Chairman Bernanke

Ben Bernanke:

Thank you Sandy. Good morning. Let me begin by thanking the staff of the Board's Division of Consumer and Community Affairs, especially to Divisions Director Sandra Braunstein, for the hard work they've done to prepare for today's discussion about approving access to credit for sound small businesses. And thanks also to the many partners who helped us to organize today's event; particularly the Small Business Administration and the Treasury's Community Development financial Institutions Fund. I'm pleased to welcome all of you to the Federal Reserve Board.

This gathering addressing the financing needs of small businesses serves as a capstone for a series of more than 40 meetings conducted across the country starting in February organized by the Federal Reserve Systems Community Affairs offices. These meetings provided forums for small business owners, trade associations, lenders, bank supervisors, federal, state and local government officials and other stakeholders to exchange ideas about the challenges facing small businesses both in the short run and in the longer term.

Some of these meetings were small group discussions while others were larger sessions that addressed specific topics such as minority entrepreneurship or guaranteed loan programs. For example as Cindy mentioned, I attended a meeting in Detroit that combined a general discussion of small business credit issues with a session focusing on specific case of suppliers to the auto industry. Many of which are small and medium-sized firms.

Participants in that session highlighted the interconnectedness of the auto supply chain and the crucial role of stable financing for small businesses ranging from part suppliers to independent automobile dealers in the recovery of the automobile industry as a whole. This was of course just one meeting in one city. A meeting in Miami focused on the needs of Hispanic-owned small businesses. Similarly informative discussions took place in cities such as New York, San Francisco, and Chicago among many others including Omaha, Nebraska, Morgantown, West Virginia, Toledo, Ohio, and Little Rock, Arkansas.

Our objective in organizing this series was to gather information that we and others can use to help develop policies that will support the flow of loans to creditworthy small businesses. For instance by identifying and addressing specific credit gaps or impediments to lending were improving the access to small businesses to critical support services; such as assistance in filing loan applications. This information serves as the basis for today's discussions and next steps that policy makers and stakeholders can undertake to insure that small businesses are able to participate in and contribute to the economic recovery.

Before we get to the next steps however I would like to provide context by briefly discussing the importance of small businesses to job creation and the economic recovery, reviewing the actions the Federal Reserve has taken to support small business financing, and offering some observations about what we heard during the small business meeting series.

Small businesses are central to creating jobs in our economy. They employ roughly one-half of all Americans and they account for about 60% of gross job creation. New or small businesses less than two years old are especially important. Over the past 20 years these startup enterprises accounted for roughly one-quarter of gross job creation even though they employed collectively less than 10% of the workforce.

The formation and growth of the small businesses depends critically on access to credit. Unfortunately, those businesses report that credit conditions remain very difficult. For example, the net percentage of survey respondents telling the National Federation of Independent Business that credit conditions have tightened over the prior three months has remained extremely elevated by historical standards. And one measure of banks loan to small businesses dropped from more than 710 billion dollars in the second quarter of 2008 to less than 670 billion in the first quarter of 2010. An important but difficult to answer question is how much of this reduction has been driven by the weaker demands for loans from small businesses, how much by a deterioration of financial condition of small businesses during the economic downturn, and how much by restricted credit availability. No doubt all three factors have played a role. Clearly though to support the recovery, we need to find ways to ensure that creditworthy borrowers have access to needed loans.

Over the past two years, the Federal Reserve and other agencies have made a concerted effort to stabilize our financial system and our economy. These efforts importantly have included working to facilitate the flow of credit to viable small businesses. At the Federal Reserve we help bring capital from the securities markets to small businesses through the Term Asset-backed Securities Loan Facility, the TALF program. More than 850,000 small business loans were financed in part by securities whose issuance was through TALF. We've also been focused on strengthening the nation's banks so that they can resume normal lending as quickly as possible. For example, the stress test that we conducted last year helped restore confidence in the banking system; allowing banks to raise the capital that they need to offset credit losses and ultimately to provide the basis for new lending.

We have heard the often expressed concern that bank examiners have prevented banks from making good loans. We take this issue very seriously. The Federal Reserve has worked assiduously with the other banking regulators to develop interagency policy statements on this issue aimed at both banks and bank examiners. Our message is clear. Consistent with maintaining appropriately prudent standards, lenders should do all that they can to meet the needs of creditworthy borrowers. Doing so is good for the borrower, good for the lender and good for our economy. To ensure that this message is being heard and acted upon, we've conducted extensive training programs for our bank examiners as well as outreach with bankers. We will continue to seek feedback from both bankers and borrowers.

Though we believe that ours and efforts are making a big difference we also know that more must be done; and that additional effective action requires hearing firsthand from knowledgeable people who can speak from diverse perspectives about the challenges now facing small businesses. The insights we obtain from small business owners, lenders, and others in this series of meetings have given us a more nuanced understanding of the problem and will help us identify areas where we might be able to do more. Not surprisingly, these meetings confirm that facilitating small business financing is not a simple or straightforward manner. Notably the term small business encompasses a heterogeneous mix of enterprises ranging from pizzerias to startup technology firms. And each small business faces a unique combination of local economic conditions and complex relationships with customers, suppliers and creditors. Hence, we should be wary of one-size-fits-all solutions.

One of the most important themes underscored during the meetings is that solving the issues faced by small businesses will require collaboration. The meeting series itself served as a model of collaboration, interactive discussion, and cooperative problem-solving. Participants included community affairs officers, bank supervisors, economists, and policy makers for the Federal Reserve. We also involved our fellow bank regulators, Small Business Administration, and a CDFI Fund. And of course small businesses and lenders played essential role. The meetings fostered stimulating conversations, lenders heard from small business owners about the frustrations over tightened credit. And likewise lenders were able to explain the considerations that go to making a small business loan. And regulators heard in detail concerns expressed about the effects of their procedures and guidance on small business lending.

Some common themes emerged from these discussions. Business owners frequently noted that the declining values of real estate and other collateral securing their loans poses a particular severe challenge. As one business owner at a Detroit meeting I attended put it, if you thought housing has declined in value take a look at what equipment is worth. Business owners cited credit lines and working capital as their most critical financial needs followed by refinancing products that would permit them to take advantage of low interest rates. Many reported having had to resort to borrowing through their personal credit cards or from their retirement accounts. Several mentioned the need for small value loans in amounts less than $2,000 as well as the need for patient capital from investors willing to commit funds for five to ten years without an expectation of immediate returns.

Some of the lenders that participated in our meetings expressed a view that current lending conditions don't represent credit tightening as much as a return to more traditional underwriting standards following a period where standards were too lax. But though some lenders said they were emphasizing cash flow and relying less on collateral values in evaluating credit worthiness, it does seem clear that some creditworthy businesses including some who's collateral has lost value but who's cash flows remain strong, have had difficulty obtaining the credit that they need to expand and in some cases even to continue operating. The challenge ahead for lenders will be to determine how to assess the credit quality of businesses in an uncertain and difficult economic environment. It is in lender's interest after all to lend to creditworthy borrowers. Ultimately that's how they earn their profits and regulators for their part need to continue to work with lenders to help them do all that the prudently can to meet the needs of creditworthy small businesses.

Making credit accessible to sound small businesses is crucial to our economic recovery and so should be front and center among our current policy challenges. We are very pleased that you have accepted our invitation to participate in today's discussion of next steps in the efforts to promote sound small business finance. You each bring valuable insights and perspectives to this issue and I'd very much like to thank each and every one of you for your willingness to share your ideas. Thank you and the best for a good discussion today.

[Applause]