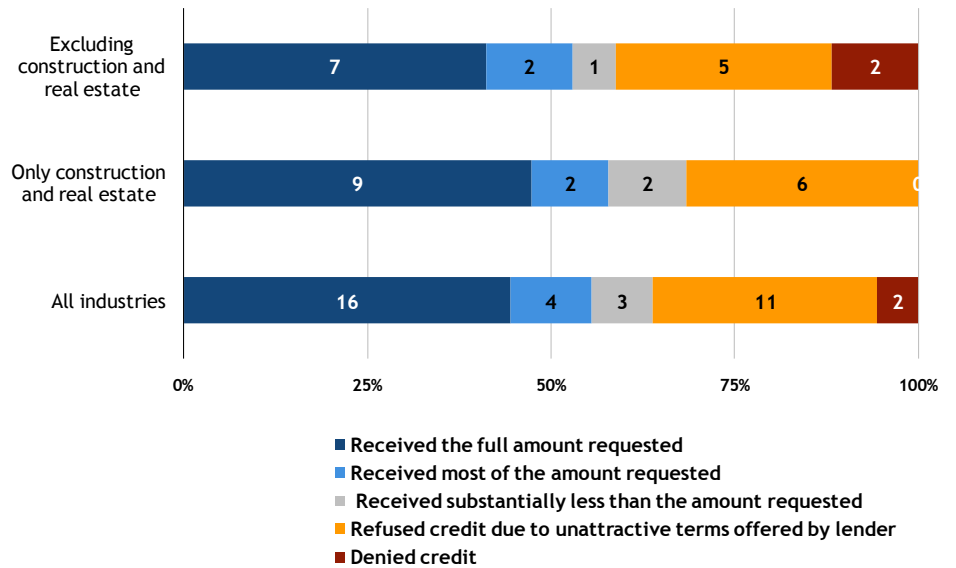
Approval rates across financing channels

Credit card companies

Applications at credit card companies were met more favorably in Q3. 56 percent of 36 applications in Q2 were met with full or most of the credit requested, an increase from 44 percent in Q2. Credit requests from vendors/suppliers also improved with 70 percent of 33 applications met mostly or in full, up slightly from 65 percent in Q2.

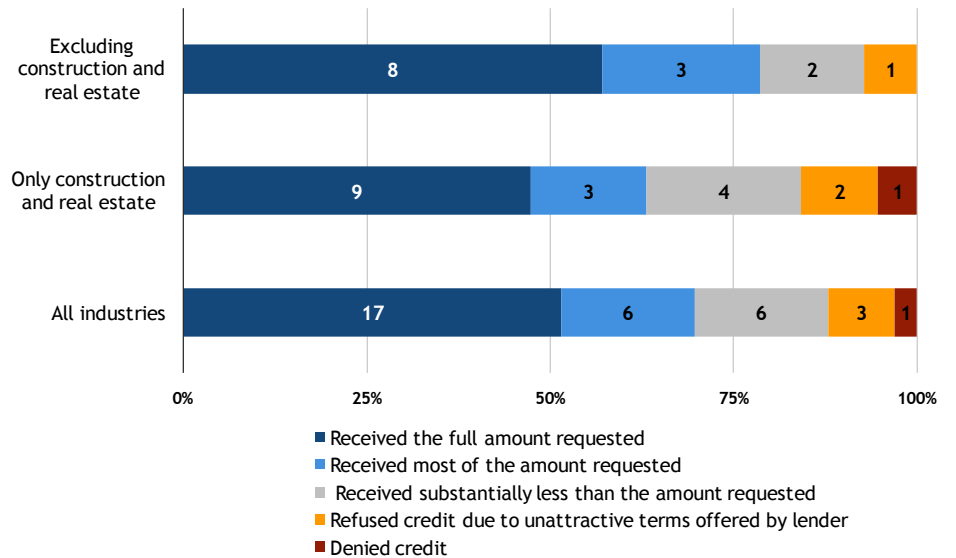
Extent to which you were able to meet your financing needs—
Credit card companies

% of applications (all industries= 36 applications)



Extent to which you were able to meet your financing needs—
Vendors/suppliers

% of applications (all industries=33 applications)



Uses of financing

Reasons for seeking credit in Q3 and reasons for planning to seek credit in Q4 or Q1 of 2011 were nearly identical. Across both questions, half of firms indicated they were seeking credit to manage cash flow while about a quarter said it was to expand their business.

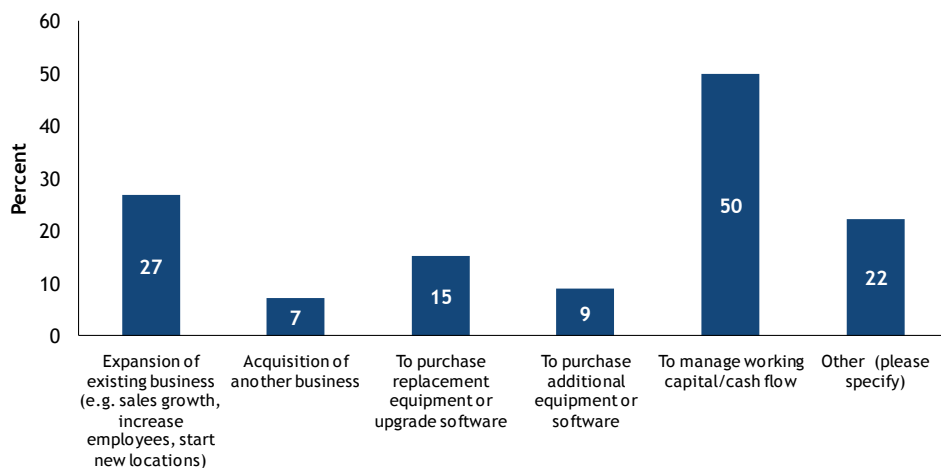
The answers are in line with responses from Q2, with one exception: slightly fewer are planning to use financing to expand their business.

66 percent of firms did not seek credit in Q3, which was in line with Q1 (62 percent) and Q2 (63 percent). The reasons firms gave for not borrowing were very similar to reasons given in Q2. The most-cited reasons were: sufficient cash on hand, sales revenue did not warrant borrowing, and existing financing met their needs.

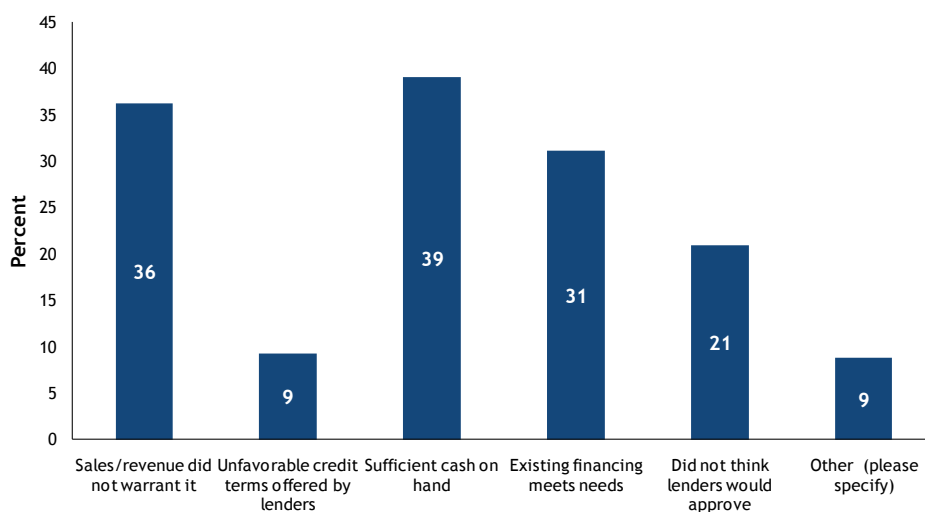
Decline in discouraged borrowers

In Q3, the percent of firms citing only supply-side reasons for not borrowing decreased from Q2, and was lower among firms not in the construction or real estate industry. The percent of discouraged borrowers also declined among the 237 firms that took the survey in both Q2 and Q3.

Reasons for borrowing
(146 responses from 112 firms)



Reasons for not borrowing
(313 responses from 215 firms)

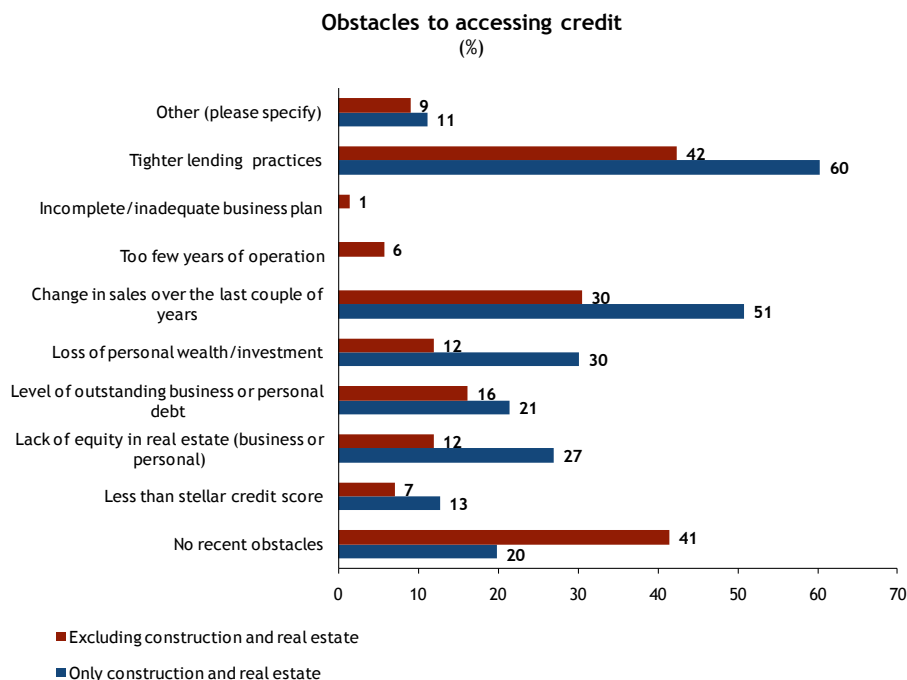


Percent of firms citing only supply-side reasons for not borrowing

	Q2	Q3
All industries	16	11
Only construction and real estate	18	15
Excluding construction and real estate	15	9
237 repeat firms only: All industries	15	10

Obstacles to financing

How construction and real estate firms perceive obstacles continues to stand out compared to firms in all other industries. Only 20 percent of construction and real estate firms see no recent obstacles compared to 41 percent of firms in all other industries. The obstacles to credit as seen by small business are little changed from Q2. However, firms noted change in sales over the past couple of years more often in Q3, with 51 percent of construction and real estate firms marking this category compared to 33 percent in Q2. This category saw a slight upward increase among other industries as well, from 23 percent to 30 percent. Several firms indicated in the comments sections that higher interest rates made it difficult for them to borrow, and several real estate and construction firms indicated it was difficult to obtain loans to build spec housing or develop land, saying bank regulators were to blame.



Young firms

Financing success

There were only 53 firms in the sample that were less than four years old. As a group, these younger firms had similar success obtaining credit, with nearly half receiving the full amount requested and 18 percent receiving most of the amount requested over all applications for credit. At the same time, there were a larger share of discouraged borrowers among this group: nearly a quarter of firms that did not apply for credit said it was due only to the belief that lenders would not approve their request or that unfavorable credit terms would be offered.

Channels of financing

The channels of financing among young firms did not differ much from the group as a whole. In line with the rest of the sample, one-third applied for credit. On average, young firms tapped more channels of fi-

ancing (4.6 instead of 3.6), and, as a result, a few channels were cited more often than others, including credit card companies, vendors/suppliers, and family or friends. However, banks were the most cited channel of financing, with 17 out of 18 young firms applying for credit at a bank. Surprisingly, young firms did not favor regional and community banks over large national banks, nor was there a significant correlation between age of a business and the use of a community or regional bank. Of the 17 firms less than four years old that recently applied for credit at a bank, only two applied exclusively at a regional or community bank. While young firms did not favor community banks over large national banks, as a group, they had more success at community banks, much like the sample as a whole.

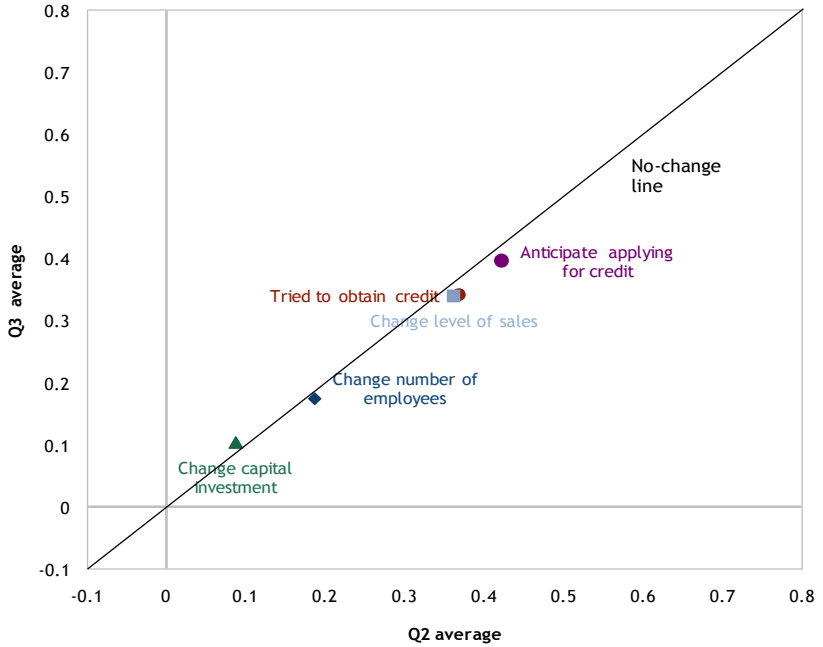
Future business conditions

Changes over the next six to twelve months

In addition to questions pertaining to credit accessibility and success, the survey also asks about anticipated changes to their business over the next six to twelve months. The net percent of survey participants responses in Q2 and Q3 are plotted here. Any dots plotted directly on the 45-degree line indicate there was no change in the net percent of responses from Q2. Dots above the 45-degree line indicate the net percent increased, while a dot appearing below the line indicates a decrease.

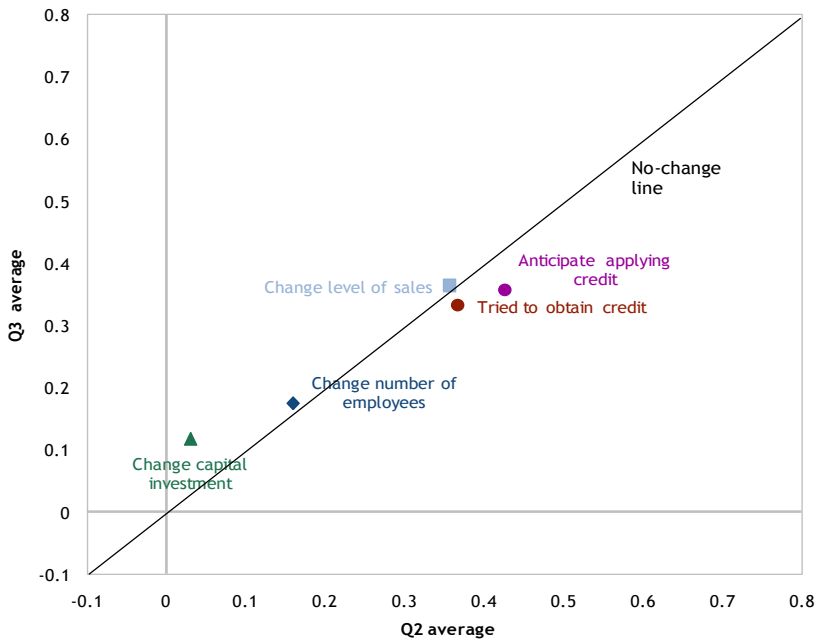
For example, among the 237 repeat respondents in the survey, 30 percent said they anticipated an increase in the number of employees in their business and 13 percent indicated they anticipated a decrease, resulting in a net 17 percent. Since this is higher than the net 16 percent that said they anticipated an increase in the second quarter survey, the dot appears above the 45-degree line. The net percent anticipating an increase in sales was one-half a percentage point higher in Q3, and the net percentage anticipating an increase to capital investment was up 8 percentage points.

Q2 versus Q3 responses—
Everyone



Notes: The responses for “Change in sales/Employees/CapX” values range from -1 to 1, where 1=Increase, 0=No change, and -1=Decrease. The “Tried to obtain/Anticipate applying” credit questions range from 0 to 1, with 1=Tried/Anticipate applying and 0=Didn't try/Don't anticipate applying.

Q2 vs. Q3 responses—
237 repeat respondents only



Notes: The responses for “Change in sales/Employees/CapX” values range from -1 to 1, where 1=Increase, 0=No change, and -1=Decrease. The “Tried to obtain/Anticipate applying” credit questions range from 0 to 1, with 1=Tried/Anticipate applying and 0= Didn't try/Don't anticipate applying.