NATIONAL ASSOCIATION
OF GOVERNMENT GUARANTEED LENDERS

"Access to Capital: Can Small Businesses Access the Credit Necessary to Grow and Create Jobs?"

Testimony Before the House Committee on Small Business

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Submitted by:

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NAGGL Gets It.

Chairman Graves, Ranking Minority Member Velázquez, and members of the Committee, my name is Lynn Ozer. I am an executive vice president at Susquehanna Bank, where I manage the bank's Small Business Administration (SBA) and government-guaranteed lending function throughout the bank's four state footprint. Susquehanna Bank is a Pennsylvania state-chartered bank that operates 223 branch offices in Pennsylvania, Maryland, New Jersey and West Virginia. The bank has been serving communities throughout the Mid-Atlantic for more than a century.

Susquehanna Bank is a subsidiary of Susquehanna Bancshares, Inc., a financial services holding company with assets of approximately $14 billion and more than 3,000 employees. SBA lending is centrally administered in our Pottstown, PA location. Our SBA loan portfolio has an outstanding balance of approximately $300 million, and we participate in virtually all the programs under the SBA 7(a) umbrella – SBA Express, Export Working Capital, Patriot Express, and Seasonal and Contract CAPLines – and are also a first mortgage lender under the SBA 504 program.

For the past 23 years, I have also served on the board of directors of the National Association of Government Guaranteed Lenders (NAGGL), headquartered in Stillwater, Oklahoma. In addition, I have been a member of the board's Executive Committee for more than 13 years, and chaired NAGGL's technical issues committee for approximately the same period.

NAGGL is a trade association with over 700 institutional members that participate in various capacities in the SBA loan programs all across the country. Our members are dedicated to providing critical capital to our nation's small businesses so that these businesses can grow, create more jobs, and contribute to our nation's economic vitality. NAGGL's lender members are responsible for approximately 80% of the annual SBA 7(a) loan volume as well as most of the lender portions of SBA 504 loans.

Thank you for inviting me to testify today on the important issue of small businesses' ability to access capital. Although my experience is on the lending side, many small business trade groups, including the International Franchise Association (IFA), whose representative is also testifying today, have told us that access to credit is the #1 issue for their membership. The IFA and many other similar organizations have found that while their members are ready and willing to take on additional risk to grow their businesses and create more jobs, accessing the capital necessary to support those efforts has proven to be a daunting task during these difficult economic times. To fully understand why, we need to look at what is happening in the banking industry today.

As a result of the recent 'great recession' many banks saw the quality of their assets decline significantly. In its March 31, 2011 *Quarterly Banking Profile*, the FDIC reported that as of that date, the non-current assets (loans on non-accrual and those 90+ days past due) at commercial banks totaled 4.79% of assets. In a normal banking environment that number would be around 1%. In addition, first quarter 2011 charge-offs were at an annualized pace of 1.91%, which is still far above the normal range of .25%-.50%. While improving over the last four quarters, both measurements still have a long way to go to get back to the normal credit-healthy range.

Because of these and other problems caused by the overall ailing economy, over the past several years, federal banking regulators have increased the capital requirements that they impose on banks. The result is a perfect storm of circumstances that together serve to stifle banks' abilities to make credit available to small businesses – fewer earning assets because of problem loans, increased capital requirements, and higher expenses due to additional FDIC insurance assessments.

So how does a financial institution make its regulatory capital ratios comply with the new requirements when it cannot raise capital? The institution shrinks its assets down so the capital that it has becomes a greater percentage of its total assets. And that is exactly what the commercial banking industry has done.

In its *Quarterly Banking Profile*, the FDIC reported that for the first quarter of 2011 (just last quarter): "Total loan and lease balances continued to fall, declining $126.6 billion (1.7 percent). This is the fifth-largest quarterly percentage decline in loan balances in the 28 years for which data are available, and it marks the tenth time in the last eleven quarters that reported loan balances have fallen (the one exception was caused by the implementation of FASB 166 and 167, which resulted in the consolidation of as much as

$400 billion in securitized loans onto banks' balance sheets in the first quarter of 2010)". Although the total amount consolidated cannot be precisely quantified, the industry would have reported a decline in loan balances for the first quarter of 2010 absent this change in accounting standards.

The combination of capital constraints and problem assets coupled with an enhanced awareness of the need for prudent lending in this economic environment has caused many lenders to become even more selective with their conventional small business lending. Loan underwriting standards are significantly tighter today than they were just a few short years ago. The result is that many creditworthy small businesses have difficulty accessing conventional loans to provide the capital that they need to grow their businesses, growth that is essential to the nation's economic recovery.

So how are banks meeting the credit needs of their small business customers? Many lenders have turned to, or returned to, the SBA loan programs, and in particular, the 7(a) loan program which is SBA's largest and oldest loan guaranty program. SBA Administrator Karen Mills noted recently that SBA had brought more than 1,200 lenders back to SBA lending over the last two years, adding: "That means we are getting more access and more opportunity for more small businesses in more communities".

This growth in the 7(a) program is essential to keeping credit flowing to small businesses because the program fills a critical gap for those businesses, particularly startup and early stage companies that need access to longer-term loans. SBA, through its private sector lending partners, accounts for well over 40% of all long-term small business loans made in America, making the agency the single largest provider of long-term capital to U.S. small businesses.

Let me briefly explain how the program works. The SBA has delegated most of the loan making and servicing authority to lenders while reserving the regulatory and oversight role to the agency. A significant percentage of the lenders in the program today are "preferred lenders", which means that SBA has delegated to them authority to attach a federal guaranty to a loan without SBA's full review. Other, generally lower volume lenders, submit their loans through a different process with SBA making the final decision about whether to attach the federal guaranty. In either case, it is the lender that actually provides the capital to the small business. SBA only steps in if the borrower defaults and there is a loss on the loan, and then, only to the limit of its guaranty, generally 85% for loans of $150,000 and less, and 75% for larger loans.

From the lender viewpoint, a key benefit of the 7(a) program is that it takes less capital to support an SBA loan than it does a conventional loan. This is because federal regulators impose different capital requirements on SBA-guaranteed loans, and because lenders can choose to sell the guaranteed portions of their 7(a) loans in the secondary market in order to increase their liquidity.

From the viewpoint of small businesses, the SBA guaranty allows increased access to capital, particularly to the kind of financing that appropriately matches the loan term to the life of the asset being financed – that is, financing long-term assets with long-term loans. According to federal statistics, the typical 7(a) loan has an average original maturity of 12 years, while conventional small business loans typically have original maturities of three years or less (with the significant majority of those loans having maturities of one year or less). Longer maturities allow small businesses to access capital that would not be available to them if repayment were required in substantially shorter periods.

The importance of SBA lending to small businesses is clearly evidenced by the demand for the programs. According to SBA statistics, between its 7(a) and 504 program guaranties, in just the last two years, the agency has helped to deliver $42 billion into the hands of small business owners. When you add the dollar value of the private sector first mortgage portion of the 504 loans, that loan total number goes even higher.

However, the very success of the 7(a) program this year is causing a new problem. Based on loan approvals to date, it appears highly likely that program demand will exceed the $17.5 billion program level ceiling set by congressional appropriators. While sufficient appropriations remain to meet program demand, the program cap will likely cause SBA 7(a) lending to shut down this summer unless the Congress acts to raise the program level. It would be a shame for the program that is best meeting the credit needs of small businesses to be suspended because of an arbitrary program ceiling.

In order to be sure that the 7(a) program is able to meet the needs of its eligible and creditworthy small business applicants, we request that the program level for SBA's business loan programs be increased from $17.5 billion to $19 billion for the current fiscal year. No additional appropriations will be required to support this increase. This action is necessary before the August congressional recess because it is highly likely that the program cap could be reached before Congress is back in session, thus shutting off small businesses' access to this important source of capital.

In closing, on behalf of my bank and other 7(a) and 504 lenders, I want to thank this Committee, the Congress and SBA for the steps that it has taken to revitalize SBA's loan programs and to make them more accessible and cost-effective to small business borrowers and lenders. Over the past several years, working together on a non-partisan basis, SBA and Congress have crafted a number of excellent short- and long-term solutions aimed at jump-starting lending to small businesses. The success of those solutions is readily illustrated by the dramatic increase in SBA lending that occurred subsequent to enactment of the Recovery and Small Business Jobs Acts. The results are clear – unprecedented lending levels in the SBA 7(a) and 504 programs realized last fiscal year, and that are on track to be realized again this fiscal year.

The public-private partnership that exists in SBA's lending programs has been and continues to be a shining example of what can be achieved when the federal government and the private sector — both lenders and other organizations, like IFA that support small business development — work together. We know that small businesses lead the way in creating new jobs, and we know that having a vibrant small business segment in our economy is vital to continuing the fragile economic recovery that we are seeing today. We also know that keeping SBA's 7(a) and 504 loan programs available to meet the capital needs of the tens of thousands of creditworthy small businesses that have nowhere else to turn is equally vital. These loan programs merit continued bipartisan support in the Congress.

Mr. Chairman, this concludes my prepared statement. Thank you for all you have done to support America's small businesses, and for giving me the opportunity to testify before you today. I would be pleased to answer any questions.

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