

CREDIT FOR MICRO-BUSINESS
Remarks of
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Introduction to a Conference on Credit for Micro-Business
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Thank you very much for inviting me here today. This conference joins two very important parts of our economy — small businesses and financial institutions. Both are essential to growing employment, continuing innovation, increasing productivity, and higher personal incomes generally.

There is no strict definition of a small business. Some people classify all firms with 100 or fewer employees as small businesses. These are the micro-businesses to which this conference is addressed, I understand. Others believe the cutoff should be higher, say 500, and certain definitions ignore labor force size altogether in favor of sales levels or other criteria. There may be disagreement over just what constitutes a small business, but it in no way detracts from their economic significance as we can see by looking at the example of financial institutions, particularly banks, which are also nowadays subject to definitional debates. Whatever the precise definition, there is pretty strong agreement among economists and others researchers that small companies are a vibrant, dynamic and vitally important segment of our economy. Evidence of that importance is apparent if we take a very conservative definition of small businesses — those with fewer than 20 employees. Such firms provide almost one-third of all private sector jobs in our economy and about twice that many net new jobs. Small businesses also provide much of our innovation.

Commercial banks and other financial intermediaries are major sources of the funds which small businesses use for working capital and expansion. They also serve as useful sounding boards, helping to focus small businesses' plans on profits and losses at an

early planning stage and providing an important element of quality control for small business plans by doing so.

In my conversations with business people in the Southeast, I often hear from managers of small businesses that one of their major problems is financing. Their comments are not specific to just the Southeast. Many surveys of small businesses in this country indicate that financing problems are widespread. Bankers on the other hand typically tell me that small businesses are quite important customers who get credit if they can show that they are credit-worthy

There is truth in both small businesses' complaints and bankers' responses. Managers of small businesses often know a lot more about producing a product or service than about making a written or verbal presentation about financial plans. Being small, these businesses often lack staff of their own who can specialize in financing. The smallest of these businesses may even be stretched to afford an accountant to make convincing presentations of data for them. Small businesses are often not typical. Thus they are difficult to analyse "by the book." In addition, new businesses and their owners often have not established a track record, a vital ingredient in any lender's or investor's risk assessment. What I have described is not true of all small businesses, but it is true often enough, I believe, to cause important difficulties.

Banks, on the other hand, get nervous when documentation is not good. They may fail to see through foggy business plans to the real potential of a business venture, particularly if their credit analysis system is not flexible and their credit analysts do things by the book.

Many of the problems seem to revolve around communication and knowledge.

Consequently, it is important that small businesses and their lenders talk to each other about their problems. My strong feelings about this need to communicate explain my excitement that this conference is taking place. I am pleased that small business people and their lenders are sitting down to talk about issues which stand in the way of their working more productively together. I believe that better understanding of these issues will help both to serve their markets more effectively, and consequently, more profitably.

I emphasize better communication and knowledge because I believe that having to provide data on finances and business plans to lenders often strengthens small businesses planning. It requires them to focus on important issues which might otherwise be slighted. The process of getting credit may weed out some businesses and projects which might succeed, but it also eliminates businesses and projects which have little or no chance, avoiding problems for both promoters and lenders. Thus, while I urge those among us who are bankers to do your best to discover the potential of small business borrowers and to meet them flexibly and imaginatively, I also urge you to stand by your attempts to make loans that will be repaid with principal and interest on schedule. You serve no one when you make a bad loan -- not yourselves, not the borrower, not the public.

I applaud you for getting together here. I am sure we all give particular thanks to Larrienne Simon, who has been the driving force behind this gathering. The rest of the morning should be very useful to us all.