

CITY OF MIAMI

SMALL BUSINESS TASKFORCE

**ECONOMIC
*EMERGENCY PLAN***



PRESENTED BY:

**The Small Business Taskforce - City of Miami Mayor's Office, Local Community Banks, Local
Micro Lender - Accion USA, The Minority Business Enterprise Center (MBEC™) and
The Small Business Administration (SBA)
In Collaboration with: The Small Business Roundtable**

The Small Business Community: Fueling the Florida Economy

Fueled by small business and microenterprise, Florida generates more economic activity than Shanghai, Taipei, Lisbon and Beijing combined. The metropolitan centers of Miami, Orlando and Tampa, together generate more than 40% of the gross state product (GSP). According to the “2008 Small Business Economy Report to The President,” published by the SBA, the small-business sector provides half of the nation’s nonfarm, private real gross domestic product (GDP). The report also indicates that in the first quarter of 2007 74% of the net new jobs were generated by firms with fewer than 500 employees and 22% were by firms with fewer than 20 employees.

Florida Small Business Profile

Small businesses are the driving engine of South Florida. Of all shapes and sizes, from “mom & pops” to multinational, these businesses keep Florida at the top list of Mega Regions. To consider:

- Florida’s smallⁱ employers represent 99% of the state’s employers and 44% of its private-sector employment.
- Small businesses created 58.7% of the state’s net new jobs from 2004 to 2005.
- Florida’s real gross state product had a negligible increase in 2007. By comparison, growth in the Southeast region was 1.5% and the United States, 2.0%.ⁱⁱ
- Net job change for 2004 to 2005 was greater for firm sizes with 1-4 employees (104,160) than it was for larger firms of 500+ employees (96,117).ⁱⁱⁱ

Given the critical importance of small business to the state economy, it is important to note that the current “stimulus” related initiatives are not geared towards the small business community. If we are to truly address the economic challenges of our time, we must redirect the focus of the initiatives to our small businesses.

Miami Perspective and the Small Business Impact

For Florida and Miami-Dade, specifically, the health of the small-business sector plays a greatly important role in the local economy’s resurgence and ongoing success. According to the 2006 Census Business Patterns, there were 1,189,508 businesses operating in Florida. 1,187,129, or 99.8%, were firms with fewer than 500 employees and 1,044,674, or 88%, were firms with fewer than 19 employees. The same source indicates that 297,605 businesses operated in Miami-Dade County. Of the total in Miami-Dade, 297,009, or 99.8%, were firms with fewer than 500 employees and 267,308, or 90%, were firms with fewer than 19 employees. The life blood of Florida’s economy and particularly Miami-Dade and the City’s economy is the small to mid-size business sector, which depend on the community banks and other smaller financial intermediaries to provide the lending and credit facilities needed to operate and grow these enterprises.

Despite aggressive program announcements geared to reigniting a stalwart like SBA lending, SBA statistics indicate that the top 10 biggest volume lenders have reduced their lending activities by nearly 80%. Today, the top 10 lenders are emerging among community banks.

Additionally, South Florida financial institutions have been left out of current programs. Only twelve Florida financial institutions have received Troubled Asset Relief Program (TARP) money

to date. The total received by these twelve institutions thus far is \$203,396,000 of the \$327,585,230,000 distributed. A mere .0621% of the total TARP funds distributed and South Florida has received \$0. The vast majority of the \$327.6 billion dollars allocated through TARP so far ended up in the hands of financial institutions whose primary business models are in Wall Street financial intermediation rather than community banking.

“An Economic Perfect Storm”: The Nation’s Perceived Instability Affects Small Businesses^{iv}

While the demise of Bear Sterns, Lehman Brothers and others have come to symbolize the ‘economic perfect storm’ in the global financial markets, precipitous declining real estate values and the recession as it hits our local communities have become the real small business problems and are the principal causes for the most obvious small business credit consequence, depressed demand. Lower credit demand is a natural result of fewer opportunities for productive investment and poorer sales with their resultant weakening balance sheets. Small business owners are frequently invested in real estate, as well.

Real estate losses, if only on paper, depress balance sheets and have made borrowing, even when legitimate investment opportunities appear, financially unworkable. All of this has led to credit tightening and while small business owners and managers are not as concerned about causes and complications as they are about impacts, many now believe that the survival of their enterprises are threatened.

What are the obstacles to the growth of a more vibrant small business economy?

From the small business perspective the issues are simple;

- *Access to financing for small businesses is virtually non-existent.*

The ability to obtain credit appears statistically related to financial strength, as measured by greater sales growth in the last two years, fewer mortgages taken out to finance other business activity, fewer upside-down properties, as well as the owner’s positive evaluation of firm performance against the competition, and firm maturity, more specifically, years of operation. Discouraged borrowers, that is, owners who do not attempt to borrow for fear of rejection, are statistically related to what appears to be weak balance sheets, specifically, falling real sales over the last two years, ownership of more upside-down properties, lesser use of real estate for collateral, more mortgages taken out to finance other business activity, and the owner’s negative evaluation of firm performance against the competition.

- *Small businesses are faced with tremendous cash flow shortage, caused by tight credit.*

Financial institutions changed the terms or conditions of a loan, line or credit card for 18 percent of small employers. (This figure is somewhat low because only the largest line of credit and the most important credit card used for business were evaluated.) Most of the changes would be termed negative, such as a lower limit on a credit card or higher interest on a line of credit, though not all changes, particularly with respect to lines, were adverse.

- *Small business owners' business and personal finances are intertwined.*

Real estate, particularly home mortgages, is frequently used to finance or collateralize other business assets. Seventy-six percent (76%) have at least one mortgage on the real estate they own with 13% having three or more mortgages, 22% having taken out at least one mortgage to finance business activities. Sixteen percent (16%) use real estate to collateralize other business assets, including 10% who use their homes as collateral. About one in 10 (9%) own at least one currently upside-down property. The financial leverage homes provide businesses in a weak economy with declining real estate values is a matter of concern.

From the standpoint of Financial Institutions;

- *Lenders are caught between bank regulations and lending.*
- *Community banks have been left out of government programs that were created to unfreeze credit availability.*

Current Efforts Are Failing Main Street America

To date the Federal government's focus has been to stabilize global systemic risk, with the hope of assisting Main Street America through 'trickle down' economics. For the most part, programs that have been announced and/or implemented have been designed to deal with the problems of multi-market financial intermediaries whose collapse would place at risk the integrity and stability of global financial markets. Unfortunately, these programs have done little to assist community banks and other lenders that provide support for the small and midsize business sectors.

Efforts to make additional capital available to small business through directed (encouraged) bank lending or indirectly through government guaranteed lending has not shown any immediate effect. Unless there is a plan to massively subsidize those loans, firms who most often want credit (high risk) are typically not able to absorb additional debt with reasonable prospects of repaying it. Such lending practices save a few while condemning others to worse circumstances than they otherwise would have encountered, leaving a third party to hold the debt. The current policy response lies elsewhere, in efforts to stimulate the economy in order to instill confidence and generate sales, thereby improving balance sheets and reducing the need to borrow. But a stimulus cannot be a random collection of politically-inspired tax cuts and spending increases, where increased productivity and the job generating potential of small business owners are neglected.

The massive expansion of liquidity now in progress with additional expansion intended may abort deflation and its consequences, but will banks use the money to lend or cover losses? Over the longer term, regulation of the financial system will be reviewed, as it should. However, the threat is the likelihood of overreaction rather than the reverse, recreating a depression-like cartelization of the financial services industry which historically reduced access to credit for small firms, particularly the young and the entrepreneurial.

TARP is the first example of a well-intentioned program that failed to meet Main Street expectations. According to a Wall Street Journal article on April 16, 2009, titled "TARP Cash Isn't Moving Forward" the Treasury Department now officially acknowledges that the largest recipients of U.S. government aid are offering less credit to businesses and consumers.

The criteria government used for distributing funds under most of its stimulus programs has a great deal to do with their ineffectiveness in helping reignite Main Street. TARP was originally intended to assist troubled banks that had been caught in the vortex of residential mortgage lending by allowing them to offload troubled assets from their balance sheets. The program quickly morphed into an initiative that did little to help community bank lenders, which are the primary source of financing for the small to midsize business sectors.

In an environment where regulators are giving a common mandate to banks to preserve capital and increase risk mitigation financial data and growing default rates are making it difficult to justify traditional loans and/or underwriting exceptions. This is in direct contradiction to the intent the stimulus investment was designed to grow.

Community Banks: An Immediate Solution

The FDIC has seized 58 banks in the past 15 months and there are no signs of abatement. Despite the dismal headlines, one end of the banking spectrum that has fared quite well during this Credit Crisis is the Community Banks. Unlike the "too-big-to-fail" banks, they never veered off their conservative course, sticking to more traditional best lending practices that, at the time, didn't seem exotic enough to keep the interest of the likes of the large banks. Perhaps, more importantly, they stuck to the golden rule: know your customer. At a time when lending poured out like a broken water main, Community Banks steered clear of speculative, overvalued financial products such as credit default swaps that resulted in high default rates and huge write offs. Now, their doors are open to lending and the more the merrier.

The re-emergence of independent banks rooted within our communities -- where local people are making decisions for local people -- is without a doubt the most efficient and effective way to get new, small businesses started which in turn hire people and jump-starts our economy. Community banks actively lend to build and grow their surrounding communities. They focus and engage in lending activities that help successful small and mid-size businesses to flourish and grow, and proactively engage in community development at the grassroots level. Yet they find themselves increasingly disenfranchised by Federal government stimulus initiatives and therefore unable to fulfill this role.

While it is certainly important to stabilize the global financial system in order to regain our national economic momentum, there are measurable and tactical components within the financial framework, which include the importance of community banks that can assist the small to midsize business sector, achieve a full economic recovery.

The Small Business Taskforce proposes solutions that can be sought both for the short-term and long-term.

Initiative	Short-Term (60 – 90 days)	Long-Term (> 120 days)
Use the Community Bank network as a conduit to provide guaranteed funds for the sole purpose of small business credit.		●
Explore ways to engage private equity capital to fill the void for other more traditional lending channels.		●
Refocus portions of Federal government aid to ensure health of the community banking sector.	●	
Target Federal programs to geographies of greatest need – address the epicenters of the current economic downturn by prioritizing aid programs according to economic impact at Main Street level.	●	
Work with bank regulators to recalibrate risk weight for small to mid size business loans to soften impact on capital.	●	
Work with banking regulators to allow community banks to spread whole-loan losses over multiple earning periods to alleviate stress on capital and to rebuild capital levels at a pace that is more reasonably tied to revenue generating potential.	●	
Encourage SBA and other guarantee programs to be more tolerant of lower personal credit scores when underwriting during these unprecedented economic times.	●	
SBA must consider current economic environment for the small and mid size business sectors equal to or greater than a natural disaster and must therefore enable the sector to access programs like the SBA Economic Injury Loan and Economic Disaster Loan programs as is it were a time of natural disaster.	●	
Consider expanding SBA loan guarantee programs to accommodate a broader range of micro-lending activities and/or to enhance equity capital risk mitigation.		●
Expand or enact tax credit programs that entice equity capital to invest in targeted industries not readily served by traditional lending channels.		●
Assist community banks that did not dabble in exotic derivatives products or high-risk and complex debt instruments but instead were caught in the vortex as a result of actively lending to build and grow their communities.		●

At this present time in our history, we cannot afford to make casual choices and to wait for answers to knock on our doors. The Small Business Taskforce, comprised of city government, federal agencies, community banks and lenders and the Small Business Roundtable, stand ready to work with the new Administration and Congress to listen and act courageously in providing the urgent life support that is needed for small businesses across America. The alternative is life-threatening. Let us act with the knowledge that our economic danger is not only imminent on Main Street; it is already here.

ⁱ Note that a small business is defined here as one with fewer than 500 employees. The majority of small businesses are less than 20 employees. The “informal” economy is not taken into account. Small Business Profile published in 2008 by the US Small Business Administration, Office of Advocacy.

ⁱⁱ U.S. Dept of Commerce: Bureau of Economic Analysis.

ⁱⁱⁱ U.S. Dept of Commerce, Bureau of the Census.

^{iv} National Federation of Independent Business, Volume 8, Issue 7, 2008