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Credit Tightens for Small Businesses

By PETER S. GOODMAN

Many small and midsize American businesses are still struggling to secure bank loans, impeding their expansion plans and constraining overall economic growth, even as the country tentatively rises from its recessionary depths.

Most banks expect their lending standards to remain tighter than the levels of the last decade until at least the middle of 2010, according to a survey of senior loan officers conducted by the Federal Reserve Board. The enduring credit squeeze appears to reflect an aversion to risk among lenders confronting great uncertainty about the economy rather than any lingering effects of the panic that gripped financial markets last fall, after the collapse of the investment banking giant Lehman Brothers.

Bankers worry about the extent of losses on credit card businesses as high unemployment sends cardholders into trouble. They are also reckoning with anticipated failures in commercial real estate. Until the scope of these losses is known, many lenders are inclined to hang on to their dollars rather than risk them on loans to businesses in a weak economy, say economists and financial industry executives.

“The banks are just deathly afraid,” said Sam Thacker, a partner at Business Finance Solutions in Austin, Tex., which helps small businesses line up financing. “I don’t see commercial banks coming back to the market anytime soon.” In the long view, tighter loan standards seem healthy after a terrible crisis attributed in part to years of recklessly lenient lending.

But some economists worry that bankers have overshot the boundaries of a healthy reaction, as even strong companies are finding it difficult to borrow.

“The banks are still very risk averse,” said Robert J. Barbera, chief economist of the research and trading firm I.T.G. “Regional banks are in a particularly tough spot, because they’re choking on commercial and residential real estate.”

Bankers acknowledge that loans are harder to secure than in years past, but they say this attests to the weakness of many borrowers rather than a reluctance to lend.

“Banks want to lend money,” said Raymond P. Davis, chief executive of Umpqua Bank, a regional lender based in Portland, Ore. “The problem is the effect that the recession is still having on us. Some of these businesses are still trying to come out of it. For them to go to a bank, if they are showing weak performance, it is harder to borrow.”

As the financial crisis has largely eased in recent months, big companies have found credit increasingly abundant, with bond issues sharply higher.

But for ordinary consumers, the picture is quite different. What was once of a flood of come-ons for home equity loans and credit cards has been replaced by notices of lowered credit limits.

For many smaller companies, too, borrowing remains tough.

Some 14 percent of small businesses found loans harder to secure in August than in July, according to the most recent survey by the National Federation of Independent Business. Among companies borrowing regularly, less than one-third reported that all their credit needs were being met.

"It's quite significant, because small businesses generate significant job growth," said Andrew Tilton, a senior economist at Goldman Sachs. "And small businesses rely more on bank financing, whereas large businesses have the alternative of raising money in the capital markets."

Businesses with fewer than 500 employees hold more than half of the nation's private sector jobs, according to the Small Business Administration.

In Port Arthur, Tex., Five Star Feeds, which sells gardening supplies, pet food and livestock feed, is stuck in a holding pattern on a planned expansion as the owner, Tina E. Bean, tries to persuade her local banker to provide $150,000 in credit.

Ms. Bean began the business in 2001 and has been profitable ever since, she said. She has already borrowed about $800,000 for her expansion, more than doubling the size of her storefront as she adds new product lines, including Western-style clothing like jeans and cowboy boots.

But without the last $150,000, she is unable to order the new products. Her new shelves remain bare. She missed the deadline to tap her final $150,000 in credit, she says, and her banker refused to offer a new loan, even as she insisted that she could not move into the new space.

"His answer is, 'We'll cross that bridge when we get there,' " Ms. Bean said. "Well, I'm there. I can't open the store if I don't have anything to put in it."

Until she obtains financing, she has no reason to hire the two or three people she will need to run the larger space. She has no reason to place orders that would increase work for truck drivers who ferry blue jeans and pet grooming supplies to retail stores, and no need to bring on accountants, insurance agents, lawyers, forklift drivers and auto mechanics whose business opportunities would be incrementally expanded by more commerce.

Among small privately held companies, the amount of debt they carry as a portion of their equity has slipped by about 5 percent since 2007, according to Sageworks, a financial analysis firm in Raleigh, N.C. The drop reflects not only how companies have cut their inventories and paid down debt, but also the tightened credit terms they face when they try to borrow, said a Sageworks spokeswoman, Melinda Crump.

For companies that work on a contract basis bidding for jobs in advance, tight credit sometimes precludes their ability to seek new business: They cannot raise capital to hire workers and add equipment.

In Alexandria, Minn., Bob Novak, president of ACB Construction, has in recent months declined to bid on large-scale government jobs in Utah because of what he describes as a frustrating lack of credit for people in his line of work. His work force has shrunk to 1, from 14, in the last two years, yet every effort to generate fresh business seems to get snuffed out by rejections from banks.

“You might as well not walk through the door of a bank and have construction behind your name,” Mr. Novak said. “You cannot get a loan if you don’t look profitable, and you can’t look profitable if you can’t bid the work. I’ve had to walk away from jobs because I cannot get the funding.”

Med-National provides medical and dental services on a contract basis, mostly to the Defense Department. The San Antonio-based company has been in business for more than 20 years, has never lost money, and logged $5.9 million in sales last year, said the executive vice president, Robert S. Welborn Jr.

Yet as the company recently sought to secure a pair of contracts with the United States Army, its plans were delayed for nearly a year as it tried and failed to persuade a bank to lend it $300,000. The financing was required to hire the roughly 20 people needed to deliver the services — doctors and dentists and support staff.

Mr. Welborn initially called local banks with whom he had done business in years past, among them JPMorgan Chase and Wachovia. Their answer surprised him: no.

“It used to be you could practically just jangle your keys and they would give you some money,” Mr. Welborn said. “It isn’t anything like that anymore.”

In August, Mr. Welborn finally lined up financing from Wells Fargo and began hiring. Yet the delay and the uncertainty have left him reluctant to pursue other contracts.

“If we could borrow the money more easily,” he said, “we would be hiring even more people.”