FEDERAL DEPOSIT INSURANCE CORPORATION

2018

FDIC Small Business Lending Survey







FDIC

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The insights from the Small Business Lending Survey (SBLS) are a result of the contributions of a large number of U.S. banks. In particular, the Federal Deposit Insurance Corporation (FDIC) sincerely thanks the approximately 1,200 banks that responded to the survey. Without their invaluable participation, it would not have been possible to provide a nationally representative picture of banks' small business lending practices, or to compare the experiences of different-sized banks.

In addition, 40 banks across the U.S. participated in interviews with FDIC staff, helping ensure that the questions asked by the SBLS were understandable, answerable, and relevant to the banking industry. These conversations were necessary because the SBLS was specifically designed to cover topics not already addressed by other data sources. Another 11 banks were visited to test the functionality of the web interface used to collect survey responses. The FDIC thanks these 51 banks for giving generously of their time and expertise to the development of the final survey questionnaire.

Multiple divisions of the FDIC collaborated to complete this study. Staff from the FDIC's Division of Insurance and Research (DIR) led and coordinated the survey development, implementation, analysis, and writing. The primary authors of the report are DIR staff Jacob Goldston, Yan Y. Lee, and Smith Williams. Valuable research and analytical support were provided by DIR staff Claire Brennecke, Alexis Ercolino, Isabella Jaeger, Maria Hussain, Chet Polson, Benjamin Rodriguez, and Jeffery Traczynski. Karyen Chu of the Division of Depositor and Consumer Protection (DCP) and Jack Reidhill (DIR) provided invaluable insight and guidance throughout all phases of the project. Kris Rengert from DCP and Rae-Ann Miller and Suzy S. Gardner from the Division of Risk Management Supervision contributed to the survey development phase. A number of senior officials and staff provided helpful comments and suggestions on drafts of the report; from DIR, Fred Carns, Richard Brown, Phillip Shively, Rosalind Bennett, Stefan Jacewitz, and Jonathan Pogach, and from DCP, Keith Ernst.

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Diane Ellis
Director, Division of Insurance and Research

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EXECUTIVE SUMMARY

The survival and growth of small businesses depends on access to credit, and banks are the most common source of external credit for small firms. Nonetheless, very little comprehensive information is available about how small business lending is conducted by banks. Given the current consolidation trend in U.S. banking, it is essential to understand the practices that banks use to meet the needs of small businesses, and how these practices differ between banks of different sizes. In particular, the continued decline in the number of small banks and of bank branches (for banks of all sizes) may have significant negative effects on U.S. small businesses.

To fill this information gap, the Federal Deposit Insurance Corporation (FDIC) conducted the nationally representative Small Business Lending Survey (SBLS). High-quality data on the small business lending practices of U.S. banks were collected in 2016 and 2017. Approximately 1,200 banks responded to the survey—over one-sixth of all banks in the nation—yielding a 60 percent survey sample response rate. The survey design allows researchers to make inferences about the U.S. banking industry as a whole, as well as to draw distinctions between small and large banks.

At present, few surveys of bank small business lending exist, and none covers the range of topics captured by the SBLS. Further, most existing surveys cover only small banks and do not allow for comparisons between small and large banks, as the SBLS does. (This report defines banks with less than $10 billion in assets as small, and banks with at least $10 billion in assets as large.)

The SBLS collected information on banks' entire volume of commercial and industrial (C&I) lending by firm size and by residential real estate collateral, which enables the FDIC to provide direct evidence that small business lending by banks is currently understated. The findings of the survey show that the best available proxy for small business C&I lending substantially understates the amount of lending extended by banks to small businesses, especially by small banks.

In addition, the data collected by the SBLS confirm that small banks are indeed more likely to rely on relationship lending practices, while large banks are more likely to use transactional methods. Yet the results reveal that small business lending at all banks, regardless of bank size, is characterized by a core set of practices centering on local personal interactions. Thus, the survey's unique combination of findings provides depth and nuance to the current knowledge of small business lending.

The following detailed results support the conclusions of this report.

Banks Lend More to Small Businesses Than Is Currently Measured

The C&I Loan-Size Proxy Understates Lending in at Least Two Ways

- The best available measure of small business lending is a proxy based on loan size, but many loans made to small businesses are above the loan-size limit used ($1 million). For banks with between $1 billion and $10 billion in assets, over a fifth of their C&I lending above $1 million was made to businesses with under $1 million in revenue.
- The proxy also fails to capture small business lending secured by residential real estate. Yet 6 percent of lending by small banks for commercial and industrial purposes was secured by 1- to 4-family residential properties.

Conservative Extrapolations Show Substantial Understatement of Lending

- In 2015, small business C&I lending in the U.S. banking industry was understated by at least 12 percent ($37 billion).
- Small business C&I lending by small banks was understated by at least 29 percent.

A Core Set of Small Business Lending Practices Are Used By Banks of All Sizes

Relationships Are Important

- Both small and large banks most frequently cite relationships and personal attention as their top competitive advantages.
- Large majorities of both small and large banks are typically willing to grant exceptions to their underwriting policies based on existing loan and depositor relationships.

Practices Are High-Touch and Staff-Intensive

- Majorities of both small and large banks use high-touch, staff-intensive practices to maintain and generate small business lending relationships, and customer referrals are a focus for both sizes of banks.
- Small banks are more likely to focus on community involvement and personal attention, while large banks focus more on professional referrals and their own branch network.

Small Business Lending Primarily Occurs Locally

- A large majority of small banks define their small business lending trade areas locally, as do a substantial share of large banks.
- Almost all banks accept applications at branches; both sizes, but especially large banks, also accept applications during staff visits and over telephone calls.
- Very few small or large banks accept small business loan applications online.

Competition Is Focused on Local Banks

- Banks typically view a local bank of similar size as their most important competitor.
- Local banks of other sizes are also often considered to be frequent competitors, but nonlocal banks are rarely viewed as such.
- Credit unions and FinTech firms are emerging as competitors, but are not currently top competitors.

The Same Products and Underwriting Criteria are Generally Used

- The majority of both small and large banks offer a similar set of loan products, including lines of credit, letters of credit, and term loans.
- Small and large banks largely use similar underwriting criteria.
- Small and large banks typically accept the same types of collateral.

Small Banks are Relationship Lenders, Competitive in the Small Business Lending Market

Small Banks Are More Flexible in Characterizing Small Businesses and Engaging with Start-Ups

- Small banks use a diverse array of concepts to describe their small business customers, including qualitative attributes such as owner characteristics (e.g., “wears many hats”) and localness of the business (e.g., “involved in community”).
- Small banks evaluate a wide variety of additional criteria to qualify start-ups for loans, including evaluating owner characteristics (e.g., “education” or “experience in industry”).

Small Banks Are Perceived As Relational, Attentive, and Fast

- Small banks are more than three times as likely as large banks to be considered by competitors as having advantages in customer service.
- Small banks are almost four times as likely as large banks to be considered by competitors as being faster at making loans.

Local Small Banks Are Considered Top Competitors by Banks of Both Sizes

- Majorities of both small and large banks consider a local small bank with $1 to $10 billion in assets as one of their top three competitors, and about one-fifth of both sizes of banks consider such a bank to be their number one competitor.
- A third of large banks even consider one of the smallest local banks, those with $1 billion or less in assets, as a top three competitor for small business lending.

Large Banks Are Perceived to Be Convenient and Cheaper

- Large banks are more likely to be considered by competitors to have an advantage in providing convenience, particularly by having broad branch networks.
- Large banks are more likely to be considered by competitors to have an advantage in pricing, particularly in their ability to offer lower interest rates.

Large Banks Are More Transactional, with Perceived Advantages in Convenience and Pricing

Large Banks Use Quantifiable Metrics to Characterize Small Businesses and Look for Guarantees When Lending to Start-Ups

- Large banks use only a small number of quantifiable terms to describe their small business customers—in particular, firm revenue/sales or loan size. Four-fifths of large banks cite revenue/sales.
- The vast majority of large banks use additional criteria in lending to start-ups, citing a few specific ones; four-fifths of all large banks look for additional guarantees from new businesses, particularly SBA guarantees.

Large Banks Are More Likely to Use Transactional Practices

- The majority of large banks use formal limits to define small businesses, and they require minimum loan amounts. Large banks are more than four times as likely as small banks to evaluate business credit scores in underwriting.
- Large banks are more than three times as likely as small banks to offer credit cards, and more than seven times as likely to use standardized small business loan products.

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SECTION 1. Introduction

The survival and growth of small businesses depends on access to credit, and banks are the most common source of external credit for small firms.[1] Banks are able to provide this degree of financing because they have a special ability to identify creditworthy small businesses that often lack verifiable evidence of their quality.[2] Yet, despite the importance of banks to small businesses and the importance of small businesses to the larger economy, very little comprehensive information is available about small business lending by banks.[3] In particular, evidence is scarce about how banks define small business lending, what approaches they take to meet the needs of these customers, and whether small banks and large banks approach small business lending in significantly different ways.

The need for such information is important given the trends in the banking industry since the Great Recession. One such trend is consolidation: between 2008 and 2017 the number of small banks in the country dropped by nearly a third and small-bank assets dropped by more than 14 percent, whereas large banks increased their assets by 13 percent (in this report, small banks are defined as those with under $10 billion in assets, and large banks as those with at least $10 billion in assets).[4] Even so, at the end of 2017 small banks, though holding only 17 percent of banking assets, held nearly 53 percent of small loans to businesses (according to the Call Report measure for small business lending).[5] Another trend is the decline in the number of bank branches. In 2017 there were nearly 10 percent fewer branches in operation—for all sizes of banks—than there had been in 2008.

The critical question, then, is how the continuation of these trends is likely to affect the availability of credit to small businesses. The answer to that question requires a many-faceted answer to a different question: how do banks manage their small business lending, and in particular do small banks differ from large banks and are any such differences likely to affect small businesses?

The established understanding of small business lending is that small and large banks *do* differ in the practices they use, the geographic areas they serve, and the types of information on which they

1 On the need for access to credit, see Titan Alon et al., "Older and Slower: The Startup Deficit's Lasting Effects on Aggregate Productivity Growth," *Journal of Monetary Economics* 93 (2018): 68–85, https://doi.org/10.1016/j.jmoneco.2017.10.004; and Thorsten Beck, Asli Demirgüç-Kunt, and Vojislav Maksimovic, "Financial and Legal Constraints to Growth: Does Firm Size Matter?" *Journal of Finance* 60, no.1 (2005): 137–77. On the role of banks, see Federal Reserve System, "Report on Employer Firms," *Small Business Credit Survey*, April 2017. https://www.newyorkfed.org/medialibrary/media/smallbusiness/2016/SBCS-Report-EmployerFirms-2016.pdf; and Federal Reserve Bank of Cleveland. *2016 Small Business Credit Survey Report on Microbusinesses: Nonemployer and Small Employer Firms.* November 2017. https://clevelandfed.org/global%20search?q=2016+Small+Business+-Survey%3A+Report+on+Microbusinesses%3A+Nonemployer+and+Small+Employer+Firms.+Published+November+2017.+Federal+Reserve+Bank+of+Cleveland.

2 On the advantages of banks relative to other external credit options, see Gregory Udell, "What's in a Relationship? The Case of Commercial Lending," *Business Horizons* 51 (2008): 93–10.

3 On the importance of small businesses to the U.S. economy, see U.S. Small Business Administration, Office of Advocacy, *Frequently Asked Question (2017),* https://www.sba.gov/sites/default/files/advocacy/SB-FAQ-2017-WEB.pdf.

4 For a full description of the structural changes in the industry, see Federal Deposit Insurance Corporation, *FDIC Community Banking Study,* December 2012, https://www.fdic.gov/regulations/resources/cbi/report/cbi-full.pdf; and Eric C. Breitenstein and Nathan Hinton, "Community Bank Mergers since the Financial Crisis: How Acquired Community Banks Compared with Their Peers," FDIC Quarterly 11, no. 4 (2017): 41–52, https://www.fdic.gov/bank/analytical/quarterly/2017-vol11-4/fdic-v11n4-3q2017-article2.pdf.

5 The Call Report measure is the sum (reported to regulators) of outstanding small commercial and industrial loans, small commercial real estate loans, and small agricultural and farmland loans. See the box at the beginning of Section 2 for a discussion of the small business lending captured by regulatory Call Reports.

base their decisions (see the box for detail on these differences). One implication is that the continued decline of small banks could have significant adverse effects on access to credit by these banks' small business customers even if large banks continued to operate in the affected geographic area. This concern is most acute for firms that have little quantifiable evidence of their creditworthiness—most notably, start-ups. Although some evidence exists that is consistent with the established view of differences between small and large banks, no nationally representative survey has asked banks of all sizes to describe how they conduct small business lending, making it difficult to understand the possible implications of these practices for small businesses' access to credit in the future.

To fill this knowledge gap, the Federal Deposit Insurance Corporation recently conducted the Small Business Lending Survey (SBLS) to collect

RELATIONSHIP LENDING AND TRANSACTIONAL LENDING

The consensus explanation for banks' centrality to small business finance is that banks have a unique ability to generate information that allows them to identify the high-quality small firm and, by extension, the profitable small business loan.[a] Although all banks are thought to use a variety of methods to identify high-quality small businesses, small and large banks are widely considered to hold distinct advantages in how they generate information. As a result, small and large banks are expected to manage their small business lending programs differently.

Specifically, small banks are regarded as having a comparative advantage in gathering and using "soft" information—knowledge of both the local community and the small businesses within it—which the bank has accumulated over multiple interactions, and which is hard to quantify or transmit. Small banks are typically located within the communities they serve, which therefore lowers the transaction costs of engaging with and monitoring the firm or of gathering knowledge of the local market. Further, small banks are usually closely held organizations with few managerial layers between bank owners and loan officers, so that the loan officer may be more motivated to gather and use soft information when deciding whether to grant a business loan.[b] Small banks are therefore considered more flexible and able to engage with small businesses on a case-by-case basis. It is for these reasons that small banks as a group are believed to specialize their commercial and industrial lending to small businesses and are typically called relationship lenders.

Large banks are regarded as taking advantage of economies of scale to gather and use large amounts of quantifiable, or "hard," information about the borrower. This reliance on hard information requires that bank management specify the types of data used as well as the metrics for determining small business quality, usually well before any business applies for a loan. Further, since the information used by large banks is quantifiable, it can be submitted and shared electronically, which may reduce the need for the large bank decisionmakers to be in close proximity to the small business. This structure facilitates a high-volume small business lending model, and is often referred to as transactional lending.

[a] Udell, "What's in a Relationship?"

[b] Allen N. Berger and Gregory F. Udell, "Small Business Credit Availability and Relationship Lending: The Importance of Bank Organisational Structure," *Economic Journal* 112, no. 477 (2002): 32–53; and Jeremy C. Stein, "Information Production and Capital Allocation: Decentralized versus Hierarchical Firms." *Journal of Finance* 57, no. 5 (2002): 1891–921, https://doi.org/10.1111/0022-1082.00483.

high-quality data on the small business lending practices of a large, nationally representative sample of U.S. banks. The survey had a sample response rate of 60 percent, with approximately 1,200 banks, or more than one-sixth of all banks in the country, responding. The answers given to the questions have been weighted to reflect the whole population of U.S. banks. There are currently few other surveys of small business lending that survey banks, and these other surveys include convenience samples of only small banks, which prevents comparison between different-sized banks; these other surveys also cover fewer topics.[6] The SBLS is the only survey able to provide nationally representative findings that reflect a broad view of the practices of the entire industry, including both small and large banks.

The survey instrument was developed in consultation with experts at the U.S. Census Bureau and benefited from suggestions by more than 40 banks of all sizes across the United States; these banks agreed to provide feedback on draft versions of the survey in one-on-one interviews throughout 2015.[7] The survey, which was conducted between June 2016 and January 2017, captured information about banks' experiences in the calendar year 2015.

The survey questions covered the following subject areas:

- Banks' characterizations of their small business borrowers
- The volume of C&I lending to small businesses that is not captured in current bank reporting to regulators
- Banks' market area and their competitive environment for small business lending
- Competitive practices and advantages
- Loan products offered and underwriting practices, including for loans to start-ups.

The answers given in the first two areas allow the survey to make a particularly significant contribution to the measurement of small business lending. As explained in Section 2 of this report, the standard loan-size measure for small business C&I lending does not fully correspond to banks' own definitions of what is a small business and what is small business lending, and therefore the standard measure is unable to capture substantial portions of such lending. The survey has made it possible to quantify two missing portions. Thus, the findings from the survey provide policymakers, bankers, and academics a better understanding of aspects of small business lending by banks that is currently understated.

6 See Federal Reserve System and Conference of State Bank Supervisors, Community Banking Research and Policy Conference, October 4–5, 2017, *Community Banking in the 21st Century 2017*, https://www.communitybanking.org/~/media/files/cb21pub_2017_book_web.pdf; and Jeff Bajek, "RMA Survey: Trends in Small Business Lending at Community Banks," *RMA Journal*, March 2017, https://www.rmahq.org/ProductDetail.aspx?productid=491302131. Both publications report on surveys that use convenience sampling rather than random sampling. An exception is the Federal Reserve Bank of Kansas City's newly launched *KCFed Small Business Lending Survey*, April 2, 2018, https://www.kansascityfed.org/~/media/files/publicat/research/indicatorsdata/smallbusiness/2018/1stquarter/smallbusinesslendingsurvey04-02-18.pdf?la=en, which uses a nationally representative sample that includes large banks but has a narrower focus on the terms of lending offered by banks to small businesses. There are also current surveys of small business owners about their credit needs and experiences, which use either convenience samples or focus on a small set of firms. For examples of a small business owner surveys, see Federal Reserve System, "Report on Employer Firms," *Small Business Credit Survey*, April 2017, https://www.newyorkfed.org/medialibrary/media/smallbusiness/2016/SBCS-Report-EmployerFirms-2016.pdf or DesRoches, David and Potter, Frank and Santos, Betsy and Sengmavong, Ae and Zheng, Yuhong, "Kauffman Firm Survey (KFS) Seventh Follow Up Methodology Report," June 28, 2013, https://ssrn.com/abstract=2286725.

7 The survey development phase involved three rounds of interviews with institutions in both rural and urban areas and in ten states. See Appendix A for details on sampling methodology, survey development, and survey validation; see Appendix B for a discussion of the extrapolation methodology used to generate estimates, presented in Section 2, of small business lending by banks that is understated in current regulatory reports; see Appendix C for the full survey instrument.

The answers given in the remaining areas all relate to the approaches that banks take toward small business lending, and provide direct evidence on the differences between small and large banks. Sections 3, 4, and 5, each in its separate subject area, provide evidence in support of the established understanding, but they also show that, in practice, the differences between the approaches taken by the two sizes of banks involve many nuances. Although small and large banks do emphasize distinct aspects of small business lending, a core set of practices centering on locally-based personal interactions characterizes much of small business lending regardless of bank size.

Sections 3, 4, and 5 report the survey findings in detail, by bank size, with Section 3 focusing on the environment for banks (market areas and competitors), Section 4 looking both within and without (competitive practices and perceptions of advantages), and finally, Section 5 focusing on the bank itself (loan products offered and underwriting practices). Each of these sections specifies the topic to be addressed and its rationale, describes the survey findings, and concludes by briefly discussing implications for small businesses' future access to credit.

SECTION 2.
Defining and Measuring Small Business Lending

Despite the importance of small businesses to the U.S. economy and the importance to small businesses of credit received from banks, there is no comprehensive measure of bank small business lending. The best quantitative measure available consists of the amount of outstanding small loans to businesses and farms that banks report on their quarterly Call Reports to regulators (see box). The Call Report uses specific definitions that are standard across banks and across time periods. Moreover, the definitions result in numbers that are accurate for what they are counting and are frequently used by regulators, bankers, and academics to describe and study small business lending. However, the strength of this measure—consistency across banks—is precisely why it likely misses important parts of small business lending: banks' definitions of small business lending may differ from one based solely on a specific loan size, and as a result, some small business lending may not be captured by regulatory reports. This section uses the survey findings to answer two important questions: First, what size businesses and what size loans do banks themselves consider to be small, and in that regard, do small and large banks differ? Second, is small business lending by banks as measured by the Call Report understated and, if so, to what extent?

Specifically, this section investigates the small commercial and industrial (C&I) loans to businesses captured by the Call Report, defined as outstanding C&I loans of $1 million or less at the time of origination. This report refers to this component of the Call Report as the "Call Report proxy" for bank small business C&I lending. While most policymakers, bankers, and academics would agree that firms receiving loans under the $1 million mark are small, the concern is that the proxy fails to pick up C&I loans of *more than $1 million* made to businesses that the banks themselves categorize as small. Therefore, the survey explores whether banks have varied definitions of small business lending that deviate from the loan-size definition used by the proxy. Another significant concern is that the definition of small business lending used in the Call Report excludes any lending secured by residential real estate, even though banks commonly accept personal real estate as collateral for small business loans (as is shown in Section 5). The box referred to above provides a richer explanation of the Call Report and the types of loans it covers under small business lending.

2.1 Defining Small Business Borrowers: Banks' Approaches

This subsection explores whether banks have varying definitions for whom they consider to be small business borrowers, and whether these definitions differ from the $1 million limit of the loan-size proxy. In particular, the coexistence in the U.S. banking industry of both small and large banks (those with assets under $10 billion and those with assets of $10 billion and over, respectively) suggests that any quantitative measure such as the proxy may coincide more with some banks' definitions than with others'. To provide insight into the variations among banks in this regard, the survey asked banks to describe their small business customers and specify whether there are certain limits by which they define small business customers and loans.

One might expect that a bank's approach to lending would affect its perception of its small business borrowers. For example, if small banks as a group are relationship lenders, as they are commonly believed to be, then individual small banks are more likely to develop a fuller picture of their borrowers by taking into account qualitative information in

The Call Report Measurement of Small Business Lending by Banks

"Call Report" refers to the Consolidated Report of Condition and Income that every U.S. bank is required to submit to regulators each quarter. The instructions for Schedule RC-C Part II define loans to small businesses and small farms as the sum of (a) the outstanding commercial and industrial (C&I) loans of $1 million or less at the time of origination, (b) the outstanding commercial real estate loans with origination amounts of $1 million or less, and (c) the agricultural production and farmland loans of $500 thousand or less. The FDIC's Small Business Lending Survey focused exclusively on small business C&I lending captured in (a), which in this report is referred to as the "Call Report proxy" (or "loan-size proxy").

The quantitative limit of the Call Report proxy with regard to C&I lending reflects the assumption that the borrowers of loans under $1 million are businesses that are small. Because of the high correlation between loan size and business size, in the early 1990s regulators adopted the $1 million loan limit as a proxy definition of small business. However, since that time, the limit has never been adjusted for inflation; if it had been, in December 2015 it would have been over $1.6 million.[a] As a result, the probability is high that loans of greater than $1 million are extended to small businesses but are not captured by the proxy.

The proxy uses loan size as the criterion rather than borrower size because all banks track loan size but not all banks track business size.[b] The value of using information that banks already record was reaffirmed during the survey development phase, when FDIC researchers visited 40 banks of various sizes, serving various geographic markets across the United States, to discuss their ability to provide the information sought. The initial draft of the survey contained multiple questions asking banks to provide data on C&I loans by both purpose and size of firm. The interviews, however, revealed that many banks, particularly smaller ones, do not track much information in their core data systems about the borrower other than loan amount for the small business loans. As a result, many were not able to report loans by size of small business (for example, as measured by firm gross annual revenue) without substantial investments of staff resources.

Aside from limiting "small business lending" by dollar amount, the proxy places a nonquantitative restriction on what is included under small business C&I lending. Loans secured by real estate are recorded in the Call Report by their primary collateral rather than by purpose, and the Call Report therefore considers a business loan secured by a 1- to 4-family residential property to be a home mortgage rather than a business loan, even if the purpose is to support the operations of a small business. Thus, the Call Report small business loan proxy does not capture small business loans that are collateralized by the owner's residence.[c]

[a] Calculations are based on the Consumer Price Index for All Urban Consumers (CPI-U) of the Bureau of Labor Statistics.

[b] See 57 Fed. Reg. 54165 (Nov. 17, 1992) 54235-54239. https://cdn.loc.gov/service/ll/fedreg/fr057/fr057222/fr057222.pdf.

[c] The survey questions did not focus on the two other Call Report components that capture other lending that supports the operations of small businesses: (b) commercial real estate loans with originations less than or equal to $1 million, and (c) agricultural production and farmland loans with origination amounts less than or equal to $500,000.

addition to quantitative measures. By contrast, if large banks as a group are transactional lenders, as they are commonly believed to be, then individual large banks are more likely to view small business borrowers in more strictly quantitative terms in order to quickly compare the borrower's information with the predetermined quantitative limits set for specific loan programs. This difference in approach could lead to substantial differences in what the two sizes of banks consider to be their small business customers and their small business loans.[8] As Figure 2.1 illustrates, there are in fact substantial differences between small and large banks in how they describe their small business customers.

Figure 2.1 shows the shares of small banks and large banks that describe their small business borrowers using answers that fall within one or another of ten broad categories.[9] The particular survey question was an open-ended one asking banks to describe their small business borrowers. Large banks generally describe their small business borrowers in terms of specific financial characteristics, especially revenue or sales, whereas small banks display much greater diversity of opinion about what makes a business "small." Here and throughout this report, differences discussed between different sizes of banks are statistically significant at the 10 percent level at least, and typically at higher levels of precision than 10 percent.

As the figure indicates, the overwhelming majority of large banks (78.9 percent) use revenue or sales to characterize their small business borrowers, and some also mention loan size or aggregate loan exposure (26.9 percent and 21.0 percent) as a defining feature of small businesses. Large banks limit their descriptions to a few key, measurable financial concepts, which is consistent with a more quantitative—or transactional—approach to small business lending.

Although revenue or sales is the most commonly referenced concept for small banks, more than half of small banks do *not* consider revenue or sales in their description of their small business customers. Further, only very small shares of small banks consider loan size or loan exposure to be a defining feature of their small business borrowers. Instead, over a quarter (26.1 percent) of small banks see ownership structure (for example, whether a company is owner operated, closely held, or a "mom-and-pop shop") as an important defining feature of small businesses. In addition, between 10 and 20 percent of small banks discuss number of employees, business focus (for example, if the business has a "local footprint," is "involved in the community," or needs "personal attention"), or owner characteristics (for example, if the owner is "local" to the community, "wears many hats," or is active in daily operations).

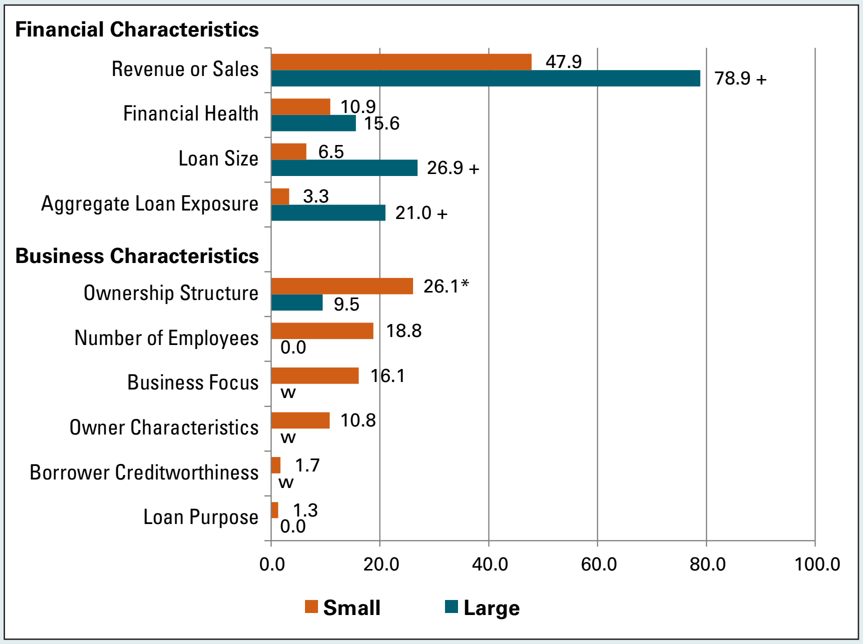
The differences between small and large banks in how they define their small business customers are further illustrated by their responses to specific survey questions asking about their use of either aggregate loan exposure (ALE) or gross annual revenue (GAR) as quantitative limits for defining small businesses. Figure 2.2 shows the shares of small and large banks that indicate they use such limits. The responses are analogous to the open-ended responses that described their small business borrowers: a substantial majority of large banks use either aggregate loan exposure (70.3 percent) or gross annual revenue (61.8 percent) as a limit to define small businesses, whereas only 20.4 percent of small banks define small businesses by a GAR limit and an even smaller share (14.7 percent) use an ALE limit.

Small banks' lack of reliance on strict firm-revenue limits combined with their use of more diverse and generally less quantifiable concepts to describe their small business customers suggests that small banks have a more varied view of their small business borrowers, consistent with a greater reliance on relationship lending methods. The heavy use of limits by large banks, particularly ALE limits, suggests that the current Call Report definition of small business C&I lending by loan size may be more in sync with these banks, provided the proxy is close to the limits they use.

8 For a fuller discussion of the differences between relationship and transactional small business lending, see the box in Section 1.

9 More than 50 distinct concepts were mentioned that were aggregated into these 10 categories. In addition to describing their small business customers, some banks also referenced characteristics of their own bank in the response, or responded that all (or none) of their business lending is to small businesses.

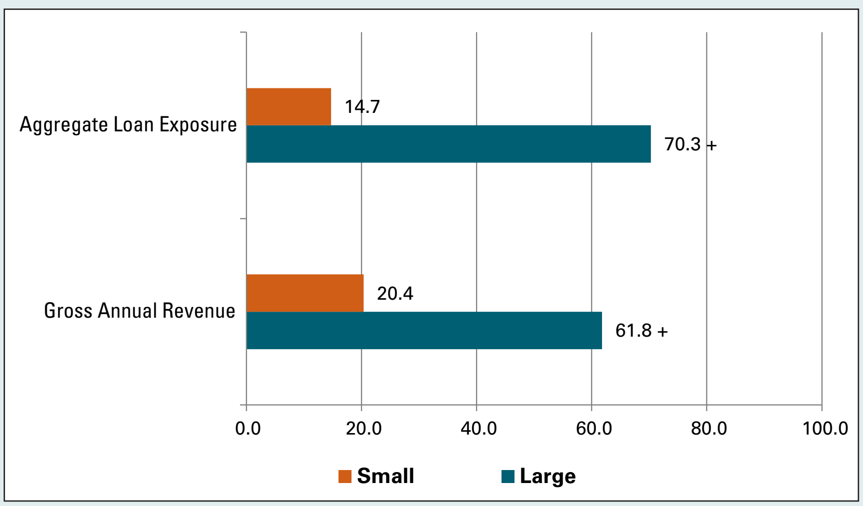
Figure 2.1: Percentage of Banks That Reference These Characteristics When Describing Small Business Borrowers



Source: SBLS Question 1.

Notes: Entries marked with a "w" indicate that the number of responses falls below the allowable reporting threshold for protecting respondents' identities. At the statistical significance of 10 percent, "*" denotes that small banks are more likely than large banks to use this characteristic to describe small business borrowers; "+" that large banks are more likely than small banks. "Characteristics" categories aggregate individual bank responses to an open-ended question; results will not sum to 100.0 percent.

Figure 2.2: Percentage of Banks That Use a Maximum Allowable Limit for Either of These Financial Measures to Define Small Business Lending



Source: SBLS Questions 3 and 4.

Notes: At the statistical significance of 10 percent, "+" denotes that large banks are more likely than small banks to use this maximum allowable limit to define small business.

Therefore, to compare how well banks' quantitative limits coincide with the proxy limit of $1 million, the survey investigated the sizes of the limits banks use in practice. The results appear in Figure 2.3. For the banks that use ALE limits, Panel A reports the shares of small and large banks that use one or another of three particular dollar limits. The fact that the limits used are often lower than or equal to the $1 million used by the Call Report proxy suggests that for banks that do use ALE limits, the proxy definition is a reasonable approximation of their practices. Specifically, of the banks that use limits, nearly 70 percent of small banks and nearly 60 percent of large banks use a limit equal to or less than $1 million. However, of the large banks that use an ALE limit—and large banks are those most likely to use ALE to define small business lending—a substantial share (41.8 percent) set their ALE limit above $1 million, which indicates that there is small business lending made by banks which is not fully captured by the Call Report proxy.[10]

The survey results also show that of banks that use a GAR limit to define a small business, nearly all use a limit of $1 million or more. Figure 2.3, Panel B, shows that of small banks that use a GAR to define a small business, only 6.1 percent set their maximum limit below $1 million, and of large banks, none do. Panel B also shows that of banks that use a GAR limit, majorities of both sizes set it above $1 million. Therefore, nearly all banks that use a GAR limit to define a small business agree that at least businesses with a GAR of $1 million or less are small businesses. In fact, 27.1 percent of small banks and 56.4 percent of large banks that use a GAR limit even set it at $5 million or more.

2.2 Measuring Small Business Lending (I): Loans That Exceed the Proxy Limit

As just noted, the definitions that banks set for small business loans are often paired with amounts that are above the $1 million limit of the Call Report proxy. This loan amount discrepancy between banks' practices and the proxy is a potential source of the proxy's understatement of small business lending. To explore this source of potential understatement, the survey asked banks about the quantity of outstanding loans of different origination amounts made to businesses of different sizes, as measured by the businesses' GAR. The information is used to calculate the fraction of C&I loans *above* the proxy limit that are made to businesses considered to be small. Because of data constraints, results can be reported only for banks with $1 billion to $10 billion in assets.[11]

The survey finds (as just noted, only for banks with $1 billion to $10 billion in assets) that a substantial share of the outstanding C&I loans greater than $1 million—loans not captured by the proxy—are made to businesses with GAR of $1 million or less that are generally understood to be small (Figure 2.3, Panel B, shows that virtually all banks that use GAR limits use one of $1 million or above). Figure 2.4 presents, for Q4 2015, the ratio of outstanding C&I loans originated at amounts greater than $1 million allocated by the borrower's GAR, to total outstanding C&I loans originated at amounts greater than $1 million. For these banks, 21.2 percent of all loans originated at amounts greater than $1 million are made to businesses with a GAR of $1 million or less. An additional 38 percent of these loans are made to businesses with a GAR of between $1 million and $10 million. Given that the GAR limits used by some banks to define small businesses are above $1 million, it is very likely that the share of loans over $1 million made to businesses with a GAR of between $1 million and $10 million also includes loans to small businesses. Thus, for banks with assets between $1 billion and $10 billion, at least one-fifth and possibly more than one-half of the loans they originated above the proxy limit are actually made to small businesses.

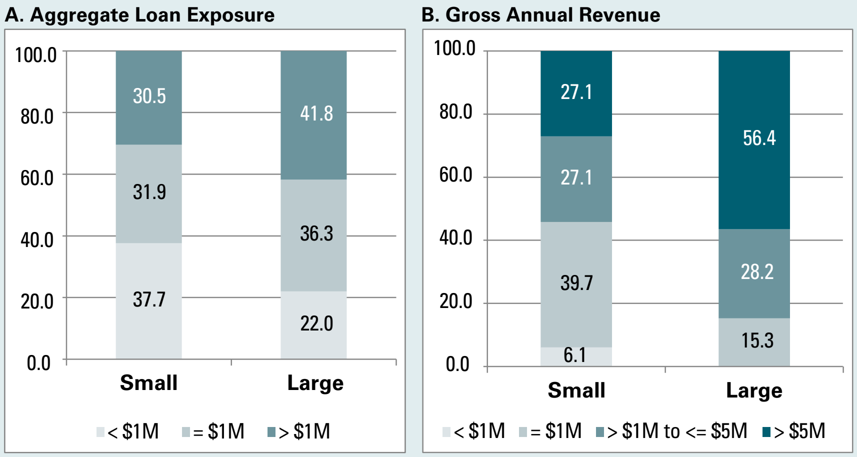
2.3 Measuring Small Business Lending (II): Loans by Banks That Specialize Their C&I Loans to Small Businesses

Small business lending at amounts over the $1 million mark made by banks with under $1 billion in assets was explored as well. The established understanding of small business lending is that small banks (banks with assets under $10 billion) focus most of their C&I lending on small businesses. This may be partly because the relationship lending orientation of small banks gives them an informational advantage in small business lending, compared with large banks. In addition, very small banks may not have the resources to meet the credit needs of larger businesses without taking on excessive risk. Thus, if these banks indeed lend

[10] It should be noted, however, that slightly over one-fifth of large banks that use an ALE limit use limits under $1 million, which could potentially indicate overreporting of small business lending.

[11] Because of the limitations of the core data systems at most banks with less than $1 billion in assets, only banks with more than $1 billion in assets were asked these questions in the survey. Unfortunately, however, the number of banks with assets greater than $10 billion that answered these questions falls below the reporting threshold for protecting respondents' identities.

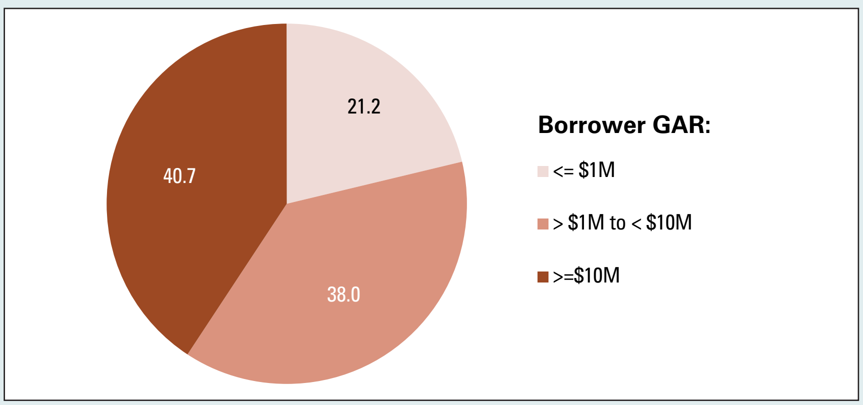
Figure 2.3: Percentage of Banks That Use These Limits to Define Small Business Lending



Sources: SBLS Questions 3A and 3B.

Notes: Banks that responded "yes" to using maximum allowable limits for either of these two measures in order to define small business lending were asked the amount of the limit they used. At the statistical significance of 10 percent, small banks are more likely than large banks to use an aggregate loan exposure (ALE) limit of less than $1 million and to use a gross annual revenue (GAR) limit of exactly $1 million; large banks are more likely than small banks to use a GAR limit of greater than $5 million.

Figure 2.4: Percentage of Total Outstanding C&I Loans of $1 Million or More at Origination, by Borrower's Gross Annual Revenue, 2015 Q4
(Banks with $1 Billion to Less Than $10 Billion in Assets)



Source: SBLS Question 14.

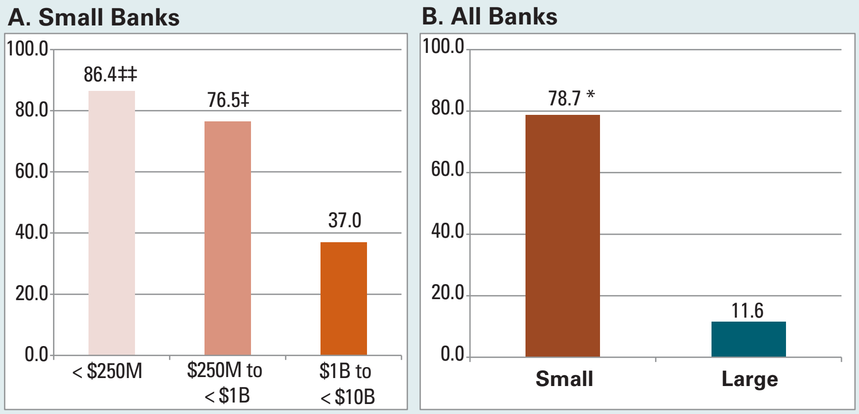
Notes: Question 14 was asked only of banks with assets of greater than $1 billion, because of the limitations of core data systems encountered at smaller banks during the survey development phase. However, the number of responses from banks with assets greater than $10 billion falls below the allowable reporting threshold for protecting respondents' identities.

almost exclusively to small businesses, the loan-size proxy would understate small business lending at small banks—and in fact, the Call Report shows that over one-half of outstanding C&I loans in Q4 2015 made by banks with less than $1 billion in assets were originated at amounts greater than the proxy limit of $1 million. To provide insight into this possible source of understatement by the proxy, the survey included a simple yes or no question, answered by banks of all sizes, on whether the bank considers "largely all" of its C&I lending in 2015 to have been made to small businesses.[12]

The established understanding that small banks specialize in small business lending is supported by the findings of the survey, which show that an overwhelming majority—86.4 percent—of the smallest banks (banks with less than $250 million in assets) make C&I loans almost exclusively to

[12] The wording of this question was informed by the discussions with the 40 banks interviewed during the survey development phase. Few were willing to respond affirmatively to a question that asked if "all" of their C&I lending was to small businesses because they were concerned that there might be a small number of loans that did not fit their small business definition and they did not want to misrepresent themselves to a bank regulator. Modifying the question using the words "largely all" instead of "all" assuaged the banks' concerns.

Figure 2.5: Percentage of Banks That Make "Largely All" of Their C&I Loans to Small Businesses



Source: SBLS Question 2.

Notes: At the statistical significance of 10 percent, "‡‡" denotes that banks with less than $250 million in assets are more likely than banks with $250 million to less than $1 billion in assets and more likely than banks with $1 billion to less than $10 billion in assets to make "largely all" of their commercial and industrial (C&I) loans to small businesses; "‡" that banks with $250 million to less than $1 billion in assets are more likely than banks with $1 billion to less than $10 billion in assets; "*" that small banks are more likely than large banks.

small businesses (see Figure 2.5). Of banks with assets between $250 million and $1 billion, more than three-quarters (76.5 percent) also say that their C&I loans are almost exclusively to small businesses. On the basis of these results, one simple way to comprehensively capture small business lending by banks with assets of less than $1 billion would be to count their entire C&I loan portfolio, regardless of the size of the original loan amount.[13] Doing so would have increased by around 75 percent the amount of small business lending reported for these banks in the Q4 2015 Call Report proxy.[14]

Larger small banks (banks with assets between $1 billion and $10 billion) are much less likely to be as overwhelmingly small-business oriented in their C&I lending. Although a substantial share (37.0 percent) of these banks do make largely all their C&I loans to small businesses, that constitutes a 40 percentage point or more drop compared with the smaller banks. Overall, 78.7 percent of small banks make largely all their C&I loans to small businesses. The contrast with large banks (those with $10 billion or more in assets) is not surprising: only a small share (11.6 percent) makes largely all their C&I loans to small businesses. As banks grow in size, the decreasing shares of banks that focus their commercial lending on small businesses is consistent with the established understanding that smaller banks specialize their C&I lending to small businesses.

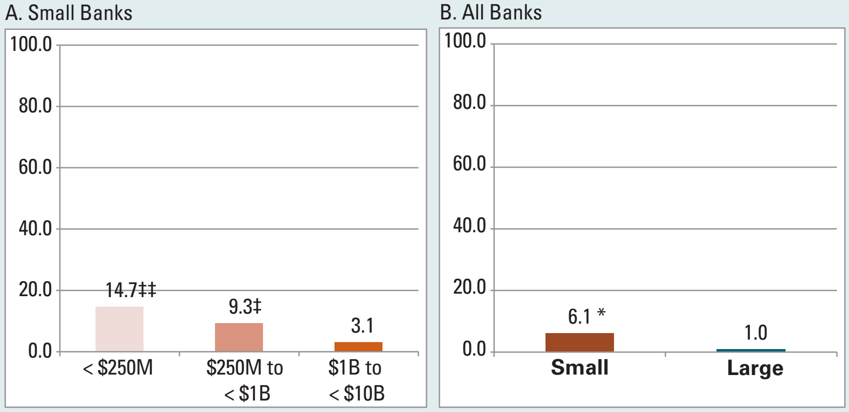
2.4 Measuring Small Business Lending (III): Loans Secured by Residential Mortgages

A second potential source of the proxy's understatement of small business lending involves the use of residential mortgages to secure small business loans. The Call Report small business C&I loan proxy does not capture small business loans that are collateralized by the owner's residence. Loans secured by real estate are recorded in the Call Report by their primary collateral rather than by purpose. Thus, the Call Report considers a loan secured by a 1- to 4-family residential property to be a home mortgage rather than a business loan, even if the purpose is to support the operations of a small business. The survey provides an opportunity to investigate any understatement of small business

13 Note, however, that this simple method is not used in the extrapolations presented in Section 2.5. That section is focused on extrapolating a lower bound of the understatement of small business lending by the proxy, and therefore a more conservative method was used.

14 Specifically, the Q4 2015 Call Report shows that the *combined* outstanding C&I loans for all banks with assets less than $1 billion totaled $108.7 billion; of that amount, $46.8 billion was originated above $1 million and $61.9 billion below $1 million.

Figure 2.6: Percentage of Total C&I Originations Secured by 1- to 4-Family Residential Properties



Source: SBLS Questions 8 and 9.

Notes: At the statistical significance level of 10 percent, "‡‡" denotes that banks with less than $250 million in assets are more likely than banks with $250 million to less than $1 billion in assets and more likely than banks with $1 billion to less than $10 billion in assets to have their total C&I loans to small businesses be secured by 1- to 4-family residential properties; "‡" that banks with $250 million to less than $1 billion in assets are more likely than banks with $1 billion to less than $10 billion in assets; "*" that small banks are more likely than large banks.

lending that may be due to the use of personal real estate as collateral.[15]

Personal residential property is in fact an important source of collateral for small business lending. For many households, the most valuable asset is a home, and the equity may be used by small business owners to secure a business loan.[16] There is evidence, both in the survey and elsewhere, that for banks and small businesses alike, the acceptance (by banks) and use (by small businesses) of 1- to 4-family residential properties for collateral is common. Section 5 of this report shows that a majority of banks, particularly small ones, commonly accept 1- to 4-family residential properties as collateral for small business loans, and other studies estimate that over one-third of small businesses use personal assets to secure loans.[17]

For small banks—and particularly for the smallest of the small—the findings of the survey show that C&I loans secured by 1- to 4-family residential properties are an important part of the overall C&I portfolio. Banks of all sizes were asked for the volumes of their total C&I originations and for their C&I originations secured by 1- to 4-family residential properties for the calendar year 2015. Figure 2.6 presents the ratio of C&I originations secured by 1- to 4-family residential properties to total C&I originations, which indicates whether the proxy may not capture small business C&I lending for the reason that the loan is secured with personal residential collateral. Overall, just over 6 percent of the C&I loan originations made by small banks are secured by 1- to 4-family residential properties. Such loans make up a much smaller part of large banks' C&I lending—only 1 percent.

Among all small banks, the use of 1- to 4-family residential properties as small business lending collateral is correlated with size: those loans make up nearly 15 percent of the C&I portfolio of banks with less than $250 million in assets, but only 3.1 percent of the portfolio of banks with $1 to $10 billion in assets. This relationship between bank size and C&I lending secured by 1- to 4-family residential properties likely reflects the findings presented above that the smallest banks are more likely than larger small banks to specialize their C&I lending to small businesses. In addition, as discussed further in

[15] In this report, all C&I loans that are secured by 1- to 4-family residential properties are assumed to be loans to small businesses, on the basis that large firms are not considered likely to use these assets as collateral.

[16] See tables 5 and 8 of Federal Reserve System, Board of Governors, *2016 Survey of Consumer Finances,* https://www.federalreserve.gov/econres/files/scf2016_tables_public_real_historical.xlsx.

[17] See Federal Reserve System, "Report on Employer Firms," *Small Business Credit Survey*, April 2017, https://www.newyorkfed.org/medialibrary/media/smallbusiness/2016/SBCS-Report-EmployerFirms-2016.pdf.

Section 5, small banks (banks with assets under $10 billion) are somewhat more likely than large banks to accept personal real estate as collateral for small business lending.

2.5 Extrapolating a Lower Bound on the Proxy's Understatement of Small Business Loans

As the introduction to this section explains, the survey investigates whether the best available measure of small business C&I lending—the Call Report proxy—understates actual bank lending to small businesses in two ways. The survey results show, first, that the proxy does not capture loans to small businesses that are originated at amounts above $1 million and, second, that it does not capture loans that are secured by residential real estate. To extrapolate a lower bound for the understatement produced by these two exclusions from the proxy, the survey's nationally representative estimates are combined with the Q4 2015 Call Report amounts of bank C&I lending.[18] It should be noted that since outstanding loans are a stock measure, the Q4 figures reflect all outstanding C&I loan dollars for a bank at that moment in time.[19]

As discussed in Section 2.2, of the outstanding C&I loans originated at amounts above $1 million by banks with assets between $1 billion and $10 billion, at least one-fifth were made to small businesses—that is, businesses with GAR of $1 million or less, which by common agreement are considered small businesses. These loans are not captured by the proxy because they are above the proxy's dollar limit of $1 million. Extrapolations presented on Table 2.1 using survey results and the Q4 2015 Call Report indicate that the lower bound of the small business lending understatement caused by not counting outstanding loans originated above $1 million that are made to businesses with GAR of $1 million or less—by banks with assets between $1 billion and $10 billion—is at least *$19.1 billion*. It should be noted that businesses with GAR of *greater* than $1 million that receive outstanding C&I loans originated with amounts greater than $1 million can also be small businesses, but the level of fineness of the information collected in the survey does not allow for the calculation of this potential understatement.

In addition, the survey results discussed in Section 2.3 show that the vast majority of the small banks with assets of under $1 billion specialize their C&I lending to small businesses. These are the banks with assets of less than $250 million and with assets of between $250 million and $1 billion. Of these banks, 86.4 percent and 76.5 percent, respectively, consider largely all of their C&I lending to be to small businesses. For these banks as for all banks, C&I loans originated at amounts of less than $1 million are included in the proxy as small business lending, yet the C&I loans originated at amounts above $1 million are not. Combining the survey results and the Q4 2015 Call Report, Table 2.1 shows that the lower bound for the understatement of loans originated above $1 million made by the two groups of the smallest banks is extrapolated to be $60.2 million for banks with fewer than $250 million in assets, and $32.3 million for banks with assets between $250 million and $1 billion. The understatement is therefore extrapolated to be at least $92.5 million in total for banks with assets of less than $1 billion.[20]

The second source of understatement by the Call Report proxy, as discussed above in Section 2.4, is that 1- to 4-family residential properties secure a nontrivial share of C&I loan originations,

18 For the reader's convenience, the details of how the extrapolations are calculated are provided in Appendix B.

19 "Stock" values are snapshot values observed at a point-in-time, such as current assets and current liabilities.

20 The lower bound extrapolation is substantially more conservative than an extrapolation using the simple method of counting as small business lending all C&I loans made by these banks, regardless of origination amount, as discussed in Section 2.3. The conservative method used in this subsection is discussed in Appendix B. If instead the simple method is applied to the bottom 86 percent of banks with assets of less than $250 million, when ranked by total C&I lending, and the bottom 76 percent of banks with assets of between $250 million and $1 billion, then the Q4 2015 Call Report shows that their combined C&I lending for loans with origination amounts above $1 million was $16.9 billion, which generates a substantially larger potential understatement than the one yielded by the conservative method.

Table 2.1: Dollar Amount Understatement of Call Report Proxy for Small Business Lending, 2015 (Extrapolated Lower Bound)

Areas of Understatement	Small Banks			All Banks		
	<250M	250M to <1B	1B to <10B	Small	Large	Total
Unsecured C&I Loan Dollars with Origination Amounts of Greater $1 Million to Businesses with Gross Annual Revenues of: $1 Million or Less	$60.2M	$32.3M	$19.1B	$19.2B	Not Available[ψψ]	$19.2B
Greater than $1 Million			Not Available[ψ]		Not Available[ψ]	
Secured by 1- to 4-Family Residential Properties, Actually for C&I Loan Purposes	$4.4B	$6.5B	$4.8B	$15.6B	$2.7B	$18.3B
Total	**$4.5B**	**$6.6B**	**$23.9B**	**$34.8B**	**$2.7B**	**$37.5B**

Notes: [ψ] Extrapolations for the lower bound of the part of the understatement of small business loans that is due to the proxy's exclusion of loans with origination amounts of greater than $1 million to businesses with gross annual revenues of greater than $1 million cannot be calculated because it is unknown what portion, if any, of these loans is made to businesses that banks consider to be small. [ψψ] The number of large banks that answered the questions used for the extrapolations falls below the allowable reporting threshold for protecting respondents' identities.

particularly for banks with less than $1 billion in assets, yet loans secured by such properties are recorded on the Call Report as residential mortgages, even though the loan purpose is commercial and industrial. Table 2.1 shows that the extrapolated lower bound of the understatement of outstanding small business loans that is due to the proxy's exclusion of loans secured by 1- to 4-family residential properties is $15.6 billion for small banks (under $10 billion) and $2.7 billion for large banks ($10 billion or above), or at least *$18.3 billion* total for calendar 2015.[21]

The sum of lower-bound extrapolations presented in this subsection suggests that relying on the Call Report proxy understates total bank small business C&I lending by at least $34.8 billion for small banks and by $2.7 billion for large banks, for the reason that the proxy does not include loans to small businesses that either were originated at amounts greater than $1 million or were secured by 1- to 4-family residential properties. The amounts of small business C&I lending recorded by the proxy in Q4 2015 totaled $121 billion at small banks and $199 billion at large banks, for a combined $320 billion. Thus, the extrapolated lower bound of total C&I small business loans in Q4 2015 made by small banks is $156 billion, or 28.8 percent larger than what is captured by the proxy, and by large banks, $201 billion, or 1.4 percent larger than the proxy. For the industry, the survey findings show that total bank small business C&I lending was likely at least $357 billion in Q4 2015, or 11.7 percent larger than the proxy.

2.6 Conclusions

Banks are the most common source of external credit for small businesses, yet there is no comprehensive measure of small business lending by banks. The best existing measure of small business C&I lending extended by banks is the Call Report proxy, which uses a loan-size measure to identify small business lending. But banks may define small businesses differently from the proxy. Therefore, this section first reports banks' answers to questions on how they define their small business customers and

[21] Refer to Appendix B for the assumptions used to relate the survey question to the Call Report proxy. The survey question asks about loan originations (a flow), whereas the Call Report proxy collects information on outstanding loan dollars (a stock). See footnote 19 for a definition for "stocks." In contrast, flow values are quantities observed over a specified time period. For example, quarterly income statements contain flow values.

small business loans. Then, if the answers to these questions indicate there is small business lending that the proxy does not capture, the section analyzes specific areas of uncaptured lending. Finally, the section extrapolates to derive the lower bound of the understatement.

The survey shows that small and large banks differ in how they define small businesses. As expected, small banks draw on many different characteristics, including those that are qualitative, whereas large banks rely primarily on the size of the loan and the revenue of the firm. And of the small share of small banks and large share of large banks that use specific limits to define their small business loans, substantial portions use limits of greater than $1 million. Thus, the survey provides evidence that the best existing measure of bank small business C&I lending, the Call Report proxy, is unable to fully capture all loans made to small businesses. In addition, the survey documents that portions of banks' C&I loan originations are secured by personal real estate, which demonstrates another way in which the proxy understates small business lending.

The survey finds that the vast majority of small banks with assets of less than $1 billion consider largely all of their C&I lending to have been made to small businesses—a finding that confirms the common understanding that these banks specialize this lending to small firms. These are also the banks most likely to have their C&I loans secured by residential real estate. Both findings show that the proxy potentially understates the contribution of the smallest banks to small business lending relatively more than it understates the contribution of other banks. Thus, the understatement that the survey is able to document reinforces the importance not only of banks generally, but more particularly of small banks, as providers of small business credit in the United States. A conservative estimate shows that in Q4 2015, small banks held *at least* 28.8 percent more outstanding loan dollars to small businesses than the Call Report proxy captured, whereas large banks held at least 1.4 percent more.

In sum, the survey results document that the Call Report proxy substantially understates the true amount of small business lending by banks. A lower-bound estimate of the understatement based on the survey results indicates that for calendar year 2015, the proxy is at least 11.7 percent below the actual volume of small business C&I lending extended by all banks.

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SECTION 3.
Markets and Competition

This section investigates the market for small business lending, looking at how banks view their geographic reach in small business lending and what kinds of technologies and techniques banks use to bridge the physical distance between themselves and potential small business customers. The section also investigates what institutions, by geography and by size, banks consider to be their competition.

These questions matter because if banks have narrow lending areas, provide businesses with few options to apply for loans without visiting a branch, and do not consider themselves to be in competition with nonlocal financial institutions, many small business borrowers may have trouble switching to another lender if nearby banks or nearby bank branches close. Similarly, if small banks serve a substantially different set of customers from large banks and if banks view themselves as solely competing with other banks of similar size, small-bank customers may have trouble accessing credit at large banks if small banks' number and lending continue to decrease. On the other hand, if banks view nonbank financial institutions such as credit unions and financial technology lenders as important competitors, these organizations may be capable of filling in the gaps created by the changing structure of the banking industry.

3.1 What Is Your Bank's Geographic Market for Loans to Small Businesses?

The survey explores the geographic extent of banks' small business lending markets and seeks to learn whether large banks tend to have wider markets relative to their branch footprint than small banks. Previous studies have shown that small businesses located farther away from banks are less likely to obtain bank loans and that the relationship between distance and the likelihood of obtaining bank loans is stronger for smaller banks as well as for younger businesses or those that cannot clearly demonstrate creditworthiness.[22] The link between bank credit and proximity, however, may have been loosened by recent changes in the use of technology and the increasing availability of data, perhaps combined with the trend toward fewer small banks. Any such loosening would give banks a broader geographic market for their small business loans.

Specifically, the survey asked banks to describe the general geographic area where they focus their resources and outreach for commercial and industrial loans to small businesses.[23] The results show that small business lending remains focused substantially on areas close to bank locations, particularly for small banks.

[22] See Allen N. Berger et al., "Does Function Follow Organizational Form? Evidence from the Lending Practices of Large and Small Banks," *Journal of Financial Economics* 76, no. 2 (2005): 237–69, https://dx.doi:10.1016/j.jfineco.2004.06.003; Kenneth P. Brevoort and Timothy H. Hannan. "Commercial Lending and Distance: Evidence from Community Reinvestment Act Data," *Journal of Money, Credit and Banking* 38, no. 8 (2006): 1991–2012, http://www.jstor.org/stable/4123041; Udell, "What's in a Relationship?"; Kenneth P. Brevoort, John D. Wolken, and John A. Holmes, "Distance Still Matters: The Information Revolution in Small Business Lending and the Persistent Role of Location, 1993–2003," Federal Reserve Board, Finance and Economics Discussion Series, Working Paper No. 2010-08 (March 1, 2010), http://dx.doi.org/10.2139/ssrn.1559989; and Sumit Agarwal and Robert Hauswald. "Distance and Private Information in Lending," *Review of Financial Studies* 23, no.7 (2010): 2757–88, https://doi.org/10.1093/rfs/hhq001.

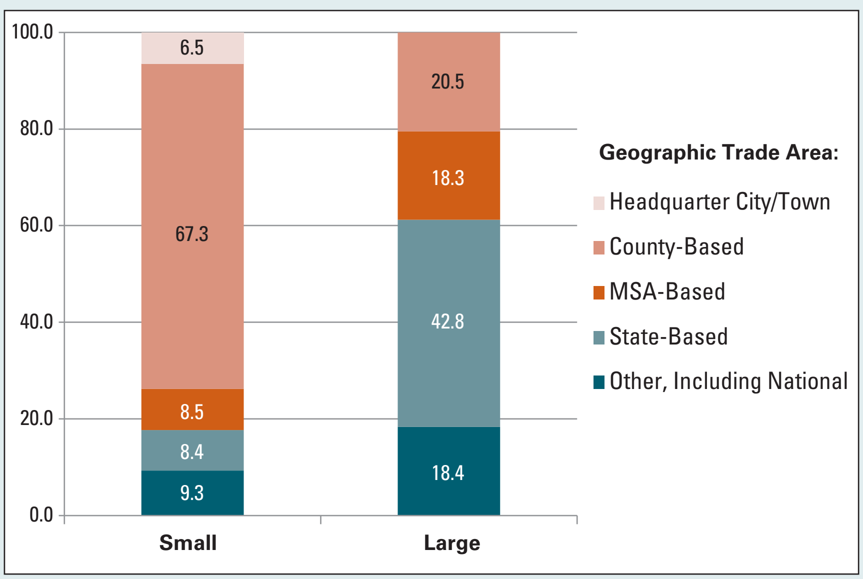
[23] The survey provided banks with nine geographical options and a write-in option. All the options were aggregated into five broader categories in order to meet the disclosure review thresholds for protecting respondents' identities. These aggregations do not change the qualitative results.

Small banks have predominantly local trade areas for small business lending. As shown in Figure 3.1, small banks focus on the city where they are headquartered (6.5 percent), on counties containing or near their branches (67.3 percent), or on metropolitan statistical areas (MSAs) containing or near their branches (8.5 percent).[24] Combined, 82.3 percent of small banks selected one of these local options. Fewer than 10 percent of small banks focus their small business lending efforts on either state-based areas (8.4 percent) or at a national level (9.3 percent). The predominantly local focus of small banks suggests that if all small banks exit a particular area, out-of-area small banks will not fill the local small business lending gap.

Large banks generally spread their resources across larger geographic areas than small banks, but a substantial minority is, like small banks, locally-focused. As Figure 3.1 shows, large banks that describe their market area as at the state level constitute the largest share (42.8 percent) of large banks, and up to an additional 18.4 percent focus at the national level.[25] However, Figure 3.1 also shows that a substantial share (38.8 percent) of large banks consider their market to be based in a more local area. Among large banks, 20.5 percent consider their target geographic markets to be at the county level, and an additional 18.3 focus their efforts at the MSA level. Therefore, although a majority of large banks do not define their geographic markets at the level of the MSA, county, or city, the share that does focus small business lending efforts on these more local geographies is surprisingly substantial. This contrasts somewhat with the implications of the established view that large banks do not require proximity to their small business customers.

The overall findings suggest that the wider geographic focus of large banks may be able to fill some of the gap in small business lending that opens up when a small local bank closes. However, despite recent changes in technology and banking structure, location remains an important factor in small business lending for many banks of both sizes.

Figure 3.1: Percentage of Banks That Use This Geographic Level as Their Trade Area for Small Business Lending



Source: SBLS Question 15.

Notes: The survey question asks banks for the geographic market, or "trade area," where they focus their resources and outreach to generate small business lending. At the statistical significance of 10 percent, small banks are more likely than large banks to use a county-based geographic trade area; large banks are more likely than small banks to use an MSA or state-based geographic trade area.

24 An MSA is a geographical area with a relatively high population density at its core and close economic ties within its boundaries. MSAs may be smaller geographically than a state but may cross state lines (e.g., the Baltimore-Washington metropolitan statistical area).

25 The number of responses of large banks that described their market area as having a national focus did not meet disclosure review thresholds for protecting respondents' identities; thus, for both large and small banks these responses were combined with the write-in responses describing the banks' market areas as other than the options provided.

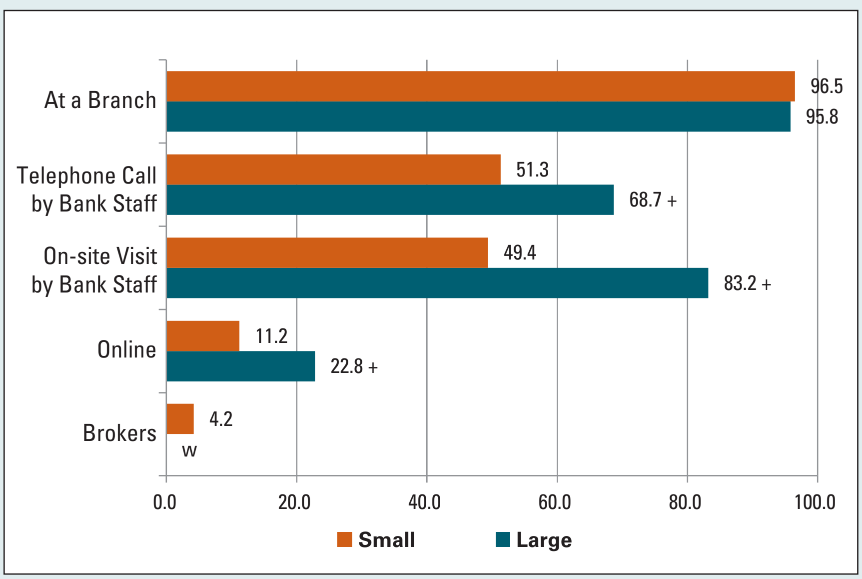
3.2 Where Can a Small Business Apply for a Loan from Your Bank?

The survey further explores the geographic extent of banks' small business lending market by looking through the lens of where small businesses are able to apply for loans. The finding above that small banks tend to define their lending areas more locally than large banks suggests that the two sizes of banks are using different methods to reach their small business customers. Understanding whether in fact methods differ, and if so, how, may become increasingly relevant as branches continue to close and bank assets become further concentrated in large banks. Given the increasing use of technology by banks, it might be expected that banks use the Internet to provide greater convenience to more-distant customers. Further, since large banks are thought to use more technology in their small business lending decisions than small banks do, it might be expected that large banks' greater reach is made possible by allowing online applications for small business loans.

Specifically, the survey asked banks where and how potential small business borrowers can submit applications for commercial and industrial loans.[26] The results suggest, surprisingly, that large banks for the most part extend their geographic reach farther than small banks through staff-time-intensive methods, with only a few large banks using online platforms.

Unsurprisingly, the survey finds that more than 95 percent of both small banks and large banks accept applications for small business loans through their branches, as shown in Figure 3.2. About one-half of small banks also accept applications through phone calls (51.3 percent) and on-site visits by bank staff (49.4 percent). However, large banks generally provide their small business customers with a broader range of ways to submit loan applications; they allow, on average, 3.5 different ways in which small businesses can apply for loans, compared with 2.7 different ways for small banks.[27] Interestingly, the broader reach of large banks is driven less by use of the Internet and more by use of telephones and cars:

Figure 3.2: Percentage of Banks That Allow Small Business Borrowers to Apply for Loans Using This Method



Source: SBLS Question 23.

Notes: Entries marked with a "w" indicate that the number of responses falls below the allowable reporting threshold for protecting respondents' identities. At the statistical significance of 10 percent, "+" denotes that large banks are more likely than small banks to allow small business borrowers to apply for loans using this method. Banks may select multiple answers; results will not sum to 100.0 percent.

[26] The survey gave banks eight options and the ability to write in three additional answers not already listed. The responses were aggregated for clarity of presentation and to comply with the requirements related to protecting respondents' identities.

[27] The survey provided banks with eight possible ways and a write-in option. The difference between what large banks report and what small banks report is statistically significant.

large banks are 11.7 percentage points more likely to accept loans online than small banks, but 17.4 percentage points more likely to accept applications during phone calls, and 33.8 percentage points more likely to accept applications during on-site visits by bank staff. Overall, only 22.8 percent of large banks accept small business applications online, compared with the 83.2 percent that are willing to via on-site visits. On-site visits have clear geographic limitations, so the willingness to make such visits to accept a loan application gives some insight into the continued importance of distance in small business access to credit.

The fact that the great majority of large banks provide staff-time-intensive ways for prospective borrowers to submit loan applications and have not adopted online submission of applications could reflect several properties of bank lending to small businesses. First, it may be hard for banks to adapt small business lending to an online environment, for direct human interaction appears inherent in the process. Even large banks, whose small business lending methods are shown in Sections 2 and 5 to rely more heavily on evaluating standard data against preset limits, have thus far not generally found it worthwhile to pursue online small business loan applications. Second, if there is a way to make online small business lending profitable, there appears to be an opportunity for innovation by financial technology (FinTech) firms. To date, there have been few partnerships between small banks and FinTechs, but recent surveys have shown banks to be open to the possibility.[28]

3.3 Who Are Your Bank's Competitors?

To investigate whether small and large banks serve distinct sets of small business customers, the survey looked at the competition these banks face. The evidence from the survey so far indicates that there is substantial geographic segmentation in the small business lending market. (To recapitulate: many banks largely lend to businesses near their branches, which in turn suggests that small business borrowers are limited to borrowing from nearby banks. Further, as bank branches decline in number, the local focus could leave small businesses with few or no feasible sources of bank credit. This concern may be partly mitigated by the fact that large banks tend to lend in broader areas than small banks.) In addition, there may also be segmentation by bank size: some small businesses may be better served by small banks than by large banks because small banks provide a more appropriate set of services or use a broader array of information to determine creditworthiness.[29] Indeed, studies have found that small banks are more likely to lend to relatively smaller and younger firms and large banks are more likely to lend to larger and more mature small firms.[30] If this is the case, some small businesses may not be able to compensate for the loss of a local small bank by using the services of a more distant large bank.

Specifically, the survey asked banks to select which types of financial institutions (banks and nonbanks) they consider to be frequent competitors for small business lending, and to rank their top three most important competitors. If the small business lending market is as geographically segmented as the findings so far indicate it is, banks should not typically view banks that lack a physical presence

[28] See Hilary Burns, "This Fintech Partnership Could Serve as Template for Small Banks," *American Banker,* April 16, 2018, https://www.americanbanker.com/news/this-fintech-partnership-could-serve-as-template-for-small-banks; and American Bankers Association. "How Banks Partner with FinTech for Digital Lending." *ABA Bank Marketing.* March 26, 2018, https://ababankmarketing.com/insights/how-banks-partner-with-fintech-for-digital-lending/.

[29] Stein, "Information Production"; David A. Carter, James E. McNulty, and James A. Verbrugge, "Do Small Banks Have an Advantage in Lending? An Examination of Risk-Adjusted Yields on Business Loans at Large and Small Banks," *Journal of Financial Services Research* 25, no. 2–3 (2004): 233–52, https://doi.org/10.1023/B:FINA.0000020663.21079.d2; and Berger et al., "Does Function Follow Organizational Form?"

[30] George W. Haynes, Charles Ou, and Robert Berney, "Small Business Borrowing from Large and Small Banks," in *Business Access to Capital and Credit,* edited by Jackson L. Blanton, Alicia Williams, and Sherrie L. W. Rhine, 287–327, Federal Reserve System Research Conference, 1999, http://citeseerx.ist.psu.edu/viewdoc/download;jsessionid=D208864BBCA8E4D281034D453A1F3D7F?doi=10.1.1.474.279&rep=rep1&type=pdf; and Berger et al., "Function Follow Form?"

in their markets as competitors. And to the extent that there is segmentation by bank size—with smaller firms more likely to borrow from small banks, as studies have found to be the case—small banks would be expected to compete solely with other small banks and large banks with other large banks.[31] But if, instead, most small businesses can be served by banks of any size, there should be more competition between banks of differing sizes. And if banks frequently view various nonbank institutions as important competitors, small businesses may be able to borrow from these organizations in the event they lose access to their current preferred lender.

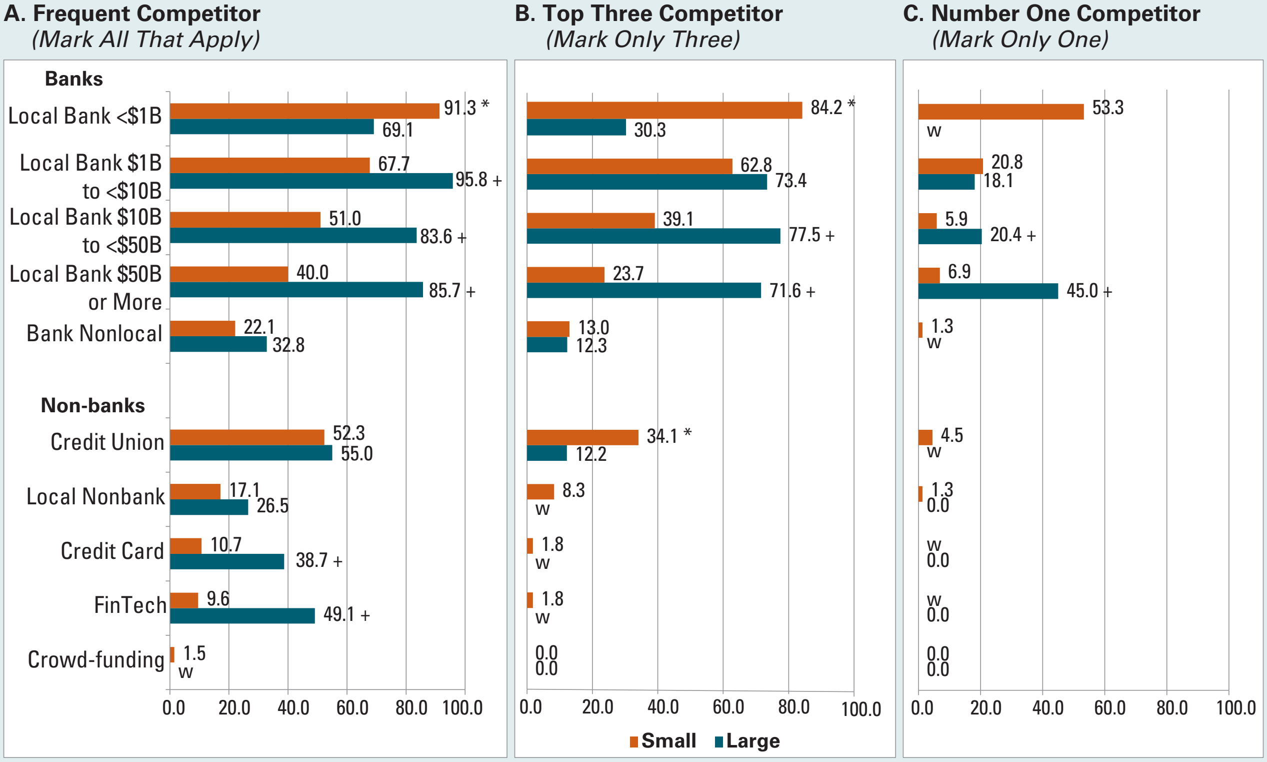
The survey finds that the most common and important competitors are other banks with a local branch presence, providing further evidence for geographic segmentation. Figure 3.3 shows the proportion of small and large banks that view each type of institution as a frequent competitor, a top three competitor, and its number one competitor (Panels A, B, and C, respectively). The overwhelming majority of both small and large banks (86.9 percent and 83.5 percent) view a local bank of some size as their number one competitor (Figure 3.3, Panel C). In contrast, nonlocal banks are seen as frequent competitors by only 22.1 percent of small banks and 32.8 percent of large banks (Figure 3.3, Panel A), with even fewer reporting them as top three competitors (Figure 3.3, Panel B), and almost no banks reporting nonlocal banks as their number one competitor (Figure 3.3, Panel C). The importance of nearby competitors reaffirms that physical presence is extremely important for small business lending, even for large banks. These findings are consistent with the finding (discussed below in Section 4) that large banks view their branch networks as sources of competitive advantage.

Banks typically view other banks of similar size to be their most important competitor—evidence consistent with segmentation by bank size in the small business lending market. Figure 3.3, Panel C, shows that nearly three-quarters of small banks believe their number one competitor to be another small local bank, either banks with less than $1 billion in assets (53.3 percent) or banks with $1 billion to $10 billion in assets (20.8 percent). Similarly, roughly two-thirds of large banks view another large bank to be their number one competitor, with this share encompassing competitor banks with $10 to $50 billion in assets (20.4 percent of large banks) and banks with greater than $50 billion in assets (45.0 percent).

When competition is considered more broadly, however, with the focus on frequent competitors for small business lending (Figure 3.3, Panel A) and on top three competitors (Figure 3.3, Panel B), there is much less market segmentation by size and much more overlap between small and large banks, with large banks particularly inclined to view small banks as competitive threats. A substantial majority of large banks (69.1 percent) view even banks with less than $1 billion in assets as frequent competitors for small business lending, and slightly less than one-third (30.3 percent) view them as top three competitors. It is also not uncommon for small banks to see large banks—and even the largest banks—as competitors, with 40.0 percent viewing banks with more than $50 billion in assets as frequent competitors and 23.7 percent viewing them as a top three competitor. This partial segmentation between small and large banks suggests that there is a reasonably wide base of small business customers that are capable of borrowing from either small or large banks. The overlap is most noticeable in how banks with $1 billion to $10 billion in assets are viewed. Figure 3.3, Panel A, shows that almost every large bank—more than 95 percent—views these “larger” small banks ($1 billion to $10 billion in assets) as frequent competitors, and Figure 3.3, Panel B, shows that three-quarters of large banks (73.4 percent) view them as top three competitors. Majorities of small banks also view this group of small banks as frequent and top three competitors. Further, statistically equal shares of small and large

31 In support of this notion, the Community Banking in the 21st Century 2017 survey finds that community banks primarily compete with other community banks for small business loans (defining community banks as those with $10 billion in assets or less). See Federal Reserve System and Conference of State Bank Supervisors, Community Banking Research and Policy Conference, October 4–5, 2017, *Community Banking in the 21st Century 2017,* https://www.communitybanking.org/~/media/files/cb21pub_2017_book_web.pdf.

Figure 3.3: Percentage of Banks That Consider This Institution a Competitor for Small Business Lending



Source: SBLS Question 16.

Notes: Entries marked with a "w" indicate that the number of responses falls below the allowable reporting threshold for protecting respondents' identities. At the statistical significance of 10 percent, "*" denotes that small banks are more likely than large banks to consider this institution a competitor for small business lending; "+" that large banks are more likely than small banks. "Nonlocal Bank, Any Size" is an aggregation of separate options for nonlocal banks of different sizes. "FinTech" is an aggregation of separate options for nonbank online lenders and marketplace lenders. See Question 16 of the SBLS for the complete list of response options provided. In Panels A and B, banks may select multiple answers; results will not sum to 100.0 percent.

banks (20.8 percent and 18.1 percent) consider banks with $1 billion to $10 billion in assets as their number one competitor.

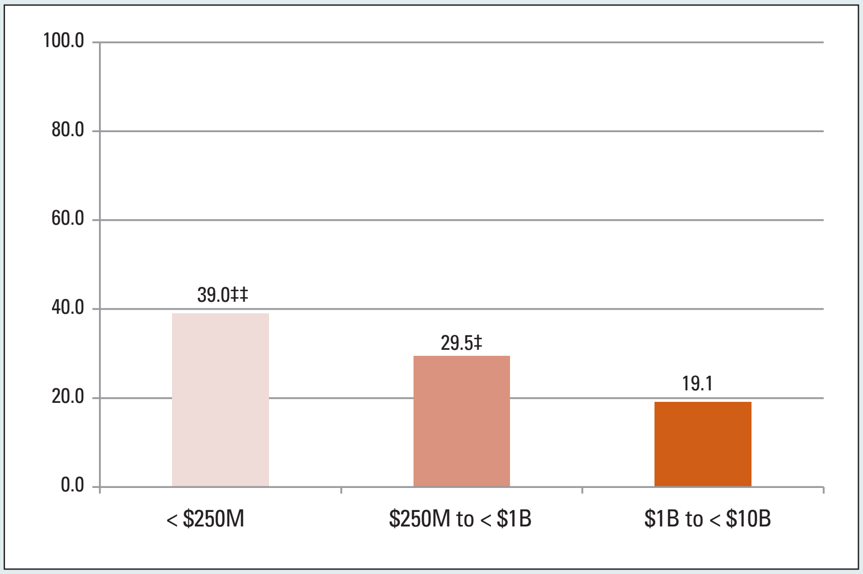
Turning to the nonbank results, banks' chief competitor among nonbanks is credit unions. Recent changes in the regulations governing credit unions have expanded the small business lending capacity of these institutions.[32] However, credit unions are typically quite small, with the median credit union having only $30 million in assets in 2017.[33] They are also focused more on their membership, which is often drawn from local populations. Thus, they would be expected to serve small businesses that are much like the small businesses served by small banks, thereby posing greater competition to those banks than to large banks.

The survey largely confirms these expectations. Figure 3.3, Panel A, shows that a slight majority of

[32] For example, the National Credit Union Administration adopted a new approach to and definition of member business lending; the new approach and definition are seen as increasing the commercial lending capacity of federally insured credit unions. See 81 Fed. Reg. 13530–13559 (March 2016), https://www.gpo.gov/fdsys/pkg/FR-2016-03-14/pdf/FR-2016-03-14.pdf; and Robby Knapp, "Member Business Loans: What Credit Unions Should Focus on Right Now," *Credit Union Journal,* June 20, 2017, https://www.cujournal.com/opinion/member-business-loans-what-credit-unions-should-focus-on-right-now.

[33] National Credit Union Administration, *Credit Union Data Summary 2017 Q1,* https://www.ncua.gov/analysis/Pages/call-report-data/reports/paca-facts/paca-facts-2017-Q1.pdf.

Figure 3.4: Percentage of Banks That Consider Credit Unions to Be a Top Three Competitor for Small Business Lending
(Small Banks Only)



Source: SBLS Question 16.

Notes: At the statistical significance of 10 percent, "‡‡" denotes that banks with less than $250 million in assets are more likely than banks with $250 million to less than $1 billion in assets and more likely than banks with $1 billion to less than $10 billion in assets to consider a credit union to be a top three competitor; "‡" that banks with $250 million to less than $1 billion in assets are more likely than banks with $1 billion to less than $10 billion in assets.

both small and large banks (52.3 and 55.0 percent) report frequent competition with credit unions. However, Figure 3.3, Panel B, shows that more than one-third (34.1 percent) of small banks view credit unions as a top three competitor, compared with only 12.2 percent of large banks.[34] Similarly, Figure 3.4 shows that among small banks, those with less than $250 million in assets are about twice as likely as those with $1 billion to $10 billion in assets to see credit unions as a top three competitor (39.0 percent compared with 19.1 percent). This is consistent with the finding that banks tend to view other banks of similar size as their top competitors. Nonetheless, Figure 3.3, Panel C, shows that only 4.5 percent of small banks view a credit union as their number one competitor, implying that other banks remain the predominant source of competition for small banks. These results suggest that credit unions would be able to fill only a small share of any potential loss in access to small business credit resulting from the loss of local small banks.

Among other nonbank lenders are FinTech firms and credit card issuers. The availability of "big data" has recently prompted FinTechs to enter the small business lending market. Since these institutions generally use technology much as large banks do, they might be expected to be more competitive with large banks.

And in fact the survey shows that FinTechs are considered as competitors only for large banks, but only as frequent competitors, not as top competitors. Figure 3.3, Panel A, shows that only about one in ten small banks view FinTechs and credit card issuers as frequent competitors, while Figure 3.3, Panel B, shows that fewer than 2 percent consider each (FinTechs and credit card issuers) a top three competitor.[35] In comparison, sizeable numbers of large banks list FinTech and credit card issuers among their frequent competitors (49.1 percent and 38.7 percent)—likely because these institutions lend in an even more transactional manner than large banks, relying almost exclusively on hard data and

[34] The number of large banks that view credit unions as a number one competitor falls below the reporting threshold for protecting respondents' identities.

[35] The number of small banks that view credit card companies or FinTech firms as a number one competitor falls below the report-ing threshold for protecting respondents' identities.

automated technologies. This view of FinTech and credit card issuers as frequent competitors of large banks dovetails with the results reported in Section 5.1 showing that two-thirds of large banks offer credit cards as one of their loan products for small business customers. Thus, these large banks are setting themselves up for direct competition with credit card issuers. However, almost no large banks view FinTechs or credit card issuers as a top three or number one competitor.[36] Thus, while FinTechs may eventually reshape the lending landscape, they are not currently viewed as a major competitor, and their ability to mitigate any loss to small businesses' access to credit if the number of local small banks were to decrease would be minimal.

3.4 Conclusions

This section finds that banks compete locally and largely use traditional "technologies" such as the brick-and-mortar branch, the car, and the telephone as conduits for loan applications from small businesses. Large banks are more willing to make use of off-site approaches than small banks, likely contributing to their larger lending areas. Many of these larger organizations, however, remain locally-oriented, and all banks view other local banks as their most important and most frequent competitors. The results support previous findings that physical distance is a key component of small business lending, so that from the perspective of small businesses, the country largely remains segmented into a series of local lending markets rather than constituting a single, integrated market. The recent decline in the number of bank branches across the country may therefore create significant problems for small businesses' access to credit if the decline means that small businesses are left with a greater distance to the nearest bank branch.

In terms of competition between banks, there is evidence that small and large banks have a partly overlapping small business clientele. The fact that, to some extent, small and large banks consider themselves to be in frequent competition with the other for small business borrowers suggests that many small businesses are capable of borrowing from either type of bank. At the same time, however, the fact that banks' main competitor tends to be a similarly sized bank suggests that small and large banks offer somewhat differentiated services that appeal to distinct groups of customers. Thus, the degree to which small businesses are able to substitute large banks for small ones will determine how much credit disruption small businesses may face as consolidation in the banking industry continues.

Many banks experience some competition in small business lending from emerging nonbank financial institutions, but few banks consider these to be among their most important competitors. Small banks are more concerned than large banks about credit unions, while large banks view both credit unions and FinTech firms as competition. This suggests that, in the absence of significant growth, nonbank institutions will have only a limited ability to fill any gaps in small businesses' access to credit that result from the trend toward fewer small banks and fewer bank branches.

[36] The number of large banks that view credit card companies or FinTech firms as a top three or number one competitor falls below the reporting threshold for protecting respondents' identities.

SECTION 4. Competitive Practices and Advantages

This section investigates the overall approaches that small and large banks take to small business lending by looking closely at the competitive practices each type of bank customarily uses and at each type's perceived competitive advantages. The preceding section presents evidence of partial segmentation in the lending market by size: small and large banks often view each other as competitors, but at the same time they rarely view each other as top competitors. This suggests that their customer bases partly overlap, with some small businesses able and willing to borrow from a bank of either size, whereas other small businesses are much better suited to small banks or to large ones.

Therefore, the survey considers the extent to which the approaches of these organizations overlap and the extent to which they diverge, and whether these approaches correspond to the understanding that small banks are relationship lenders and large banks are transactional lenders. The answer to this question is important for small businesses in the context of the recent trend toward fewer small banks. For instance, if small banks approach small business lending in a more personalized manner than large banks, small businesses that need more personalized engagement through the loan application process may lose access to credit if trends continue.

4.1 How Does Your Bank Maintain and Generate Relationships with Small Businesses?

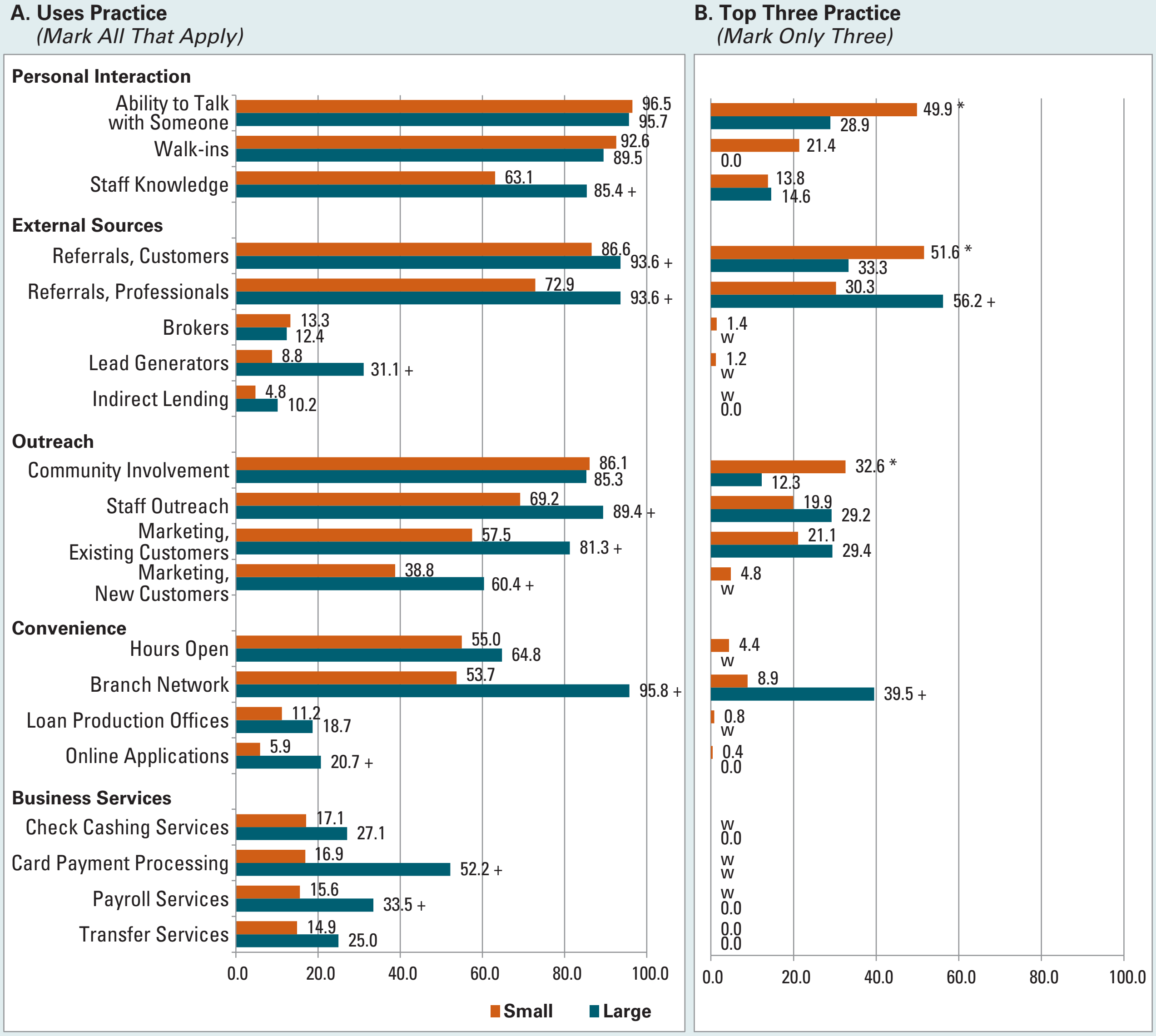
The partly overlapping competition between banks of different sizes that is discussed in Section 3 may be mirrored in an overlapping of practices between small and large banks. However, small and large banks might also be expected to use different practices, with small banks using relationship-based practices that focus on individual contact between staff and potential customers, whereas large banks may take advantage of economies of scale and scope to offer customers a greater range of products and greater convenience.

Accordingly, the survey asked banks to mark which of 20 different practices they use to generate new small business lending relationships and maintain existing ones.[37] The survey also asked banks to designate up to 3 practices as their top practices. The survey results show that there is a core set of practices for small business lending that is common to both small and large banks. Further, this core set contains practices that are high-touch and personal in nature. Figure 4.1, Panel A, presents the shares of small banks and large banks that selected each practice as one that the bank uses. The figure shows that the ability to talk to a live person, acceptance of walk-in customers, community involvement, and customer referrals are practices cited by more than 85 percent of both small and large banks. Conversely, practices that outsource or automate small business lending are relatively unpopular, even among large banks. Brokers, indirect lending, and online applications are used by less than 25 percent of both small banks and large banks, and lead generators are used by only 31.1 percent of large banks and a much smaller proportion of small banks. Together, these results suggest that for both small and large banks, small business lending is inherently relationship-focused.

Beyond these common practices, large banks appear to take advantage of their economies of scale and scope in several ways. Large banks, on average, use 2.8 more practices than small banks, possibly

[37] Banks were also given a write-in option.

Figure 4.1: Percentage of Banks That Use This Practice to Generate New and Maintain Existing Small Business Lending Relationships



Source: SBLS Question 24.

Notes: Entries marked with a "w" indicate that the number of responses falls below the allowable reporting threshold for protecting respondents' identities. At the statistical significance of 10 percent, "*" denotes that small banks are more likely than large banks to use this practice to generate new and maintain existing small business lending relationships; "+" that large banks are more likely than small banks. Banks may select multiple answers; results will not sum to 100.0 percent.

reflecting their greater resources.[38] Nearly all large banks (95.8 percent) use their branch networks to generate new relationships and maintain existing ones, whereas only slightly over half (53.7 percent) of small banks do. This, along with the findings of Section 3 about markets and competitors, underscores the crucial role that physical proximity plays in small business lending, and suggests that having multiple branches is a powerful tool for large banks. Large banks are also more than

[38] The survey finds that small banks use 8.9 different practices on average, whereas large banks use 11.7, which is a statistically significant difference.

20 percentage points more likely than small banks to engage in active marketing to both their existing customers and potential new customers, a divergence that could arise from large banks' greater economies of scale. Finally, large banks are more likely than small banks to use their other business services, such as payroll services and, especially, card processing, to attract small business borrowers, thus leveraging economies of scope to provide customers with greater convenience.

Whereas there is substantial overlap in the practices that small and large banks use, there is less overlap in the practices they prioritize. Figure 4.1, Panel B, presents the shares of small and large banks that selected each practice as one of the bank's top three practices. Small banks are between 18 and 21 percentage points more likely than large banks to prioritize the common high-touch practices—live person, walk-ins, community involvement, and customer referrals.[39] Many small banks also prioritize other practices that rely on strong connections to the community, including professional referrals (30.3 percent), marketing to existing customers (21.1 percent), and staff outreach (19.9 percent).

By contrast, large banks are 30 percentage points more likely than small banks to view the use of their branch networks as one of their most important practices, once again highlighting the importance of location in small business lending. Large banks also rely more heavily than small banks on professional referrals (56.2 percent versus 30.3 percent).

In terms of similarities, both small and large banks prioritize staff outreach and marketing to existing customers at similar rates, and although large banks do use their other business services to attract borrowers, they rarely consider the provision of these services to be crucial practices.[40] Overall, both small and large organizations do tend to prioritize different practices, with small banks using high-touch practices somewhat more intensively than large banks; but for banks of both sizes, relationships are important.

4.2 What Are the Competitive Advantages of Your Bank and of Your Number One Competitor?

In order to gain more insight into the priorities of banks of each size and the potentially different types of value they provide to their customers, the survey focused on how banks of both sizes view themselves and how other banks view them. The understanding that small banks are relationship lenders and large banks are transactional lenders could lead one to expect that each size has distinct advantages in small business lending. For example, small banks might be better at customer service and at customizing their approach for different customers, whereas large banks might offer more convenience and lower interest rates. The similarities discussed in the preceding section, however, allow the possibility that the two sizes of banks may in fact not have strongly distinct advantages.

The survey asked banks to list both their own competitive advantages and the competitive advantages of their top competitor.[41] In both cases, banks selected from a list of 18 possible advantages, and designated up to 3 as top three advantages.[42] The results are broadly consistent with the findings of the previous subsection that, even for large banks, small business lending is rarely fully transactional.

Figure 4.2 groups into six broad categories the individual advantages that banks selected, and shows that an overwhelming majority of both types of banks—86.5 percent of small banks and 83.5 percent

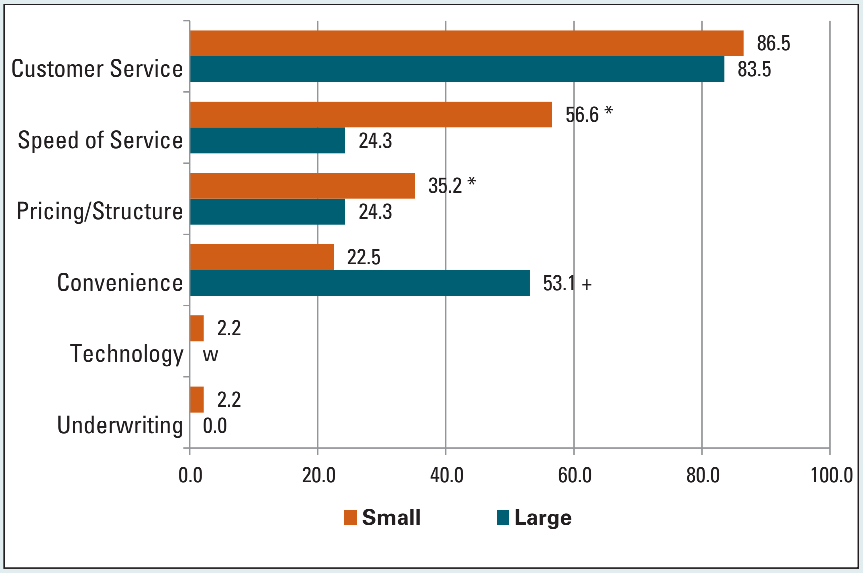
[39] The number of large banks reporting walk-ins as a top three practice fell below the reporting threshold for protecting respondents' identities.

[40] The number of small and large banks that report card processing as a top three practice fell below the reporting threshold for protecting respondents' identities; the number of large banks that report check cashing and payroll services also fell below the threshold.

[41] Top competitors for small business lending are discussed above in Section 3.3.

[42] Banks were also given a write-in option.

Figure 4.2: Percentage of Banks That Consider Themselves to Have a Top Three Competitive Advantage in This Category



Source: SBLS Question 18.

Notes: Entries marked with a "w" indicate that the number of responses falls below the allowable reporting threshold for protecting respondents' identities. At the statistical significance of 10 percent, "*" denotes that small banks are more likely than large banks to consider themselves to have a top three competitive advantage in this category; "+" denotes that large banks are more likely than small banks. Banks may select answers in multiple categories; results will not sum to 100.0 percent.

Table 4.1: Percentage of Banks That Consider This Competitive Advantage One of Their Own Top Three

Category	Advantage	Small Banks	Large Banks
Customer Service	Relationship	58.6	57.1
	Personal attention	58.2*	42.7
	Staff quality	29.6	32.5
Speed of Service	Decision speed	48.6*	24.3
	Funding speed	20.3	w
Pricing or Structure	Loan structure flexibility	24.7	20.3
	Fees	8.0	w
	Interest rates	4.3	w
	Term	0.8	0.0
Convenience	Convenient location	11.0	16.3
	Credit products	7.8	18.4+
	Other services	5.4	24.5+
	Number of locations	1.6	22.3+
Technology	Mobile banking	1.8	w
	Remote deposit	0.5	w
Underwriting	Collateral requirements	0.9	0.0
	Debt service coverage	0.9	0.0
	Loan-to-value	0.7	0.0

Source: SBLS Question 18.

Notes: Entries marked with a "w" indicate that the number of responses falls below the allowable reporting threshold for protecting respondents' identities. At the statistical significance of 10 percent, "*" denotes that small banks are more likely than large banks to list this as a top three competitive advantage; "+" that large banks are more likely than small banks. Banks may select multiple answers; results will not sum to 100.0 percent.

of large banks—list some aspect of customer service as one of their own top advantages. Table 4.1 breaks out the categories into their specific individual advantages and presents the proportion of small and large banks that selected each individual advantage as one of their top three. The table shows that a majority of both sizes of banks consider established relationships with their borrowers to be their most important competitive advantage (58.6 percent of small banks and 57.1 percent of large banks), making it the most commonly selected advantage for both groups. Further, there is a set of self-reported top advantages that are common to both small and large banks, mirroring the results from Section 4.1. After established relationships, three of the next four most common top advantages of small banks are also among the next four most common top advantages of large banks: personal attention from the bank, decision speed, and staff quality.[43]

Yet, while small banks and large banks both perceive their customer relationships to be their own most important advantage, their competitors are much more likely to view small banks as having superior customer service. Table 4.2 presents banks' views of the top advantages for their number one competitor, be it a small bank, a large bank, or a credit union.[44] The table shows that nearly half (47.5 percent) of those who compete with small banks view customer relationships as one of small banks' top advantages, compared with 16.2 percent of those who compete with large banks. Figure 4.3 shows that this pattern continues into the broader measures of advantage—the categories within which the individual advantages are grouped. The figure shows that a majority (58.8 percent) of the banks competing with small banks consider them to have an aspect of customer service as a top advantage, compared with only 17.3 percent of those that compete with large banks. This suggests that small banks do have some advantages in relationship lending, consistent with the higher emphasis they place on the components of customer service relative to large banks, as shown in Section 4.1.

The clearest advantage of small banks, however, across both internal and external evaluations, is speed. Figure 4.2 shows that a majority of small banks (56.6 percent) consider an aspect of speed of service—either decision speed or funding speed—to be one of their own top three advantages, compared with slightly less than one-quarter of large banks (24.3 percent). Further, small banks are viewed as similarly advantaged by their competitors. Figure 4.3 shows that over one-quarter (26.2 percent) of small banks' competitors view speed as one of small banks' top advantages, compared with only 7 percent of large banks' competitors.

This speed advantage for small banks is particularly noteworthy because one might expect large banks, using quantitative data, to have a more standardized decisionmaking process resulting in quicker decisions. In practice, however, it appears that the flatter organizational structure of small banks, with fewer layers of management separating loan officers from bank owners, allows for faster decisionmaking and loan processing.[45] The importance of this advantage should not be underestimated, because funding speed is often an important consideration for small business borrowers.[46] This advantage also suggests, however, that if technological advances

[43] The fifth most common top advantage of small banks—loan structure flexibility—is the seventh most common for large banks, but the difference between small and large banks is small and statistically insignificant (24.7 percent of small banks compared with 20.3 percent of large banks). The fourth most likely advantage for large banks is other services offered, and large banks are much more likely than small banks to list this as a top advantage (24.5 percent of large banks compared with 5.4 percent of small banks).

[44] As shown in Section 3, almost all banks selected one of these organizations as their number one competitor. Banks that did not select one of these organizations as their number one competitor are excluded from this analysis.

[45] As discussed in Stein, "Information Production," both capital allocation and loan quality decisions are made locally at small banks, whereas at large banks capital allocation decisions are made at a distant central office, although loan quality is determined locally. The overall speed of small business loan decisions appears to be due partly to lack of distance between the officials who determine resource allocation and those who determine loan quality.

[46] The 2016 Small Business Credit Survey found that small businesses cite long waits for loans as one of their most frequent issues when receiving bank loans. See Federal Reserve Bank of Cleveland, *2016 Small Business Credit Survey Report on Microbusinesses: Nonemployer and Small Employer Firms,* November 2017, https://clevelandfed.org/global%20

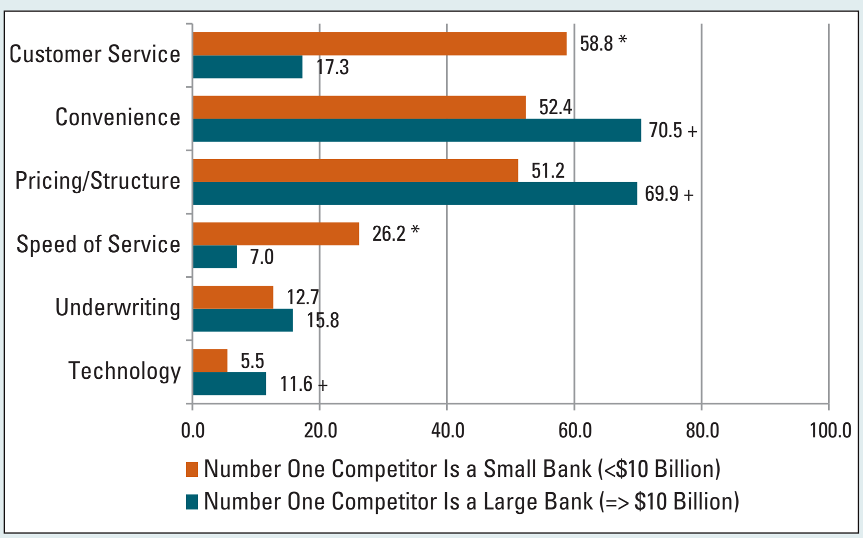
Table 4.2: Percentage of Banks That Consider This Competitive Advantage One of Their Number One Competitor's Top Three

		Top Competitor is a ...		
Category	**Advantage**	**Small Bank**	**Large Bank**	**Credit Union**
Customer Service	Relationship	47.5*	16.2	w
	Personal attention	26.1	w	0.0
	Staff quality	12.1	w	0.0
Speed of Service	Decision speed	21.7*	6.0	0.0
	Funding speed	9.7*	5.0	0.0
Pricing or Structure	Loan structure flexibility	24.2	22.7	40.8ϕϕ
	Fees	7.0	6.5	13.1
	Interest rates	29.6	59.3+	85.1ϕϕ
	Term	8.0	22.6+	39.1ϕϕ
Convenience	Convenient location	25.9	28.2	w
	Credit products	15.4	23.8+	w
	Other services	15.8	21.7	w
	Number of locations	17.8	33.7++	17.7
Technology	Mobile banking	3.5	7.7+	0.0
	Remote deposit	3.0	w	0.0
Underwriting	Collateral requirements	6.9	10.9	18.5ϕ
	Debt service coverage	3.2	2.4	w
	Loan-to-value	5.4	5.6	w

Source: SBLS Questions 16 and 17.

Notes: Entries marked with a "w" indicate that the number of responses falls below the allowable reporting threshold for protecting respondents' identities. At the statistical significance of 10 percent, "*" denotes that small banks are more likely than large banks to be considered by their competitor banks to have this competitive advantage as one of their top three; "+" that large banks are more likely than small banks; "++" that large banks are more likely than both small banks and credit unions; "ϕ" that credit unions are more likely than small banks; "ϕϕ" that credit unions are more likely than both small and large banks. Banks may select multiple answers; results will not sum to 100.0 percent.

Figure 4.3: Percentage of Banks That Consider Their Number One Competitor to Have a Top Three Competitive Advantage in This Category



Source: SBLS Questions 16 and 17.

Notes: At the statistical significance of 10 percent, "*" denotes that small banks are more likely than large banks to be considered by their competitor banks to have a top three competitive advantage in this category; "+" that large banks are more likely than small banks. Banks may select answers in multiple categories; results will not sum to 100.0 percent.

allow large banks or FinTech firms to increase their decision speed, small banks may face more competitive pressures in the future.

In contrast to small banks, large banks are viewed both internally and externally as offering greater convenience to their customers, with a broader range of services offered and a larger number of branches. Figure 4.2 shows that slightly more than half (53.1 percent) of large banks believe some form of convenience to be one of their own top advantages, compared with slightly less than a quarter (22.5 percent) of small banks. Similarly, Figure 4.3 shows that more than 70 percent of large banks' competitors view them as having convenience advantages, compared with just over half (52.4 percent) of small banks' competitors. These convenience advantages include number of locations. Table 4.1 shows that 22.3 percent of large banks consider number of locations to be one of their own top three advantages, whereas the comparable figure for small banks is only 1.6 percent. Table 4.2 shows that 33.7 percent of large banks' competitors view number of locations as one of large banks' top three advantages, compared with 17.8 percent of small banks' competitors for small banks' advantages. This once again shows the importance of physical branches in small business lending.

As for price advantages, evaluations vary depending on whether banks are rating themselves or whether competitors are rating them. Table 4.1 shows that very few banks of any size consider interest rates or fees to be one of their own top advantages. However, many banks do view interest rates as being a top advantage of their number one competitor. This is especially true for the competitors of large banks. As Table 4.2 shows, 59.3 percent of the competitors of large banks view interest rates as a top advantage of their large-bank competitor. By a large margin, this is the most common perceived top advantage for large banks, and large banks are twice as likely as small banks to be perceived as having this advantage. The frequency of this perception suggests that large banks do possess some advantages in pricing, but the evidence is surprisingly mixed, given the important role pricing usually plays in competitive markets.

As discussed in Section 3, few banks have a nonbank as their number one competitor. Nevertheless, it is possible to make some observations about banks' perceptions of credit unions, for the latter are listed as the number one competitor by 4.5 percent of banks (overwhelmingly small banks). Table 4.2 shows that the top perceived advantages of credit unions are pricing (85.1 percent) and, to a lesser extent, other elements of loan structure. This perception of advantages likely stems from the perceived tax-advantaged status of credit unions. Although pricing and loan structure are advantages more commonly associated with large banks rather than small banks, it appears that credit unions are more likely than large or small banks to be perceived as having advantages on these dimensions. Furthermore, despite their community focus and small average size, credit unions are viewed as having very different advantages from the ones small banks are perceived to have.

4.3 Conclusions

The survey finds that relationship lending practices are highly important for both small and large banks—a finding that suggests that small business lending is, to some extent, inherently relationship focused. With near universality, both small and large banks report using relationship lending practices, and they believe that their customer relationships, and their customer service in general, are among their top advantages.

Small banks, however, appear to focus more heavily on these practices and are more likely to view them as their most important practices. Small banks are also more likely to be viewed by their competitors as having advantages in customer relationships and in customer service in general. In addition, small banks consistently perceive themselves and are perceived by others as having a significant advantage in decision and funding speed. Given that large banks are thought to make lending decisions based on evaluating quantifiable data against preset

search?q=2016+Small+Business+Survey%3A+Report+on+Microbusinesses%3A+Nonemployer+and+Small+Employer+Firms.+-Published+November+2017.+Federal+Reserve+Bank+of+Cleveland.

limits, one might assume that they would be able to analyze the data and come to decisions faster. Large banks' advantage of relying on quantifiable data, however, is evidently less important than the flatter organizational structure of small banks, where fewer managerial layers separate loan officers from bank owners. The importance of this speed advantage may be considerable, for speed in decisionmaking and funding is one of the top concerns of small businesses.

Large banks, by contrast, provide more convenience, both by offering a greater variety of products and services and by having a larger number of branches. Branches are consistently shown to be among the most important advantages of large banks, with branch networks serving as small business lending hubs. The advantages large banks derive from these networks further emphasize the importance of physical presence and proximity in the practice of small business lending (as discussed in Section 3). Large banks are also viewed as being able to offer lower interest rates than their competitors, although large banks themselves do not view this as an important advantage.

Overall, the results of the survey confirm the widely held belief that small banks focus on relationship lending practices and view their relationships with their clients as essential to their business model. Somewhat contrary to expectations, however, large banks are also heavy users of relationship lending practices when lending to small businesses. But small banks are shown to focus more intensively on relationship lending than large banks do, and this finding suggests that small banks' approach to small business lending is distinct from the approach of large banks. If that is the case, the decreasing number of small banks in the country may disadvantage the small businesses that prefer a less transactional approach.

SECTION 5. Loan Products and Underwriting Practices

This section explores whether and to what extent the established view of small business lending—that small and large banks differ in their small business lending models—is supported by differences in loan products offered and approaches to underwriting. Understanding differences that may exist is a prerequisite for understanding how small businesses' access to credit may be affected as the U.S. banking industry changes. For example, knowing whether large banks base extensions of credit on quantifiable information may be particularly important to start-ups and other small businesses that lack a long track record of performance.[47] Therefore, to explore how small and large banks manage their small business lending, the survey asked about the small business loan products offered by banks and about banks' underwriting practices.

Specifically, the survey asked what loan products are offered by small and large banks; what needs these products meet; what underwriting criteria are evaluated; what collateral is accepted; for what reasons the bank is willing to make underwriting exceptions; does the bank require a minimum loan amount and use standardized loan products; and finally, does the bank lend to start-ups, and if so, does it underwrite such loans differently from loans made to established small businesses.

5.1 What Loan Products Does Your Bank Offer to Small Businesses?

The survey examines whether the different small business lending models of small and large banks as suggested by the established view result in different loan products being offered by the two sizes of banks. For example, one result of large banks' heavy reliance on quantifiable information may be that more large banks than small banks offer credit cards, which in turn could reduce the willingness of large banks to offer loans requiring greater staff input.

Specifically, the survey asked banks what commercial and industrial loan products they offered to small businesses in 2015 and which of these were their top product by loan volume.[48] The results show that there are few differences in the loan products that small and large banks offer to small businesses and that there are certain core loan products used by nearly all banks to extend such credit. The results also show, however, that the top products of small and large banks differ.

Figure 5.1, Panel A, shows that large majorities of both small and large banks are equally likely to offer the same loan products to small businesses, namely, lines of credit (94.6 percent and 97.9 percent), amortizing term loans (91.1 percent and 95.9 percent), and balloon term loans (84.5 percent and 79.0 percent). Although majorities of both small and large banks offer letters of credit, large banks are more likely to offer this product to their small business customers (73.2 percent for small banks, 87.5 percent for large banks).

As expected, the most notable difference is in the share of small and large banks that offer credit cards to small businesses. Large banks are more than three times as likely as small banks to offer credit cards (68.8 percent and 21.0 percent), a finding that is consistent with the established understanding that large banks rely more on automation and predetermined limits in their decisionmaking about small business loans. The underwriting of credit cards typically uses quantifiable information (such as credit scores), which can be evaluated quickly and does not

[47] See Berger et al., "Function Follow Form?," for example.

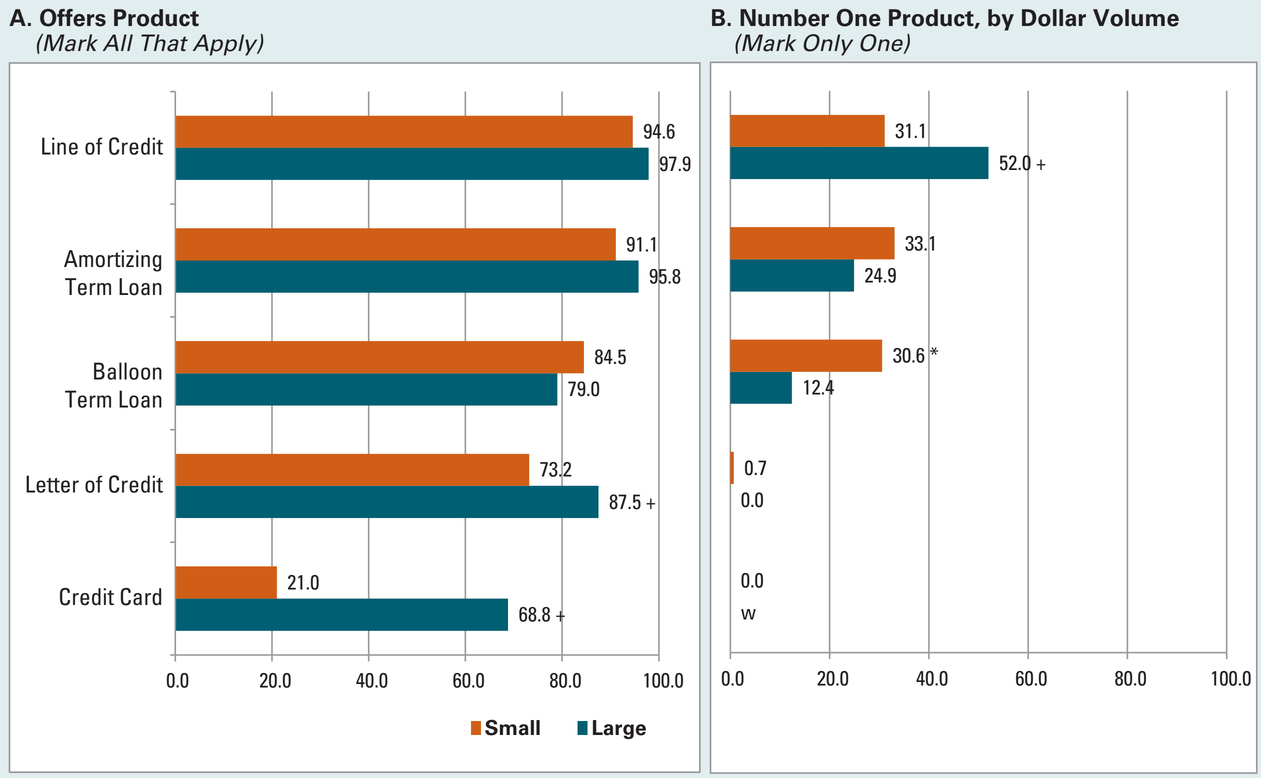
[48] A list of five products was provided; banks were also given a write-in option.

require interaction with bank staff or specialized information about the business or the local market.

In identifying their top C&I loan product to small businesses, both small and large banks cite only one of three: amortizing term loans, balloon term loans, and lines of credit. Figure 5.1, Panel B, shows that small banks are equally likely to indicate any one of the three as their number one product by volume, with about a third of small banks citing each as their top one.[49] Large banks, on the other hand, are more likely (52.0 percent) to indicate that lines of credit are their number one product by volume; amortizing term loans are a distant second (24.9 percent), and balloon term loans an even more distant third (12.4 percent). Further, lines of credit are more likely to be the top product for a larger share of large banks than small banks (52.0 percent and 31.1 percent), while balloon term loans are the top product for a larger share of small banks (30.6 percent and 12.4 percent).[50]

Overall, these results—that there are core loan products used by all banks to extend credit to small businesses but that the top products differ for the two types of banks—could imply either that the small businesses that borrow from one size bank have different needs from the small businesses that borrow from the other size bank, or that small and large banks have distinct advantages in providing

Figure 5.1: Percentage of Banks That Offer This Loan Product to Small Businesses



Source: SBLS Question 19.

Notes: Entries marked with a "w" indicate that the number of responses falls below the allowable reporting threshold for protecting respondents' identities. At the statistical significance of 10 percent, "*" denotes that small banks are more likely than large banks to offer this loan product to small businesses; "+" that large banks are more likely than small banks. In Panel A, banks may select multiple answers; results will not sum to 100.0 percent. In Panel B, banks were asked which is their number one product used by small businesses, by dollar volume of originations in 2015.

[49] The testing of differences between the shares of small banks indicating one of these three products over another as their number one loan product by volume did not reveal statistically significant differences.

[50] There is no statistically significant difference between small and large banks in their likelihood of having amortizing term loans as their top product.

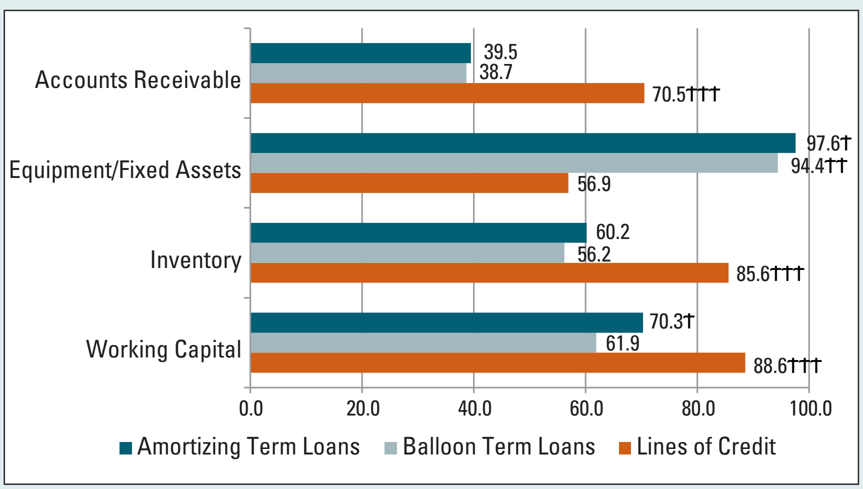
balloon term loans (small banks) or lines of credit (large banks).

5.2 For What Purposes Do Small Businesses Use These Products?

Small businesses use credit to meet different needs. Some are longer term, such as equipment purchases, and others are shorter term, such as accounts receivable, and different loan products may be better suited for one purpose over another. Thus, the survey asked about the purposes for which the top loan products are used. While there is substantial overlap in the purposes for which all types of loans are extended, the results (see Figure 5.2) show that term loans (both amortizing and balloon) are most often extended for longer-term purchases of equipment or other fixed assets and that lines of credit are most often extended for shorter-term purposes. Because the findings reveal that small and large banks generally do not differ much in the purposes for which specific loan products are extended, the results for small and large banks are combined here.

Specifically, almost all banks with amortizing or balloon term loans as their top product report that these loans are typically used to support the financing of longer-term asset purchases such as equipment (97.6 percent for amortizing term loans, 94.4 percent for balloon term loans).[51] By contrast, about half, 56.9 percent, of banks with lines of credit as their top product see these loans as financing equipment purchases. Instead, lines of credit are more often used to finance day-to-day operations, such as accounts receivable (70.5 percent), inventory (85.6 percent), and working capital (88.6 percent).[52] These shares are between 18 and 30 percentage points higher than for banks whose top product is either of the two types of term loans. While small sample sizes prohibit detailed comparisons between small and large banks split by top loan product for term loans, an analysis

Figure 5.2: Percentage of Banks That Cite This as the Purpose for Which Their Number One Loan Product to Small Businesses Was Used
(All Banks Combined)



Source: SBLS Question 22C.

Notes: At the statistical significance of 10 percent, "†" denotes that amortizing term loans are more likely than balloon term loans and lines of credit to be used to purchase equipment/fixed assets, and more likely than balloon term loans to be used for working capital; "††" that balloon term loans are more likely than lines of credit to be used to purchase equipment/fixed assets; "†††" that lines of credit are more likely than amortizing and balloon term loans to be used for accounts receivable, inventory, and working capital. Banks may select multiple answers; results will not sum to 100.0 percent.

[51] Statistically, the share of banks that report financing equipment/fixed assets with amortizing term loans is significantly higher than the share of banks that report any of the other three loan purposes, tested separately. This is true for both small banks and large banks. The number of large banks with balloon term loans as their top product fell below the threshold for protecting respondents' identities, and therefore the difference between small and large banks could not be tested.

[52] When lines of credit are a bank's number one product, there are statistically significant differences among loan purposes except between working capital and inventory.

(not shown) of the loan purposes for lines of credit shows that both small and large banks are more likely to use lines of credit for shorter-term purposes.

These results, coupled with the tendency of large banks to extend lines of credit more often than small banks do, suggest that small banks may play a larger role in financing long-term investments by small businesses. It is therefore possible that the continuing shift from small banks to large banks could pose problems for small businesses that are attempting to grow.

5.3 Which Underwriting Criteria Are Used by Your Bank to Evaluate Small Business Borrowers?

The survey investigates differences in the underwriting criteria used by small and large banks because the established view implies separate approaches to small business lending. And differences in criteria may produce differences in access to loans. For example, if large banks satisfy their evaluation criteria by requiring standard information, some small businesses may find it harder than others to provide such information. Specifically, the survey asked banks to indicate how often they use specific underwriting criteria to evaluate small businesses for their top loan product.[53]

The results show that banks of all sizes assess a wide variety of underwriting criteria in evaluating small businesses for loans, and the set of criteria does not typically differ by bank size. Figure 5.3 shows that, for 11 of the 14 possible criteria provided by the survey, large majorities of both small and large banks "always" or "almost always" evaluate each criterion. The findings suggest that banks of all sizes use most of the quantifiable information available to them to evaluate the creditworthiness of their small business applicants.

However, some differences between small and large banks exist. Small banks are statistically more likely than large banks to evaluate traditional loan and owner characteristics, namely, loan debt-service coverage (95.7 percent and 78.5 percent), loan-to-value (95.0 percent and 74.3 percent), owner net worth (93.2 percent and 82.9 percent), and owner debt-to-worth (70.0 percent and 57.5 percent). Large banks are more likely than small banks to evaluate personal guarantees (95.7 percent and 86.2 percent), owner credit score (91.6 percent and 79.2 percent), and business age (87.4 percent and 71.3 percent). The largest difference between small and large banks is in the use of business credit score. Whereas 64.1 percent of large banks indicate that they always or almost always evaluate business credit score, only 14.8 percent of small banks do. Further, business credit score is the criterion least often cited by small banks. Overall, these differences suggest that firms whose owners have a lower credit score and fewer outside resources, and firms that are younger, may be more likely to obtain funding at a small bank.

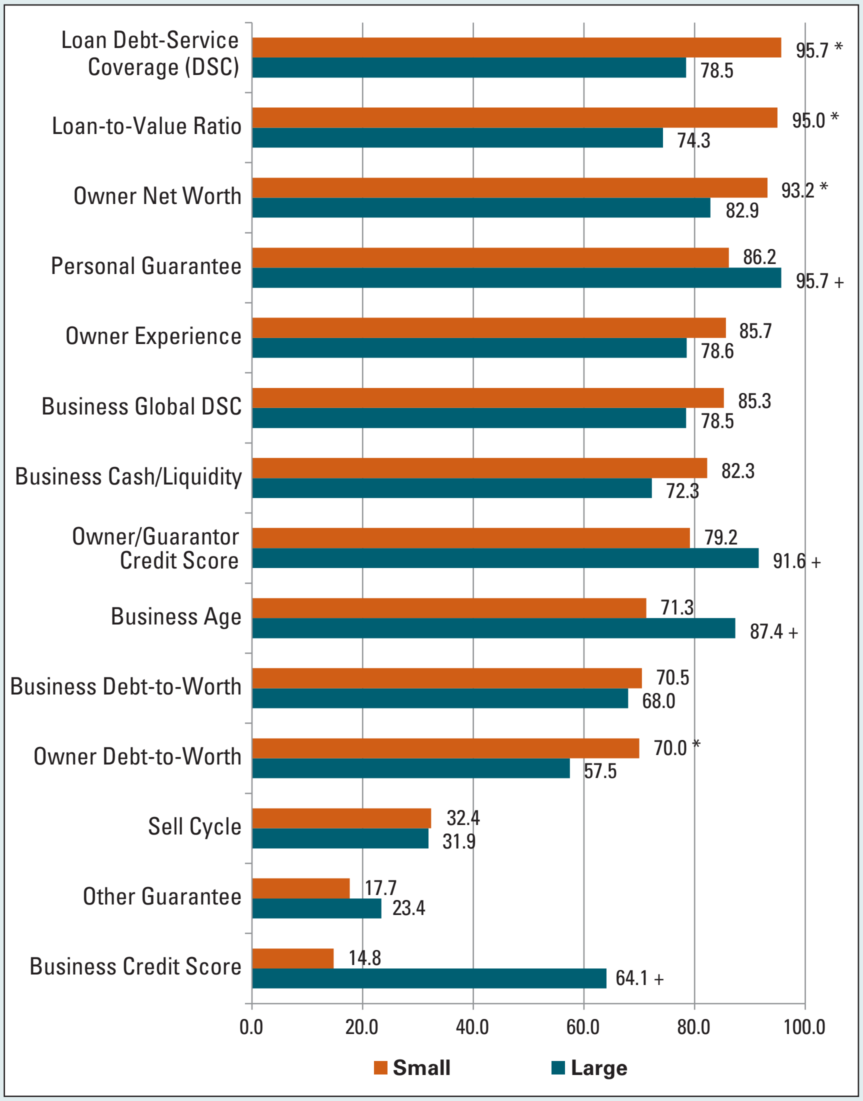
5.4 What Collateral Does Your Bank Accept from Small Businesses?

Another aspect of underwriting that may reflect the distinct approaches of small and large banks to small business lending is the collateral accepted. For example, the standardized approach of large banks may make them reluctant to lend against collateral whose value is not easily established or that is not easily sold. Differences, if any, in the types of collateral typically accepted will bear on the question of whether, as the local composition of banks changes, certain types of firms will have more trouble securing a small business loan. Thus, the survey asked banks to describe what collateral they commonly accept—or to indicate if they commonly accept no collateral—for their top loan product.[54]

[53] The survey asked whether the underwriting criteria they use are the same across the types of products they offer, even if the limits for approval are different. Majorities of both small and large banks (91.1 percent and 66.5 percent) say they use the same underwriting criteria across loan products. Since the same criteria are used across products, the discussion here of underwriting criteria combines answers across the three top loan products. Note, however, that although majorities of both small banks and large banks say they use the same underwriting criteria across products, the proportion of large banks doing so is considerably smaller than the proportion of small banks—a result implying that large banks are more likely to use different standards by product.

[54] Banks were offered eight collateral options, and were also given a write-in option.

Figure 5.3: Percentage of Banks That "Always" or "Almost Always" Use This Underwriting Criterion to Evaluate Small Business Loan Applicants for Their Number One Loan Product to Small Businesses



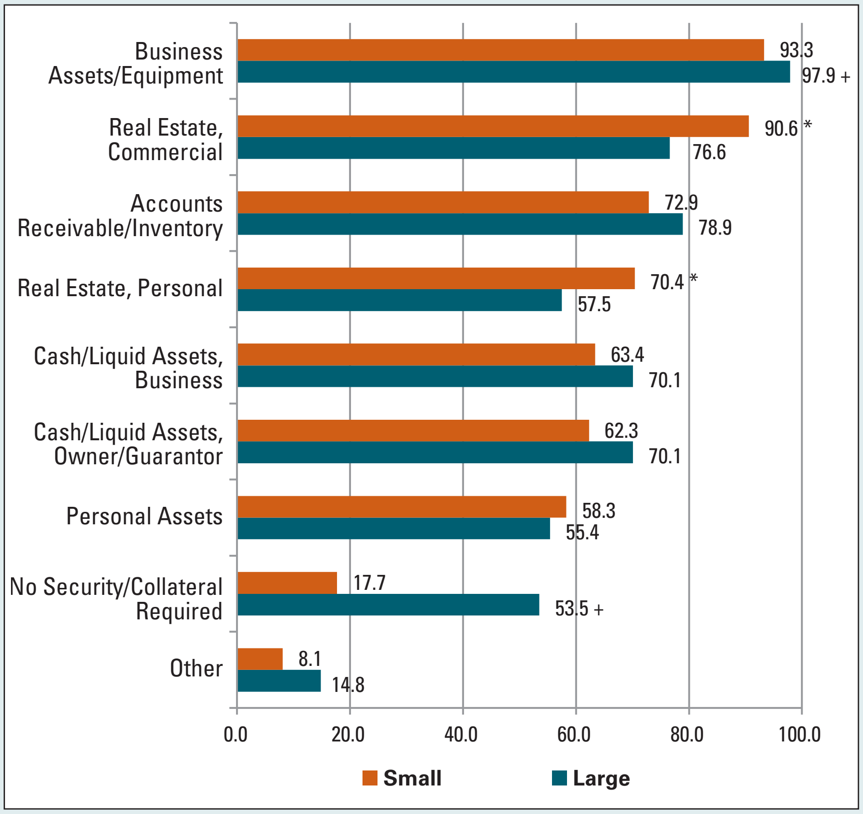
Source: SBLS Question 22E.

Notes: At the statistical significance of 10 percent, "*" denotes that small banks are more likely than large banks to "always" or "almost always" use this underwriting criterion to evaluate loan applicants for their number one loan product to small businesses; "+" that large banks are more likely than small banks. Banks may select multiple answers; results will not sum to 100.0 percent.

The results, which are reported in Figure 5.4, show that majorities of both small and large banks accept nearly all types of collateral. However, there are a few small statistical differences. Large banks are slightly more likely than small banks to accept business assets (97.9 percent and 93.3 percent). Small banks are more likely than large banks to accept real estate collateral, both commercial real estate (90.6 percent and 76.6 percent) and personal real estate (70.4 percent and 57.5 percent). The widespread acceptance of real estate–related collateral and the "localness" of small banks' small business borrowers (discussed in Section 3) reinforce the notion that small banks are tied to the outcomes of their local communities.

There is also one large difference: large banks are three times as likely as small banks to commonly accept no collateral for their small business loans (53.5 percent and 17.7 percent). This result is consistent with the expectation that small banks rely more heavily on collateral to mitigate the risk of lending to small businesses, since large banks are better able to mitigate risks by lending in multiple markets and making a high volume of loans. This result is also consistent with findings that large

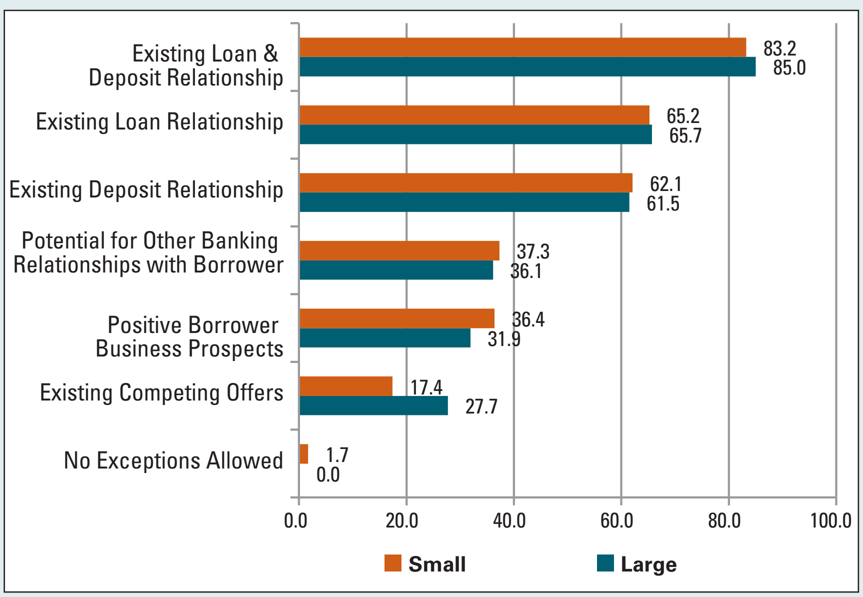
Figure 5.4: Percentage of Banks That Commonly Accept This Collateral for Their Number One Loan Product to Small Businesses



Source: SBLS Question 22D.

Notes: At the statistical significance of 10 percent, "*" denotes that small banks are more likely than large banks to commonly accept this collateral for their number one loan product to small businesses; "+" that large banks are more likely than small banks. Banks may select multiple answers; results will not sum to 100.0 percent.

Figure 5.5: Percentage of Banks That Cite This as a Typical Reason to Make Exceptions to Loan Policy for Their Number One Loan Product to Small Businesses



Source: SBLS Question 22F.

Notes: At the statistical significance of 10 percent, "*" denotes that small banks are more likely than large banks to cite this as a typical reason to make exceptions to loan policy for their number one loan product to small businesses; "+" that large banks are more likely than small banks. Banks may select multiple answers; results will not sum to 100.0 percent.

banks are more likely to lend to large, mature firms, which typically have more established credit records.[55]

5.5 When Is Your Bank Willing to Make an Underwriting Exception for a Small Business?

Under certain circumstances, banks may be willing to make exceptions to their internal underwriting policy. The use of exceptions, therefore, is another area in which small and large banks may have distinct approaches to small business lending. Small banks collect nonstandard data while regularly interacting with small firms, and this "soft" information may be used to grant exceptions to underwriting policy. In contrast, large banks' reliance on standard information and predetermined thresholds makes it hard to predict a basis on which exceptions would be made. Thus, the survey asked banks to cite the circumstances under which they are willing to deviate from their usual underwriting practices.[56] Perhaps surprisingly, both small and large banks reported that exceptions to underwriting policy are most likely considered because of a previous relationship with the small business borrower. Further, the results show that small and large banks have statistically equal percentages for each of the reasons for allowing exceptions to underwriting policy.

Figure 5.5 shows that large majorities of both small banks (83.2 percent) and large banks (85.0 percent) say that a combined existing loan and deposit relationship is a reason to make an exception to underwriting policy. In addition, about two-thirds of both small and large banks say that an existing loan relationship (65.2 percent and 65.7 percent) or an existing deposit relationship (62.1 percent and 61.5 percent) alone is a reason to make an exception. These findings, while consistent with the expectations for small banks, are somewhat unexpected for large banks.[57] Nonetheless, they suggest that maintaining relationships in conducting small business lending is important to both small and large banks.

About one-third each of small and large banks also consider potential for other banking relationships with borrower (37.3 percent and 36.1 percent) and positive business prospects for the borrower (36.4 percent and 31.9 percent) as reasons for underwriting exceptions, and smaller shares take into account existing competing offers (17.4 percent and 27.7 percent).

5.6 Does Your Bank Require Minimum Loan Amounts and Use Standardized Loan Products?

An important potential difference between small and large banks stemming from their distinct approaches is the way they manage loan requests from small businesses, and specifically whether they apply preset criteria. Two common preset criteria are a required minimum loan amount and the use of standardized loan products. Small banks' use of nonstandard information may lead to greater flexibility and willingness to customize loans according to the individual needs of a small business. Large banks' use of predominantly standard data may enable a high-volume, economies-of-scale model, with the fixed administrative costs of underwriting covered by the use of a required minimum loan amount or minimized by the use of standardized products that have a preset structure and preset offered terms. Therefore, the survey explores differences between small and large banks in the use of loan amount floors and standardized small business loan products.[58] The results show that large banks are indeed more likely to use both.

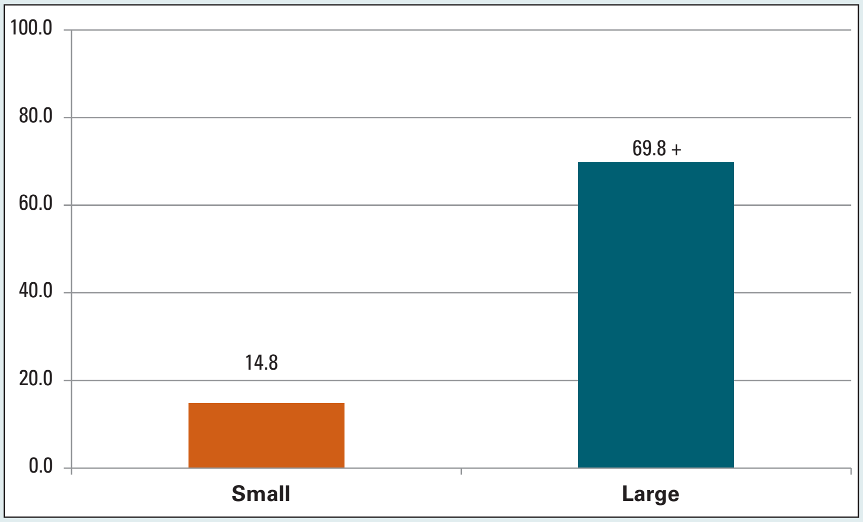
55 See, for example, Haynes, Ou, and Berney, "Small Business Borrowing," or Berger et al., "Function Follow Form?"

56 Banks were provided with a list of eight possible options, and were also given a write-in option. Although large majorities of both small and large banks reported "Strong Mitigating Factors," the option is dropped in this discussion because it was subsequently deemed to include almost all the other options.

57 Note, however, that the survey asked about reasons for exceptions rather than the frequency with which banks make exceptions.

58 Standardized loan products are ones in which the terms of the loans are preset and the criteria for suitability and approval are easily measurable and predetermined.

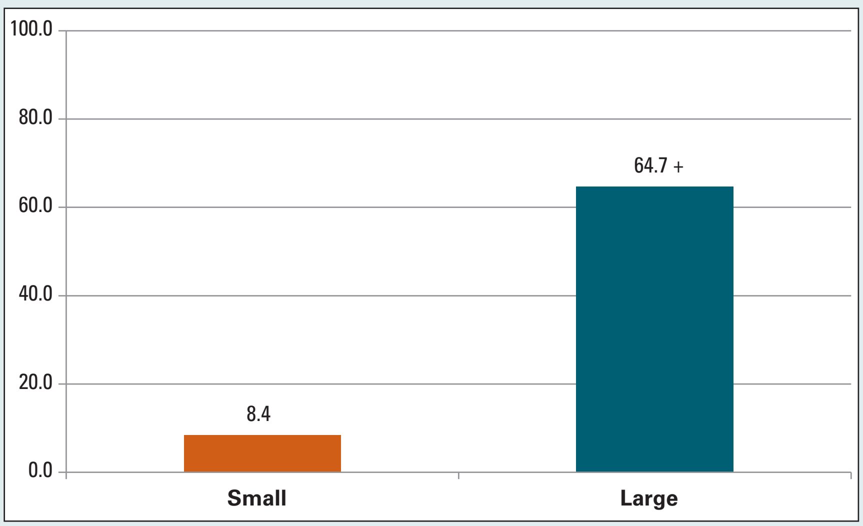
Figure 5.6: Percentage of Banks That Require a Minimum Loan Amount for Their Number One Loan Product to Small Businesses



Source: SBLS Question 22B.

Notes: At the statistical significance of 10 percent, "+" denotes that large banks are more likely than small banks to require a minimum loan amount for their number one loan product to small businesses.

Figure 5.7: Percentage of Banks That Use Standardized Small Business Loan Products



Source: SBLS Question 5.

Notes: At the statistical significance of 10 percent, "+" denotes that large banks are more likely than small banks to use standardized small business loan products.

Figure 5.6 shows the share of banks that require a minimum loan amount for their top loan product to small businesses. Only a small share (14.8 percent) of small banks require a minimum loan amount for their top loan product to small businesses, compared with a majority (69.8 percent) of large banks. This finding suggests that a small business needs to request a loan of a certain size at most large banks before the bank is willing to consider making a loan. The findings also support the view that small banks remain flexible when evaluating a potential small business borrower.

Figure 5.7 shows the share of banks that use standardized loan products. As expected, a majority of large banks (64.7 percent) use such products. While only a modest share (8.4 percent) of small banks use standardized products, within the group of small banks as a whole there are differences by size. In fact, the likelihood of using standardized loan products grows with size. Only 3.8 percent of banks with less than $250 million in assets use standardized loan products (not shown), but 11.6 percent of banks with assets between $250 million to $1 billion do, and

27.3 percent of banks with assets between $1 billion and $10 billion do as well.[59] The advantages to small businesses from using standardized loan products are that the underwriting can be quicker to process and the products can offer more competitive interest rates. The disadvantages are that only a subset of small businesses may be able to satisfy the standard criteria required to qualify for them, and the small businesses seeking the loans may prefer loan terms different from the ones offered.

5.7 Does Your Bank Lend to Start-Ups, and if so, Do You Underwrite the Loans Differently from Loans for Established Small Businesses?

New small businesses—start-ups—are central to the concern about whether small and large banks' distinct approaches to small business lending produce differences in access to small business loans. When start-ups survive, they create more net jobs in the United States than businesses of any other age group, and start-ups have higher rates of employment growth and productivity growth than older firms. The likelihood of their survival increases with their access to credit.[60] Yet start-ups lack much of the standardized information used to underwrite loans, and therefore the nonstandard information used by small banks may be especially important for new firms' access to bank credit. As noted above, several studies conclude that large banks are less likely than small banks to lend to small, young firms, and more likely to lend to large, mature firms.[61] To address the issue of how the growth in large banks' share of bank assets might affect start-ups' ability to access financing, the survey asked banks about their underwriting practices for loans to new small businesses.

Most banks define start-ups as younger than two years,[62] and the survey finds that most banks make loans to start-ups. Figure 5.8 shows that 79 percent of small banks and 73.2 percent of large banks make such loans. The statistically equal likelihood of small and large banks lending to start-ups is somewhat surprising, given the advantages that small banks are thought to have in using nonstandard information to overcome the data constraints of new businesses. However, a reported willingness to lend does not necessarily indicate the level of actual lending to start-ups.

To minimize the risk associated with lending to an untested new business, banks may require start-ups to meet additional underwriting criteria, and this requirement, in turn, may create substantial barriers to actually obtaining a loan. Thus, the survey asked banks an open-ended question to describe any differences between the underwriting criteria used for start-ups and those used for established small businesses.

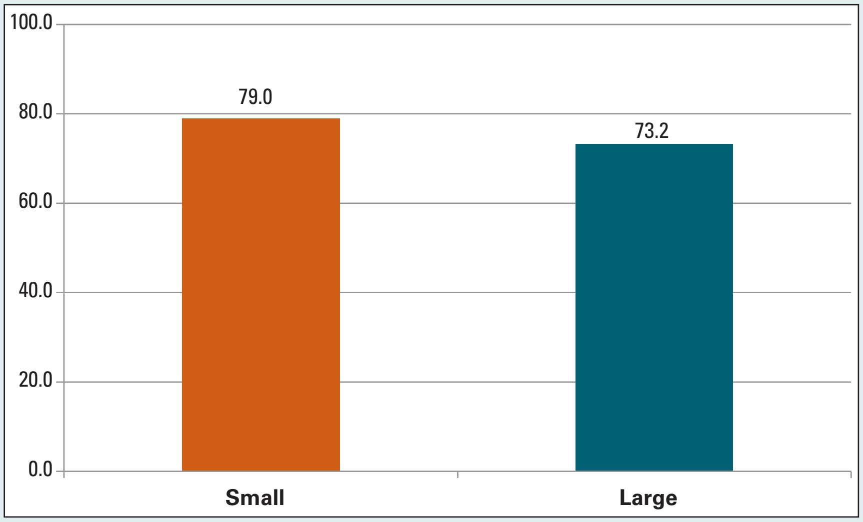
59 These differences are statistically significant.

60 On net job creation, see Tim J. Kane, "The Importance of Startups in Job Creation and Job Destruction," Kauffman Foundation Research Series, Firm Formation and Economic Growth, July 2010, http://dx.doi.org/10.2139/ssrn.1646934. On employment growth, see John Haltiwanger, Ron S. Jarmin, and Javier Miranda, "Who Creates Jobs? Small versus Large versus Young," *Review of Economic and Statistics* 95, no. 2 (2013): 347–61, https://doi.org/10.1162/REST_a_00288. On productivity growth, see Alon et al., "Older and Slower." On the relationship between survival and access to credit, see Alicia M. Robb and David Robinson, "The Capital Structure Decision of New Firms," *Review of Financial Studies* 27, no. 1 (2014): 153–79; Jeongsik J. Lee and Wei Zhang, "Financial Capital and Startup Survival," *Academy of Management Proceedings* 2011, no. 1 (2017), https://doi.org/10.5465/ambpp.2011.65869494; Traci Mach and John D. Wolken, "Examining the Impact of Credit Access on Small Firm Survivability," Federal Reserve Board, Finance and Economics Discussion Series, Working Paper No. 35 (2011), http://dx.doi.org/10.2139/ssrn.1956696; and Rebel A. Cole and Tatyana Sokolyk, "How Do Firms Choose Legal Form of Organization? Evidence from the Kauffman Firm Surveys," Working Paper (July 16, 2018), https://ssrn.com/abstract=2028176.

61 Again, see, for example, Haynes, Ou, and Berney, "Small Business Borrowing," or Berger et al., "Function Follow Form?"

62 The survey finds that the median age under which both small and large banks state they define a start-up is two years. The mean age is also two years. However, small banks have slightly more variance across quartiles. Whereas large banks at the 25th and 75th percentile consider businesses under two years of age to be a start-up, small banks at the 25th percentile consider businesses under one year of age to be a start-up, and those at the 75th percentile consider businesses under three years of age to be a start-up. (See SBLS Question 21a.)

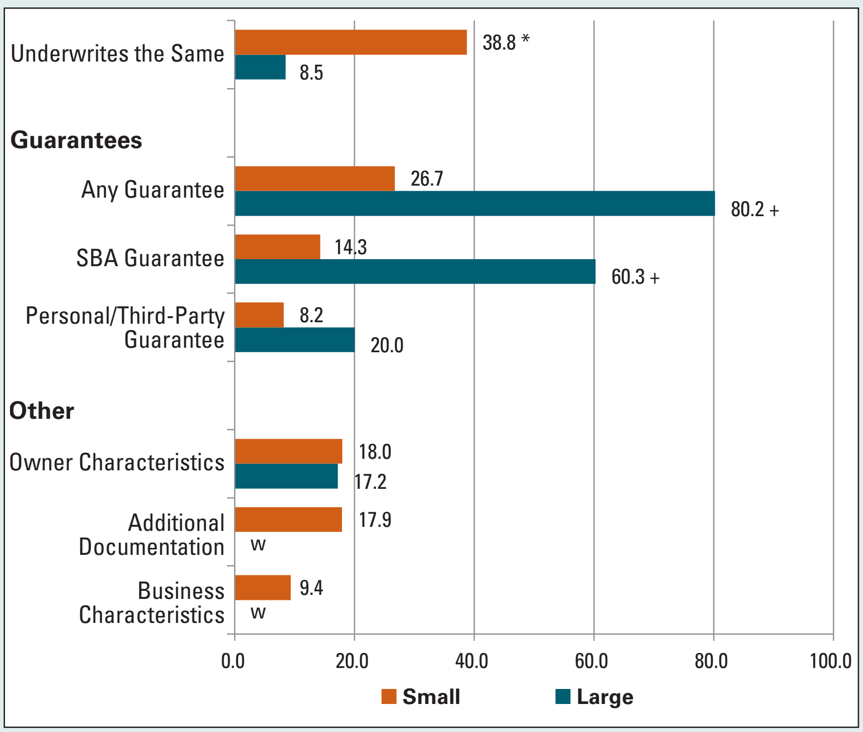
Figure 5.8: Percentage of Banks That Make C&I Loans to Start-Up Small Businesses



Source: SBLS Question 21C.

Notes: At the statistical significance of 10 percent, small and large banks are equally likely to make C&I loans to start-up small businesses.

Figure 5.9: Percentage of Banks That Underwrite Start-Up Small Businesses Differently from Established Small Businesses, Using a Practice in This Category



Source: SBLS Questions 21C1 and 21C1a.

Notes: Entries marked with a "w" indicate that the number of responses falls below the allowable reporting threshold for protecting respondents' identities. At the statistical significance of 10 percent, "*" denotes that small banks are more likely than large banks to underwrite start-up small businesses differently from established small businesses using this practice; "+" that large banks are more likely than small banks. Underwriting categories aggregate individual bank responses to an open-ended question; results will not sum to 100.0 percent. Although banks were asked this question only if they had responded "yes" to whether they underwrite start-up small businesses differently from established small businesses, the numbers reported in the figure show percentage shares for all banks.

Most banks underwrite loans to start-ups differently from how they underwrite other small business loans, but large banks are much more likely to do so than small banks. Figure 5.9 shows that less than 10 percent of large banks report using the same underwriting procedures for start-ups as for established small businesses, whereas a substantial share of small banks use the same procedures (38.8 percent).

Large banks are also much more likely than small banks to mention looking for guarantees as part of their additional underwriting process for start-ups. More than 80 percent of large banks say they explore *some* form of additional guarantee, including Small Business Administration (SBA) guarantees, compared with only 26.7 percent of small banks. Large banks show particular interest in SBA support, with 60.3 percent mentioning these programs as an additional criterion, compared with only 14.3 percent of small banks.

In contrast, small banks describe using more diverse and generally "softer" additional criteria for underwriting start-ups. These include requiring additional documentation such as business plans (17.9 percent), or looking at business characteristics such as the start-up's industry or the quality of its management (9.4 percent).[63] Whereas small and large banks are equally likely (18.0 percent and 17.2 percent) to describe aspects of owner characteristics in their additional criteria, small banks use a greater variety of terms in this category, such as education, training, or personal credit history.[64] These differences between small and large banks suggest that small banks are more flexible in underwriting start-up loans.

5.8 Conclusions

This section investigates whether small and large banks differ in how they conduct their small business lending, and if they do differ, whether some small businesses are potentially better served by small banks. Inasmuch as some small banks have been shown to use a wider range of information to underwrite loans, one would expect that start-ups and less established small businesses are more likely to gain access to credit from these small banks. Although the survey results show differences between small and large banks that suggest the possibility that less established small businesses may benefit more from the approach used by small banks, the results also indicate a high degree of commonality between the approaches taken by the two sizes of banks.

The survey supports the understanding that small banks are relationship lenders and approach small business lending in a more flexible and customized, case-by-case way compared with large banks; and a result of this approach may be that less established firms are more likely to receive credit. Small banks are found less likely than large banks to use minimum loan amounts on their top products or to rely on standardized loan products. And small banks are more likely than large banks to accept real estate collateral, a practice that is consistent with small banks' having a more intimate knowledge of their local communities. Further, small banks often lend to start-ups using the same underwriting criteria they use for established small businesses; alternatively, they often evaluate a wide set of additional information, including relationship-based soft information such as owner's experience or the management team's skills.

The survey also supports the understanding that large banks are transactional lenders and rely on standardization in their small business lending decisionmaking, thus facilitating a high-volume, economies-of-scale business model and perhaps screening for more established firms—the ones most likely to meet the standards and to have the quantifiable data to show that they do. Large banks are much more likely than small banks to evaluate business credit score, require minimum loan amounts, and use such standardized loan products as credit cards. Further, when large banks do lend to start-ups, the criteria they use are almost always different from the criteria they use for established small businesses, particularly with respect to requests for outside guarantees.

Yet, despite the findings suggesting that small and large banks use distinct models for small business lending, there are also notable areas of commonality. The most surprising commonality is that for both sizes of banks, existing relationships are a

63 However, the significance of the difference between the shares of small and large banks that consider additional documentation or business characteristics cannot be reported, because the number of large banks doing so falls below the threshold for protecting respondents' identities.

64 This diversity mirrors the varied ways in which small banks describe their small business borrowers (as discussed in Section 2), and may reflect how small banks are more attuned to the local economic environment or to the individual borrower.

dominant reason for allowing exceptions to loan policy. In addition, small and large banks generally offer the same types of loan products, use similar underwriting criteria to evaluate small business borrowers, and accept the same collateral, with a few exceptions. Thus, although small and large banks may approach small business lending using distinct business models, as seen in Section 4 and as shown here, the process appears to involve many common elements and be somewhat relational in nature for both small and large banks.

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APPENDIX A. Survey Methodology

The data source for this report is the Small Business Lending Survey (SBLS), a newly-designed, large-scale, nationally-representative survey of small business lending practices in the banking industry. The Federal Deposit Insurance Corporation (FDIC) undertook this survey of banks in order to provide new insights into many aspects of small business lending for which information is not already collected, including how banks define small businesses, interact with their small business customers, perceive their competition, view the dimensions on which they compete for small business loans, and underwrite their loans, including loans to startups. Additionally, the SBLS was intended to cover small business lending at all banks and to explore differences across small and large banks.

The SBLS was developed by the FDIC in consultation with survey experts at the U.S. Census Bureau. Throughout 2015, the FDIC and the Census Bureau conducted three rounds of interviews with 40 banking institutions of various sizes in both rural and urban areas in ten states during the survey development phase. The interviews were conducted to ensure that the survey questions were understood by bank personnel, that the information gleaned from the questions matched the intent of the researchers, and to ensure that the requested information could be provided by the respondents using a reasonable amount of bank resources. The survey was estimated to take 3 to 6 hours to complete, depending on the size and complexity of the respondent bank. In the first half of 2016, the Census Bureau tested the usability of the web interface used to administer the survey to ensure that it functioned as intended.

Data collection for the SBLS was conducted by Census Bureau between June 2016 and January 2017. The data collection was conducted entirely online through the Census Bureau's Centurion data collection website. The survey instrument can be found in Appendix C.

A.1 Sample Selection

The universe of banks covered by the SBLS was constructed using the December 2015 Report of Condition and Income (Call Report) and the June 2014 Summary of Deposits (SOD) data. All banks that met the following criteria were included in the universe:

1. Present in both the December 2015 Call Report and the June 2014 SOD data.
2. Had at least one branch in a U.S. state or in the District of Columbia.[65]
3. Had positive total net outstanding loans.
4. Was a FDIC-insured institution.
5. Had positive core deposits.
6. Was a commercial bank, consumer bank, mutual savings bank, stock savings bank, mutual savings & loan, stock savings & loan, cooperative bank, credit card company, finance company, commercial credit company, agricultural credit company, or a leasing company.[66]

This resulted in a universe of 6,018 banks out of the 6,182 banks extant in the December 2015 Call Report. The universe was then stratified along two dimensions: 1. Total asset size, and 2. Whether the majority of the institution's deposits were in branches located within a metropolitan statistical area (MSA). Combining these two dimensions created eight strata, the characteristics of which are summarized in Columns (1) through (3) of Table A.1. Column (4) gives the number of banks in the universe of each stratum.

[65] Some banks included in the Call Report and Summary of Deposits exclusively have branches in U.S. territories.

[66] The sixteen "banker's banks" existing at the time were excluded from the universe.

Table A.1: Frame and Initial Sample, by Stratum

Stratum	Assets	Deposits held in MSA	Universe	Initial Sample Size	Percent of Stratum in Sample	Adjusted Sample Size	Number of Respondents	Stratum Response rate
1	Less than $250M	Over 50%	1,499	397	26.5%	388	227	58.5%
2		Under 50%	2,061	413	20.0%	407	253	62.2%
3	$250M to Less Than $1B	Over 50%	1,104	376	34.1%	369	214	58.0%
4		Under 50%	693	336	48.5%	333	194	58.3%
5	$1B to Less Than $10B	Over 50%	483	301	62.3%	291	181	62.2%
6		Under 50%	85	84	98.8%	83	53	63.9%
7	$10B to Less Than $50B	Any	60	60	100%	58	34	58.6%
8	$50B or More	Any	33	33	100%	32	18	56.3%
Total			6,018	2,000	33.2%	1,961	1,174	59.9%

The sampling methodology drew a disproportionate stratified random sample for Strata 1 through 6 (covering all banks with less than $10 billion in assets) and a "certainty" sample for Strata 7 and 8, which contain all the largest banks.[67] This methodology was employed in order to ensure that the SBLS could produce accurate estimates for large banks. The sample sizes for Strata 1 through 6 were assigned based on power calculations conducted by the U.S. Census Bureau.[68] The distribution of the initial sample of 2,000 banks is given in Column (5) of Table A.1. While the survey was conducted, 39 banks that were initially included in the sample had closed, were uncontactable, or were found to be out of the scope of the survey because they had no branches in a state or in the District of Columbia. These institutions were removed from the sample for a final sample of 1,961 banks, as shown in Column (7) of Table A.1.

The banks selected in the sampling process were sent an advance contact letter and an initial survey request by mail, which introduced the study and outlined the procedures for logging on to the Census Bureau's data collection website to respond to the survey. Sampled banks which did not respond within 45 days of the beginning of the response period received follow-up letters and telephone calls.

A.2 Survey Response Rate

Of the 1,961 banks present in the adjusted sample, 1,174 (59.9 percent) responded to the survey.[69] This response rate meets the Census Bureau's standards for quality control.[70] The response rates varied slightly between strata, ranging from 56.3 percent for Stratum 8 to 63.9 percent for Stratum 6 (see column 9 of Table A.1). However, none of the differences in response rates between strata were statistically significant at the 10 percent confidence level.

67 "Disproportionate" indicates that probability of selection into the sample is different for banks in different stratum.

68 Power calculations estimate how many banks are required to sample in each strata in order to yield a desired level of precision.

69 A bank was considered to have responded to the survey if it gave a response to question 2, the first non-qualitative question in the main survey. See below for an analysis of question-by-question response rates.

70 See Sub-requirement F1-6.2b of U.S. Census Bureau Statistical Quality Standards.

The overall incidence of survey nonresponse meets the Census Bureau standards for quality control. While the response rate meets the Census Bureau's standards, there may still be some concern about nonresponse bias. To address this concern, the banks in the adjusted sample were compared to the subset of banks that responded to the survey, based on information available in the Call Report and the SOD. Table A.2 shows how sample banks differed from respondent banks within each stratum based on 20 relevant characteristics.

Overall, directly testing for significant differences between respondent and non-respondent banks in each stratum finds that only 22 out of 160 tests (13.8 percent) were significant at the 10 percent confidence level, only slightly greater than would be expected to be found by random chance. The most notable difference is that, in Strata 7 and 8, banks with more employees per $100 million in assets and that were specialized in commercial lending were more likely to respond to the survey.

Table A.2: Mean Values for Sample and Respondent Banks, by Stratum

Characteristics	Stratum 1			Stratum 2			Stratum 3			Stratum 4		
	Resp	Sample	Sig	Resp	Sample	Sig	Resp	Sample	Sig	Resp	Sample	Sig
Ln(assets)	4.7	4.7		4.5	4.5		6.1	6.1	+	6.1	6	
Employees per $100M assets	24.2	24.5		24.1	24.5		22.4	24.8		24.1	24	
Branches per $100M assets	2.4	2.4		3	2.9		1.5	1.5		1.9	1.9	
Asset growth rate, 3yr annualized	3.2	3		2.5	2.7		7.6	7.2		4.5	4.8	
Asset allocation (%)												
…C&I loans	8.1	7.9		6.7	6.9		8.7	8.9		7.7	7.5	
…CRE loans	17.7	17		8.6	9.1		23.5	22.7		16.2	16.1	
… C&I and CRE loans	25.8	24.9		15.2	16	+	32.2	31.5		23.9	23.6	
Market area population (%)												
… in MSA	95.5	95		13.6	13.5		94.6	94		31.4	33.1	
… in LMI census tract	24	25.4		16.1	16.3		27.3	26.6		19.5	18.8	
… black non-Hispanic	9.1	9.4		6.7	6.3		9.6	10.2		7.6	7.5	
… Hispanic	9.2	9.6		5.6	6.9	**	13.3	12.9		6.9	7.6	
… minority	23.9	24.6		15.5	16.5		30.2	30.1		18.5	19.3	
% of deposits in MSA branches	97.2	96.7		3.7	3.8		93.3	92.8		12.3	12.2	
Specialization (%)												
Agriculture	18.9	18.6		52.6	50.9		4.2	3.8		26.3	27.3	
Commercial	56.8	53.9		20.2	21.9		75.7	75.3		52.1	51.7	
Mortgage	9.7	9.8		9.1	7.1	*	9.8	9.8		6.2	4.8	
Headquarter location (%)												
Midwest	8.8	9.3		2	2		21	20.6		10.8	9.6	
Northeast	48	46.6		58.5	55	+	26.6	28.2		43.8	42	
South	32.2	32.2		32.4	35.1		39.3	40.7		37.6	39.6	
West	11	11.9		7.1	7.9		13.1	10.6	+	7.7	8.7	

Notes: A "+" denotes statistical significance at 10 percent; "*" at 5 percent; "**" at 1 percent. Hypothesis tests compare differences between respondents and non-respondents.

Table A.2 (cont): Mean Values for Sample and Respondent Banks, by Stratum

Characteristics	Strata 5			Strata 6			Strata 7			Strata 8		
	Resp	Sample	Sig	Resp	Sample	Sig	Resp	Sample	Sig	Resp	Sample	Sig
Ln(assets)	7.8	7.7		7.5	7.5		9.9	10		11.9	12.1	
Employees per $100M assets	17.5	18.7	+	21.3	21.7		14.9	12.9	*	12.5	10.9	*
Branches per $100M assets	1.1	1.2	*	1.6	1.7	*	0.8	0.7	+	0.6	0.5	
Asset growth rate, 3yr annualized	10.9	10.8		8	8.3		14.5	13.4		7.9	6.6	
Asset allocation (%)												
...C&I loans	11.7	11.1		8.6	8.9		14.9	14		16.3	15.9	
...CRE loans	22.3	21.6		18.5	18.9		15.7	14		8.5	6.8	*
... C&I and CRE loans	34	32.7	+	27.1	27.9		30.5	28	+	24.9	22.7	
Market area population (%)												
... in MSA	93.5	93.5		58.9	58.1		93.3	94.6	+	94.7	95.8	+
... in LMI census tract	26.1	26.2		22.8	22.2		28.6	28.2		30.6	31.8	
... black non-Hispanic	9.5	9.7		6.2	7.5		11.7	10.5		11.1	11.1	
... Hispanic	14.3	14.9		8.8	7.8		17	16.4		17	16.4	
... minority	33.3	33.5		20.3	20.3		40	39.1		39	38.1	
% of deposits in MSA branches	91.5	91.3		28.3	28.1		90.5	92.4		95.2	96.5	*
Specialization (%)												
Agriculture	1.7	1		17	19.3		0	1.7		0	0	
Commercial	85.1	84.9		69.8	68.7		85.3	70.7	**	77.8	62.5	*
Mortgage	6.6	6.9		3.8	2.4		5.9	10.3		0	0	
Headquarter location (%)												
Midwest	27.6	24.7		26.9	22		21.2	24.6		11.1	18.8	
Northeast	27.1	28.2		34.6	35.4		24.2	21.1		22.2	28.1	
South	26.5	31.6	*	26.9	32.9		30.3	31.6		44.4	34.4	
West	18.8	15.5	*	11.5	9.8		24.2	22.8		22.2	18.8	

Notes: A "+" denotes statistical significance at 10 percent; "*" at 5 percent; "**" at 1 percent. Hypothesis tests compare differences between respondents and non-respondents.

A.3 Item Response Rate

In addition to the high survey response rate, most questions also exhibited a high item response rate, where item response rate is defined as the proportion of banks that were asked the question that actually answered the question. Figure A.1 shows the overall unweighted item response rate by question.[71,72] Item response rates were high across the board, with most questions having a response rate above 85 percent, meeting Census Bureau standards for quality control.[73, 74]

The exceptions are Question 14 (with response rates between roughly 40 and 60 percent, depending on sub-question), and Questions 25 and 26 (with response rates around 37 and 39 percent). Question 14 is a relatively labor-intensive question requiring banks to be able to report outstanding loan balances by both loan balance and business size, and it is possible that banks overestimated their capability to do so while answering screener Questions 6 and 7. The low response rates for Questions 25 and 26, which are the last two questions of the survey, could reflect survey fatigue, or other unknown issues. Regardless, analysis of Questions 25 and 26 are not included in this report due to the low response rate.

Question response rates were generally stable across strata. Table A.3 gives the question response rate by both question and stratum. For Questions 1 through 9 and 15 through 26, which were asked of all strata, the average question response rate ranged from 91 to 95 percent across strata. For Questions 10 through 14 response rates declined from around 70 percent for Strata 5 and 6 to 42 percent for Stratum 8. Question 14 had a very low response rate among Strata 7 and 8. For this reason, the extrapolations based on Question 14 are not calculated for these banks (see Section 2 and Appendix B).

71 Note that not all banks were asked every question, as certain questions were triggered based on the bank's stratum or its responses to other questions. See the survey instrument (Appendix C) for the skip patterns.

72 Based on their answers to the screener questions, many banks were only asked a subset of Questions 7 through 14.

73 Note that Questions 2 and 14b have 100 percent question response rates by construction, the former because failing to answer Question 2 meant that the bank was considered to be a survey non-respondent, and the latter because the information was filled in automatically from the Call Report.

74 See Sub-requirement F1-6.2b of U.S. Census Bureau Statistical Quality Standards.

Figure A.1: Response Rates, by Survey Question

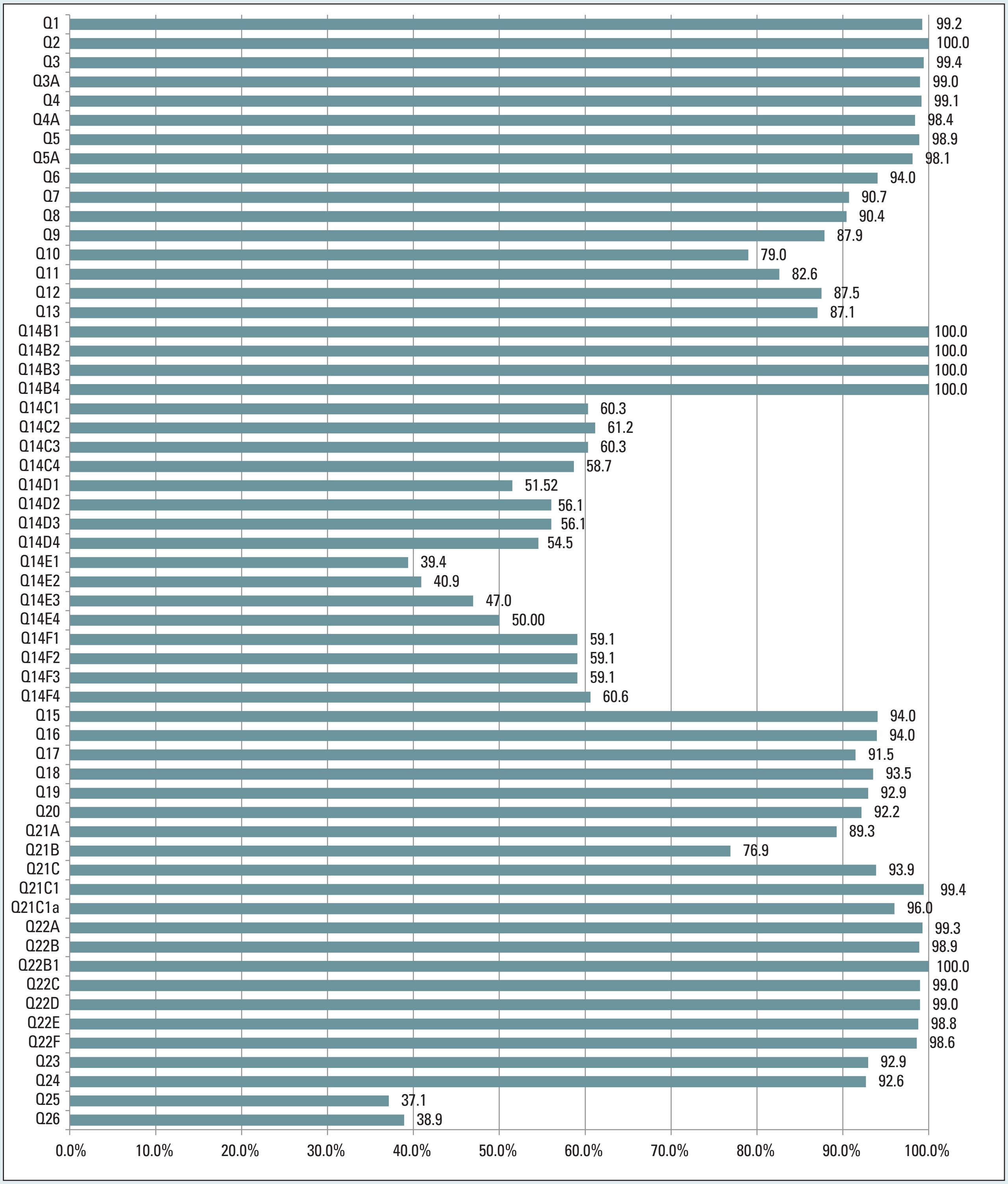

Table A.3: Response Rates, by Survey Question and Stratum

Survey Question	Stratum							
	1	2	3	4	5	6	7	8
Q1	98.2%	99.6%	99.1%	99.0%	100.0%	100.0%	100.0%	100.0%
Q2	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Q3	98.7%	99.2%	100.0%	99.0%	100.0%	100.0%	100.0%	100.0%
Q3A	94.9%	96.4%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Q4	98.2%	100.0%	98.6%	99.0%	100.0%	100.0%	97.1%	100.0%
Q4A	96.3%	95.2%	92.9%	100.0%	100.0%	100.0%	100.0%	100.0%
Q5	98.7%	99.2%	98.1%	99.0%	99.4%	100.0%	97.1%	100.0%
Q5A	100.0%	100.0%	93.1%	100.0%	100.0%	100.0%	100.0%	91.7%
Q6	93.4%	92.5%	93.0%	95.4%	95.6%	98.1%	N/A	N/A
Q7	89.4%	88.9%	91.6%	91.8%	92.8%	88.7%	97.1%	83.3%
Q8	87.7%	90.5%	91.2%	91.2%	91.8%	89.7%	96.4%	78.6%
Q9	84.5%	88.1%	88.1%	87.8%	90.4%	87.2%	96.4%	78.6%
Q10	N/A	N/A	N/A	N/A	78.7%	89.5%	76.5%	62.5%
Q11	N/A	N/A	N/A	N/A	100.0%	100.0%	66.7%	66.7%
Q12	N/A	N/A	N/A	N/A	90.2%	82.1%	89.7%	69.2%
Q13	N/A	N/A	N/A	N/A	89.5%	82.1%	86.2%	76.9%
Q14B1	N/A	N/A	N/A	N/A	100.0%	100.0%	100.0%	100.0%
Q14B2	N/A	N/A	N/A	N/A	100.0%	100.0%	100.0%	100.0%
Q14B3	N/A	N/A	N/A	N/A	100.0%	100.0%	100.0%	100.0%
Q14B4	N/A	N/A	N/A	N/A	100.0%	100.0%	100.0%	100.0%
Q14C1	N/A	N/A	N/A	N/A	64.5%	65.0%	55.6%	14.3%
Q14C2	N/A	N/A	N/A	N/A	65.8%	65.0%	55.6%	14.3%
Q14C3	N/A	N/A	N/A	N/A	64.5%	65.0%	55.6%	14.3%
Q14C4	N/A	N/A	N/A	N/A	61.8%	65.0%	55.6%	14.3%
Q14D1	N/A	N/A	N/A	N/A	57.1%	60.0%	37.5%	16.7%
Q14D2	N/A	N/A	N/A	N/A	64.3%	60.0%	37.5%	16.7%
Q14D3	N/A	N/A	N/A	N/A	64.3%	60.0%	37.5%	16.7%
Q14D4	N/A	N/A	N/A	N/A	61.9%	60.0%	37.5%	16.7%
Q14E1	N/A	N/A	N/A	N/A	42.9%	40.0%	37.5%	16.7%
Q14E2	N/A	N/A	N/A	N/A	45.2%	40.0%	37.5%	16.7%
Q14E3	N/A	N/A	N/A	N/A	52.4%	50.0%	37.5%	16.7%
Q14E4	N/A	N/A	N/A	N/A	57.1%	50.0%	37.5%	16.7%
Q14F1	N/A	N/A	N/A	N/A	66.7%	60.0%	37.5%	33.3%
Q14F2	N/A	N/A	N/A	N/A	66.7%	60.0%	37.5%	33.3%
Q14F3	N/A	N/A	N/A	N/A	66.7%	60.0%	37.5%	33.3%
Q14F4	N/A	N/A	N/A	N/A	69.0%	60.0%	37.5%	33.3%
Q15	91.6%	92.9%	96.3%	94.8%	93.9%	98.1%	91.2%	100.0%
Q16	91.6%	92.5%	96.3%	94.8%	93.9%	98.1%	91.2%	100.0%
Q17	90.3%	88.9%	93.9%	92.3%	91.2%	94.3%	91.2%	100.0%
Q18	92.1%	91.7%	95.8%	94.3%	93.4%	96.2%	91.2%	100.0%
Q19	91.2%	90.9%	95.3%	94.8%	92.3%	96.2%	91.2%	94.4%
Q20	89.9%	90.1%	94.9%	94.3%	91.2%	96.2%	88.2%	100.0%
Q21A	84.6%	86.6%	93.0%	92.3%	89.5%	92.5%	88.2%	100.0%

Table A.3: Response Rates, by Survey Question and Stratum (con't)

Survey Question	Stratum							
	1	2	3	4	5	6	7	8
Q21B	73.1%	71.1%	79.9%	81.4%	77.3%	90.6%	70.6%	88.9%
Q21C	92.5%	92.1%	96.3%	94.8%	93.4%	96.2%	91.2%	100.0%
Q21C1	100.0%	98.5%	100.0%	99.4%	100.0%	100.0%	100.0%	90.9%
Q21C1A	94.4%	91.8%	96.5%	95.8%	99.1%	97.3%	100.0%	100.0%
Q22A	99.0%	99.6%	99.0%	100.0%	98.8%	100.0%	100.0%	94.1%
Q22B	98.0%	99.1%	99.0%	100.0%	98.8%	100.0%	96.8%	94.1%
Q22B1	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Q22C	99.0%	99.1%	98.5%	99.5%	98.8%	100.0%	100.0%	94.1%
Q22D	99.0%	99.1%	98.5%	99.5%	98.8%	100.0%	100.0%	94.1%
Q22E	98.5%	99.1%	98.0%	99.5%	98.8%	100.0%	100.0%	94.1%
Q22F	98.0%	99.1%	98.0%	98.9%	98.8%	100.0%	100.0%	94.1%
Q23	91.2%	92.1%	95.3%	94.3%	91.2%	96.2%	91.2%	94.4%
Q24	90.7%	91.3%	94.9%	94.8%	91.2%	96.2%	91.2%	94.4%
Q25	34.8%	32.0%	34.1%	38.1%	35.9%	58.5%	55.9%	77.8%
Q26	38.3%	35.2%	34.6%	39.2%	37.0%	58.5%	55.9%	77.8%
Average question response rate	90.5%	90.7%	92.2%	92.8%	83.8%	84.5%	78.3%	72.2%
…excluding Survey Sections III and IV	90.5%	90.7%	92.2%	92.8%	92.1%	95.0%	93.0%	94.4%
…Survey Sections III and IV only	NA	NA	NA	NA	72.1%	69.7%	58.0%	41.6%

A.4 Analysis and Statistical Precision

In line with standard Census Bureau methodology for stratified random sampling, banks were assigned weights based on the inverse probability of selection in to the sample (with a slight correction due to the 39 banks excluded from the sample), which were then adjusted for nonresponse. All results in this report use these weights in order to produce accurate estimates that reflect the universe of banks in each stratum.

Estimated differences discussed in this report are significant at the 10 percent level or greater. This indicates that, if small and large banks were in fact equally likely to respond in the same way to a given question, the probability of obtaining estimates with an observed difference or a larger difference would be no more than 10 percent. In many cases, differences were actually statistically significant at much higher levels of precision than 10 percent.

APPENDIX B. Extrapolated Outstanding C&I Lending to Small Businesses

B.1 Extrapolated C&I Lending to Small Businesses Originated at Amounts Greater Than $1 Million, by Banks with Assets of $1 Billion to Less Than $10 Billion

In the survey, banks with $1 billion in assets or more were asked to report their outstanding C&I loan dollars broken down by loan size and business gross annual revenue (GAR). This was used to extrapolate the lower bound amount of C&I lending with origination values of over $1 million that went to small businesses. First, total outstanding C&I lending with origination amounts of greater than $1 million was taken from the Call Report. This was then adjusted by the ratio of outstanding C&I lending with origination amounts greater than $1 million that went to businesses with less than $1 million in gross annual revenue, to total outstanding C&I lending with origination amounts greater than $1 million, which was calculated from the answers collected by the survey. For banks that use GAR limits to define small businesses, almost all consider businesses with less than $1 million in gross annual revenue to be small businesses (see Section 2.1).

Due to sample size constraints, these calculations could only be done for banks with $1 billion to less than $10 billion in assets. A conservative estimate of the calculated ratio was used, specifically the lower bound of the 80 percent confidence interval estimated in the survey. The results are shown in Table B.1. Assuming that all businesses with less than $1 million in gross annual revenue are small businesses, these calculations suggest that, in Q4 2015, there was *at least* $19.1 billion in outstanding small business C&I loan dollars that was not accounted for in the Call Report proxy due to being over $1 million at the time of origination.

Table B.1: Extrapolated Lower Bound, C&I Lending to Small Businesses Originated at Amounts Greater Than $1 Million

(Banks with Assets of $1 Billion to Less Than $10 Billion Only)

Bank Asset Size	Outstanding C&I Lending with Origination Amounts Greater than $1M ($ Billions)	Ratio of Outstanding C&I Lending with Origination Amounts Greater than $1M That Went to Businesses with Less Than $1M GAR, to Total C&I Lending with Origination Amounts Greater Than $1M		Extrapolated Outstanding C&I Lending with Origination Amounts Greater Than $1M to Small Businesses ($ Billions)
		Mean Ratio	Lower Bound Ratio	
$1B to Less Than $10B	$132.5B	0.212	0.143	*Total: $19.1B*
Source:	Call Report	SBLS		

B.2 Extrapolated C&I Lending to Small Businesses Originated at Amounts Greater Than $1 Million, by Banks with Assets Below $1 Billion

For banks with assets below $1 billion, the extrapolated lower bound of C&I lending originated at amounts greater than $1 million that were made to small businesses is based on the share of these banks that described themselves as making "largely all" of their loans to small businesses. As shown in Figure 2.5, 86.4 percent of banks with under $250 million in assets and 76.5 percent of banks with $250 million to less than $1 billion in assets made largely all their loans to small businesses. Banks were then rank-ordered within the two asset size groups by Call Report C&I lending, and for each bank in the bottom 86.4 or 76.5 percent, respectively, Call Report small business proxy C&I lending was compared to total C&I lending. For all such banks where proxy C&I lending was less than half of total C&I lending, the difference between half of total C&I lending and proxy amount of lending was summed together, as a conservative extrapolation of the understatement for the two asset size groups of banks. In many cases, no extra C&I lending was counted as small business lending, since banks' proxy small business lending was already over 50 percent of their total C&I portfolio.

This highly conservative extrapolation assumes two very restrictive constraints (a) the banks which make largely all their loans to small businesses are the banks in each category which do the least C&I lending, and (b) banks which make largely all their loans to small businesses make only 50 percent of their loans to small businesses (unless they directly report a higher proportion in the small business C&I proxy). By this estimate, small business lending is underestimated by at least $60.2 million for banks with less than $250 million in assets and by at least $32.3 million for banks with between $250 million and $1 billion in assets.

It should be noted that much larger understatements are generated for these-sized banks if instead the simple method of counting their entire C&I portfolio as small business lending is used, as discussed in Section 2.3. Applying the simple method to the bottom 86 percent of banks with assets of less than $250 million and the bottom 76 percent of banks with assets of between $250 million and $1 billion, when ranked by their total C&I lending, instead yields for Q4 2015 an additional $16.9 billion in C&I lending to small businesses in loans with origination amounts above $1 million.

B.3 Extrapolated C&I Lending Collateralized by 1-4 Family Residences

The survey asked banks to report their total origination and renewal lending for C&I purposes as well as origination and renewal lending for C&I purposes that was primarily secured by 1-4 family residential properties (residentially-secured C&I). In order to extrapolate the lower bound total amount of *outstanding* residentially-secured C&I, the total amount of outstanding C&I lending in the Call Report was adjusted by the ratio of residentially-secured C&I originations to non-residentially-secured C&I originations calculated from the answers collected by the survey. This was done, first, because C&I lending collected by the Call Report by definition excludes any residentially-secured lending for C&I purposes (see the box in Section 2), and second, because the Call Report collects information on outstanding loan dollars, while the survey questions asked about origination dollars.[75]

A conservative estimate of the ratio of residentially-secured to non-residentially-secured C&I lending was used in the extrapolation, specifically the lower bound of the 80 percent confidence interval estimated in the survey. These calculations were done separately for banks with less than $250 million in assets, banks with $250 million to $1 billion in assets, banks with $1 to $10 billion in assets, and banks with over $10

[75] Dollar amounts at origination is the dollar amount extended by the loan at the time of origination, while outstanding loan balances, which is what is collected by the Call Report, instead reflects the remaining balance still owed on a loan. While these two measures capture different concepts, at a given moment in time for the industry the total dollar amounts in aggregate are similar as loan dollars that are paid off by borrowers are likely extended again as new lending.

billion in assets. The results are shown in Table B.2. Assuming that all residentially-secured C&I loans are made to small businesses, these calculations suggest that, in Q4 2015, there was *at least* $18.3 billion in outstanding small business C&I lending that was not accounted for in the Call Report proxy due to being residentially-secured.

Table B.2: Extrapolated Lower Bound, C&I Lending Collateralized by 1-4 Family Residences

Bank Asset Size	Outstanding C&I Lending ($ Billions)	Ratio of Residentially-secured C&I Origination to Non-residentially-secured C&I Originations		Extrapolated Outstanding Residentially-secured C&I Lending ($ Billions)
		Mean Ratio	Lower Bound Ratio	
Less than $250M	$31.5B	0.173	0.139	$4.4B
$250M to Less Than $1B	$77.3B	0.103	0.084	$6.5B
$1B to Less Than $10B	$188.5B	0.032	0.025	$4.8B
$10 Billion or More	$1,297B	0.010	0.002	$2.7B
Source:	Call Report	SBLS		*Total: $18.3B*

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APPENDIX C.
Small Business Lending Survey

The survey instrument begins on the following page.

[Screener]

Screener1. For calendar year 2015, do your bank's core data systems have the ability to retrieve the number and dollar volume of new loan *originations and renewals*, by purpose *(e.g. Commercial & Industrial (C&I), Commercial Real Estate (CRE), or Consumer)*, separately from collateral?[1]

a. Yes
b. No

Screener2. For calendar year 2015, do your bank's core data systems have the ability to retrieve the number and dollar volume of new loan *originations and renewals*, made to firms with $1 million or less in gross annual revenue?

a. Yes
b. No

Screener3. For calendar year 2015, do your bank's core data systems have the ability to retrieve the number and dollar volume of new loan *originations and renewals*, by firm gross annual revenue, for any sized firm?

a. Yes
b. No

Screener4. For calendar year 2015, do your bank's core data systems have the ability to retrieve the number and dollar volume of new loan *originations and renewals*, by commercial loan product type (e.g. lines of credit, term loans, etc.)?

a. Yes
b. No

Screener5. As of Call Report date ______, do your bank's core data systems have the ability to retrieve the number and dollar volume of *outstanding* loan balances, by purpose *(e.g., C&I, CRE, or Consumer)*, separately from collateral?[2]

a. Yes
b. No

Screener6. As of Call Report date ______, do your bank's core data systems have the ability to retrieve the number and dollar volume of *outstanding* loan balances, made to firms with $1 million or less in gross annual revenue?

a. Yes
b. No

Screener7. As of Call Report date ______, do your bank's core data systems have the ability to retrieve the number and dollar volume of *outstanding* loan balances, by firm gross annual revenue, for any sized firm?

a. Yes
b. No

1 For example, a C&I loan may be collateralized by a 1-4 family primary residence.

2 For example, a C&I loan may be collateralized by a 1-4 family primary residence.

[Programmer's Note: Throughout the Survey, please show Section headers on each screen with related questions]

I. Small Business Borrowers at Your Bank, in Calendar Year 2015

1. In your own words, please describe the general characteristics of the **small business borrowers** to which your bank lends, *regardless of regulatory definitions for small businesses.* (The purpose of this question is to compare how banks differ in what they consider to be small businesses.)

   ____

2. For calendar year 2015, do you consider **largely all** of the loans made by your bank for **Commercial and Industrial (C&I)** purposes to have been made to borrowers that you consider to be **small businesses**?
   a. Yes
   b. No

3. Generally speaking, does your bank internally consider a level of **gross annual revenue**, *regardless of regulatory definitions for small businesses*, above which a business would NOT be considered a **small business**?
   a. Yes
   b. No

   3A. [If Q3=Yes] What is this **annual revenue** benchmark above which a business is NOT considered a **small business**? $___,___,___.00

4. Generally speaking, does your bank consider an **aggregate loan exposure** above which the business being lent to would NOT be considered a **small business**?
   a. Yes
   b. No

   4A. [If Q4=Yes] What is this **aggregate loan exposure** above which a business is NOT considered a **small business**? $___,___,___.00

5. Does your bank offer any loan products **designed specifically for small businesses**? *Please do NOT include government-sponsored loan programs, such as Small Business Administration loans.*
   a. Yes
   b. No, our bank does not offer any products that differentiate between small businesses and all businesses

   5A. [If Q5=Yes] How many such **small business-specific loan products** does your bank offer?
   ____

[Programmer's Note: Ask Q6 only if Bank is in Strata 1-6]

6. At the end of calendar year 2015, what was your bank's "internal" (or "house") loan exposure limit, as set by your bank's Board of Directors? $___,___,___.00[3]

[3] Hover: If your bank uses different limits for different loan portfolios, please report the limit for C&I lending.

II. Total Loan Originations at Your Bank in Calendar Year 2015

7. In calendar year 2015, what were the total *originations and renewal* dollars committed to loans for **ALL purposes**, *including all consumer loans and all commercial loans to businesses of all sizes?* Please refer to the instruction box below, for detailed instructions on what lending to include.[4]

Loans for all purposes…

Include Lending Related to:

- Acquisition, Construction, and Development
- Agricultural and Farm
- Commercial and Industrial (C&I)
- Commercial Real Estate (CRE)
- Multi-family Real Estate
- 1-4 Family Residential Properties
- Consumer-activity, including (and not limited to) Auto and Credit Cards

Note:

- For renewals, include the whole amount of the renewal.
- For lines of credit, include the entire amount of the available line originated or renewed.
- Include non-portfolio loans that were originated for sale.

$___,___,___,___.00

[4] Hover: Please note that we are asking for total origination and renewal dollars for ALL PURPOSES, not only for small business lending purposes. Note also that the figures requested are NOT currently reported on the Call Report.

III. Commercial and Industrial Loan Originations at Your Bank, in Calendar Year 2015

[Programmer's Note: Ask Q8 only if Screener1=Yes]

8. In Question 7, your bank provided its total originations and renewal dollars committed to loans for ALL purposes. In calendar year 2015, what were the total *originations and renewal* dollars committed to loans for **Commercial and Industrial (C&I) purposes**, only? Please refer to the instruction box below, for detailed instructions on this Survey's definition for C&I lending.[5]

For the purposes of this Survey, loans for commercial and industrial purposes are loans to fund C&I activity, *regardless of the collateral used to secure the loan*. Specifically, …

Include:

- Unsecured C&I activity lending
- C&I activity lending, primarily secured by commercial real estate, including both owner-occupied and non-owner occupied CRE
- C&I activity lending, primarily secured by multi-family residential properties
- C&I activity lending, primarily secured by 1-4 family residential properties
- C&I activity lending, primarily secured by non-real estate assets (e.g. secured by inventory)

Exclude:

- Lending for the improvement, purchase, or refinancing of commercial real estate, including both owner-occupied and non-owner-occupied
- Lending for the improvement, purchase, or refinancing of multi-family real estate
- Lending for the purchase of 1-4 family residential properties by investors
- All Agricultural lending

$___,___,___,___.00

[Programmer's Note: Ask Q9 only if Screener1=Yes]

9. In calendar year 2015, what were the total *originations and renewal* dollars committed to loans for **Commercial and Industrial purposes**, that were *primarily secured by 1-4 family residential properties, only?* Please refer to the instruction box below, for examples of loans to include.[6]

Examples of loans to Include:

- A line of credit to a business for working capital purposes, primarily secured by the primary residence of the owner.
- A loan to an established small business borrower to open a new business, primarily secured by the primary residence of the owner.

$___,___,___,___.00

[5] Hover: Please note that the figures requested are NOT currently reported on the Call Report.

[6] Hover: Please note that the figures requested are NOT currently reported on the Call Report.

[Programmer's Note: Ask Q10 only if: Bank in Strata 5, 6, 7 or 8 AND Screener1=Yes and Screener2=Yes]

10. In calendar year 2015, what were the total *originations and renewal* dollars committed to loans for **Commercial and Industrial purposes**, *to businesses with gross annual revenues of $1 million or less, only?* Please refer to the instruction box below, for detailed instructions.[7]

For the purposes of this Survey, loans for commercial and industrial purposes are loans to fund C&I activity, *regardless of the collateral used to secure the loan.* Specifically, …

Include:

- Unsecured C&I activity lending
- C&I activity lending, primarily secured by commercial real estate, including both owner-occupied and non-owner occupied CRE
- C&I activity lending, primarily secured by multi-family residential properties
- C&I activity lending, primarily secured by 1-4 family residential properties
- C&I activity lending, primarily secured by non-real estate assets (e.g. secured by inventory)

Exclude:

- Lending for the improvement, purchase, or refinancing of commercial real estate, including both owner-occupied and non-owner-occupied
- Lending for the improvement, purchase, or refinancing of multi-family real estate
- Lending for the purchase of 1-4 family residential properties by investors
- All Agricultural lending

$___,___,___,___.00

[7] Hover: Please note that the figures requested are NOT currently reported on the Call Report.

[***Programmer's Note: Ask Q11 only if Bank in Strata 5, 6, 7 or 8 AND Screener1=Yes and Screener3=Yes and Q3=Yes AND Q3A answered with a value, different from $1 million]***

11. In calendar year 2015, what were the total *originations and renewal* dollars committed to loans for **Commercial and Industrial purposes**, *to businesses with gross annual revenues of [Insert value from Q3A] or less, only?* Please refer to the instruction box below, for detailed instructions.[8]

For the purposes of this Survey, loans for commercial and industrial purposes are loans to fund C&I activity, ***regardless of the collateral used to secure the loan.*** *Specifically, …*

Include:

- Unsecured C&I activity lending
- C&I activity lending, secured by commercial real estate, including both owner-occupied and non-owner occupied CRE
- C&I activity lending, secured by multi-family residential properties
- C&I activity lending, secured by 1-4 family residential properties
- C&I activity lending, secured by non-real estate assets (e.g. secured by inventory)

Exclude:

- Lending for the improvement, purchase, or refinancing of commercial real estate, including both owner-occupied and non-owner-occupied
- Lending for the improvement, purchase, or refinancing of multi-family real estate
- Lending for the purchase of 1-4 family residential properties by investors
- All Agricultural lending

$___,___,___,___.00

[8] Hover: Please note that the figures requested are NOT currently reported on the Call Report.

[Programmer's Note: Section IV is asked only if bank in Strata 5, 6, 7 or 8]

IV. Outstanding Loans Reported on the Call Report, for Commercial & Industrial Activity

A. Loans for Commercial & Industrial Activity, Secured by 1-4 Family Residential Properties

[Programmer's Note: Ask Q12 only if Screener5=Yes]

12. Looking at the *outstanding* balances of *[insert dollar amount]*[9] reported on your bank's *[insert date]* Call Report for closed-end loans of all liens primarily secured by **1-4 Family Residential Properties**, what was the total dollar amount that would have been classified as **Commercial and Industrial (C&I)** lending, *had it not been primarily secured by the primary residence of the owner*? Please refer to the instruction box below, for examples of loans to include.

Examples of loans to include:

- A line of credit to a business for working-capital purposes, secured by the primary residence of the owner.
- A loan to an established small business borrower to open a new business, secured by the primary residence of the owner.

$___,___,___,___.00

B. Loans for Commercial & Industrial Activity, Secured by Nonfarm Nonresidential Properties

[Programmer's Note: Ask Q13 only if Screener5=Yes]

13. Looking at the *outstanding* balances of *[insert dollar amount]*[10] reported on your bank's *[insert date]* Call Report for loans secured by owner-occupied and non-owner-occupied **Nonfarm Nonresidential Properties (i.e. Commercial Real Estate)**, what was the total dollar amount that would have been classified as **Commercial and Industrial** lending, *had it not been primarily secured by commercial real estate?* Please refer to the instruction box below, for examples of loans to include and details on lending to exclude.

Examples of loans to include:

- A loan to a business for working capital purposes, secured by the premises of the business.

Exclude:

- Lending for the purchase, refinancing, or improvement of commercial real estate, both owner-occupied and non-owner-occupied

$___,___,___,___.00

[9] Info Box: This number comes from Call Report Schedule RC-C Part 1 and is the sum of Lines 1c(2)(a) and 1c(2)(b).

[10] Info Box: This number comes from Call Report Schedule RC-C Part 1 and is the sum of Lines 1e(1) and 1e(2).

[Programmer's Note: Ask Q14 and include all columns only if Screener7=Yes. Ask Q14 and include only columns (a), (b), and (c) only if Screener 6=Yes and Screener7=No]

C. Loans for Commercial and Industrial Activity, by Firm Size

14. Looking at the *outstanding* loan balances for **Commercial and Industrial** loans, reported on your bank's *[insert date]* Call Report with origination amounts of various sizes, what was the total dollar amount of such loan balances to businesses with the following gross annual revenues?[11]

Call Report Loan Sizes (a)	Call Report Figures (b)	Dollar Amount of Loans Balances to Businesses with Annual Revenues of: $1 Mill or less (c)	Greater than $1 Mill to less than $10 Mill (d)	$10 Mill or more (e)	Total (f)
$100k or less	*[insert Call dollar amount]* [12]	$___________	$___________	$___________	*[Autocalculate: If Screener5=Yes, then sum Columns (c), (d), and (e)]*
Greater than $100k up to $250k	*[insert Call dollar amount]* [13]	$___________	$___________	$___________	*[Autocalculate If Screener5=Yes, then sum Columns (c), (d), and (e)]*
Greater than $250k up to $1 Mill	*[insert Call dollar amount]* [14]	$___________	$___________	$___________	*[Autocalculate: If Screener5=Yes, then sum Columns (c), (d), and (e)]*
Greater than $1 Mill (Note: Derived figure)	*[insert derived dollar amount]*[15]	$___________	$___________	$___________	*[Autocalculate If Screener5=Yes, then sum Columns (c), (d), and (e)] [Programmer's Note: Insert error flag if Column (b) does not match Column (f)]*

11 Hover: Please use your best estimate of revenue available, for example, revenue collected at the time of loan origination.

12 Info Box: This number is from Call Report Schedule RC-C Part 2, Line 4a, Column B.

13 Info Box: This number is from Call Report Schedule RC-C Part 2, Line 4b, Column B.

14 Info Box: This number is from Call Report Schedule RC-C Part 2, Line 4c, Column B.

15 Info Box: This number is derived from Call Report Schedule RC-C and is Schedule RC-C Part 1, Line 4a less the sum of Call Report Schedule RC-C Part 2, Line 4a, Column B, Call Report Schedule RC-C Part 2, Line 4b, Column B, and Call Report Schedule RC-C Part 2, Line 4c, Column B.

V. Small Business Commercial and Industrial Lending Competition, Practices, and Applications at Your Bank

D. Small Business Commercial and Industrial Loan Competition in Your Market

15. A bank's geographic market (or trade area) for **commercial and industrial** loans to **small businesses** is where the bank focuses its resources and outreach to generate such small business lending. What is your bank's trade area or geographic market for commercial and industrial purpose loans to small businesses? *Mark only one.*

    a. Only city/town where your bank's headquarters are located
    b. County or counties with branches
    c. County or counties with branches, and nearby (not necessarily contiguous) counties
    d. States in which branches are located
    e. States in which branches are located, and nearby states
    f. Metropolitan Statistical Areas (MSAs) with branches
    g. Metropolitan Statistical Areas (MSAs) with branches, and nearby (not necessarily contiguous) counties
    h. Metropolitan Statistical Areas (MSAs) with branches, and nearby (not necessarily contiguous) MSAs
    i. National
    j. Other ______________________
    k. Other ______________________
    l. Other ______________________

16. Currently, which institutions do you compete with most frequently for your bank's **commercial and industrial** lending to **small businesses**?

Competitor Institutions for C&I Lending to Small Business Borrowers (a)	Is this Institution a Competitor with Your Bank? *Mark all that apply.* (b)	Please Rank Your Bank's Top 3 Competitors (1=Top Competitor) (c)
a. Small banks (Less than $1 Billion in Assets)	☐	Options: 1 2 3 ***[Programmer's Note: Only allow options that were selected in Column (b)]***
b. Mid-sized local banks with a physical presence in your market ($1 Billion to less than $10 Billion in Assets)	☐	
c. Mid-sized local banks with no physical presence in your market ($1 Billion to less than $10 Billion in Assets)	☐	
d. Regional (multi-state) banks with a physical presence in your market ($10 to less than $50 Billion in Assets)	☐	
e. Regional (multi-state) banks with no physical presence in your market ($10 to less than $50 Billion in Assets)	☐	
f. Large banks with a physical presence in your market ($50+ Billion in Assets)	☐	
g. Large banks with no physical presence in your market ($50+ Billion in Assets)	☐	
h. Credit unions	☐	
i. Non-bank local lenders	☐	
j. Non-bank online lenders, including marketplace lenders (e.g., OnDeck, Lending Club, Kabbage, etc.)	☐	
k. Crowd-funding sites (e.g., Kickstarter, Indiegogo, CircleUp, CrowdFunder, etc.)	☐	
l. Credit card issuers	☐	
m. Other _____________	☐	
n. Other _____________	☐	
o. Other _____________	☐	

17. In Question 16, your bank ranked its top three competitors. In relation to your bank, which of these forms of competition do you consider to be the **competitive advantages** of *[Most frequent competitor, Ranked #1 in answer to Q16, Column (c)]*, the institution your bank ranked as its number 1 competitor, in competing against your bank for **commercial and industrial** lending to **small businesses** today?

Competitive Advantages for C&I Lending to Small Business Borrowers (a)	Do *[Most frequent competitor #1]* Have this Competitive Advantage? *Mark all that apply.* (b)	What are the Top 3 Competitive Advantages of *[Most frequent competitor #1]* ? (c)
Convenience		
a. Availability of credit products	☐	☐
b. Availability of other services (e.g., deposit capabilities, remote products)	☐	☐
c. Convenient location for borrower	☐	☐
d. Number of locations	☐	***[Programmer's Note: Only allow options that were selected in Column (b)]***
Customer Service		
e. Established relationship with business banker/loan officer	☐	
f. Personal attention given by lender	☐	
g. Quality of staff (including experience and knowledge)	☐	
Pricing/Structure		
h. Fees	☐	
i. Interest rates	☐	
j. Term	☐	
k. Flexibility in pricing or loan structure	☐	
Speed of service		
l. Closing/Funding speed	☐	
m. Decision speed	☐	
Technology		
n. Mobile banking	☐	
o. Remote deposit capture	☐	
Underwriting criteria		
p. Collateral requirements	☐	
q. Debt Service Coverage	☐	
r. Loan-to-Value	☐	
Other		
s. Other _____________	☐	
t. Other _____________	☐	
u. Other _____________	☐	

18. In relation to your bank's competitors, which of these forms of competition do you consider to be **your bank's competitive advantages** today, in generating your bank's **commercial and industrial** lending to **small businesses**?

Competitive Advantages for C&I Lending to Small Business Borrowers (a)	Does *Your Bank* Have this Competitive Advantage? *Mark all that apply.* (b)	What are *Your Bank's* Top 3 Competitive Advantages? (c)
Convenience		
a. Availability of credit products	☐	☐
b. Availability of other services (e.g., deposit capabilities, remote products)	☐	☐
c. Convenient location for borrower	☐	☐
d. Number of locations	☐	***[Programmer's Note: Only allow options that were selected in Column (b)]***
Customer Service		
e. Established relationship with business banker/loan officer	☐	
f. Personal attention given by lender	☐	
g. Quality of staff (including experience and knowledge)	☐	
Pricing/Structure		
h. Fees	☐	
i. Interest rates	☐	
j. Term	☐	
k. Flexibility in pricing or loan structure	☐	
Speed of service		
l. Closing/Funding speed	☐	
m. Decision speed	☐	
Technology		
n. Mobile banking	☐	
o. Remote deposit capture	☐	
Underwriting criteria		
p. Collateral requirements	☐	
q. Debt Service Coverage	☐	
r. Loan-to-Value	☐	
Other		
s. Other _____________	☐	
t. Other _____________	☐	
u. Other _____________	☐	

E. Commercial & Industrial Loan Products Offered to Small Businesses, by Your Bank

19. In calendar year 2015, did your bank offer any of the following **commercial and industrial** loan product types to potential borrowers that your bank considers to be **small businesses**?

Commercial & Industrial Loan Product Types Offered to Small Businesses (a)	Did Your Bank Offer this C&I Loan Product? *Mark all that apply.* (b)	Please Rank Your Bank's Top 3 Loan Product Types, By Dollar Volume of Originations to Small Businesses, in 2015 (1=Most) (c)
a. Credit cards (as principal sponsor)[16]	☐	Options:
b. Letters of credit	☐	1
c. Lines of credit (LOC)	☐	
d. Term loans – balloon	☐	2
e. Term loans – fully amortizing	☐	3
f. Other _______________	☐	***[Programmer's Note: Only allow options that were selected in Column (b)]***
g. Other _______________	☐	
h. Other _______________	☐	

20. Does your bank use the same underwriting criteria for example, owner's personal credit score, debt-service coverage, or loan-to-value ratio) across **commercial and industrial** loan products offered to **small businesses**, even if the thresholds for approval are different?[17]
    a. Yes
    b. No

21. Please tell us more about any **commercial and industrial** lending that your bank may extend to **small business startups**.[18]

    21A. Below what age would a small business be considered a **startup** by your bank? _____

    21B. In your own words, how does your bank define startups, other than by age? _____

    21C. Does your bank make **commercial and industrial** loans to **startups**?
    a. Yes
    b. No

16 Hover: The term 'principal sponsor' means that your bank is the sponsoring bank that directly handles card transactions on behalf of merchants.

17 Hover: By "threshold" we mean the acceptable level for an underwriting criterion, for example, "a maximum 75 percent loan-to-value ratio." In this example, a differing threshold could be a "maximum 80 percent loan-to-value ratio" for a different C&I loan product. Another example could be requiring a minimum personal credit score of 650 for small business term loans but a minimum of 700 for a small business credit card.

18 Hover: Please note that by 'startups' we mean new operations, not new owners of existing businesses.

21C1. *[If Q21C=Yes]* Does your bank underwrite **startups** differently from established small businesses for **commercial and industrial** lending?

a. Yes

b. No

21C1a. *[If Q21C1=Yes]* What additional underwriting criteria and/or processes does your bank apply in extending **commercial and industrial** credit to **startups**?___________
____

22. In Question 19, your bank ranked its top three loan products to small businesses. Please tell us more about your bank's *[Commercial loan product type, Ranked #1 in Q19 Column (c)]*, the loan product your bank ranked as its number 1 loan product to small businesses, for **commercial and industrial** purposes.

22A. Thinking about *[Commercial loan product #1]* for **commercial and industrial** purposes, how do you expect its volume of loans to **small businesses** to change in the next calendar year? *Mark only one.*

a. Increase

b. Stay the same

c. Decrease

22B. Is there a minimum allowable loan amount for *[Commercial loan product #1]* for **commercial and industrial** purposes, offered to **small businesses**?

a. Yes

b. No

22B1. *[If Q22B=Yes]* What is the minimum loan amount allowed for *[Commercial loan product #1]* for **commercial and industrial** purposes, offered to **small businesses**?

$____,____,____.00

22C. For what purposes are proceeds from *[Commercial loan product #1]* for **commercial and industrial** lending typically used by **small businesses**? *Mark all that apply*

a. Accounts receivable

b. Equipment, fixed assets, or leasehold improvements

c. Inventory

d. Working capital

e. Other _____________

f. Other _____________

g. Other _____________

22D. What collateral is commonly accepted used by **small businesses** for *[Commercial loan product #1]* for **commercial and industrial** purposes? *Mark all that apply.*

a. No security/collateral required

b. Secured by accounts receivable and/or inventory

c. Secured by business assets and/or equipment

d. Secured by cash or other liquid assets of business

e. Secured by cash or other liquid assets of owner of guarantor

f. Secured by commercial real estate (e.g., building, land)

g. Secured by personal assets, *other than* cash/liquid assets or personal real estate (e.g., marketable securities, vehicles)

h. Secured by personal real estate
i. Secured by other collateral _____________
j. Secured by other collateral _____________
k. Secured by other collateral _____________

22E. How often does your bank use any of the following underwriting criteria to evaluate potential **small business** borrowers for *[Commercial loan product #1]* for **commercial and industrial** purposes?

Underwriting Criteria	How Often Does Your Bank Use This Practice?
a. Loan debt service coverage b. Business' global debt service coverage c. Personal guarantee d. Other guarantee offered e. Business' debt-to-worth f. Owners' debt-to-worth g. Business' cash/liquidity position h. Owners' overall financial strength/net worth i. Business' credit score j. Owners' or guarantors' personal credit score(s) k. Loan-to-value ratio l. Sell cycle for accounts receivable or inventory m. Business' time in operation n. Owners' experience in industry o. Other ______________ p. Other ______________ q. Other ______________	<u>Options:</u> Always Almost always Sometimes Almost never Never

22F. What are typical reasons why exceptions from loan policy are allowed for potential **small business** borrowers for *[Commercial loan product #1]* for **commercial and industrial** purposes?
Mark all that apply.

a. Existing competing offers
b. Existing good customer deposit relationship
c. Existing good customer loan relationship
d. Existing good customer loan and deposit relationship, considered together
e. Positive business prospects for borrower
f. Potential for other new banking relationships with customer
g. Strong mitigating factors
h. Other ________________
i. Other ________________
j. Other ________________
k. No exceptions are allowed

F. Small Business Commercial and Industrial Loan Applications, Activity, and Access, at Your Bank

23. Where can a potential borrower that your bank considers to be a **small business** apply for a **commercial and industrial (C&I)** loan from your bank? *Mark all that apply.*

  a. Any branch
  b. Branches with loan offices
  c. Brokers (in-person or by telephone)
  d. Follow-up call from bank, after customer inquiry
  e. Online using bank's own website
  f. Online using third-party website
  g. On-site visits to businesses by bank staff
  h. Main headquarters office
  i. Other _____________
  j. Other _____________
  k. Other _____________

[Programmer's Note: Ask Q23A only if online options 'e' or 'f' selected in Q23]

23A. Does your bank accept **online** applications for **commercial and industrial** loans from all **small business** applicants? *Mark only one.*

  a. Yes, from all applicants
  b. No, from some applicants only
  c. No loan applications from small businesses are accepted online

24. What practices does your bank currently use to generate new and maintain existing **small business commercial and industrial** loan relationships?

Practices to Generate Small Business C&I Lending Relationships (a)	Does Your Bank Engage in this Practice? *Mark all that apply.* (b)	What are the Top 3 Practices Used by Your Bank? (c)
Convenience		
a. Ability to talk to someone	☐	☐
b. Accepting walk-ins	☐	☐
c. Branch network	☐	☐
d. Hours open	☐	***[Programmer's Note: Only allow options that were selected in Column (b)]***
e. Non-bank locations of loan production offices	☐	
f. Online applications	☐	
External sources		
g. Brokers	☐	
h. Indirect lending	☐	
i. Lead generators	☐	
j. Referrals from customers, or "word of mouth"	☐	
k. Referrals from "centers of influence" (e.g. local attorneys, CPAs, and Chambers of Commerce)	☐	
Outreach/Strategy		
l. Active marketing to customers from past or current banking relationships	☐	
m. Active marketing to customers *not* from past or current banking relationships	☐	
n. Community involvement and service (e.g. board participation, networking events, and other sponsorships)	☐	
o. Intentional personal contact from staff	☐	
p. Knowledgeable staff (e.g. business development specialists)	☐	
Provision of Business Services		
q. Card payment processing	☐	
r. Check cashing services	☐	
s. Payroll services or payroll cards	☐	
t. Transfer services	☐	
Other		
u. Other _____________	☐	
v. Other _____________	☐	
w. Other _____________	☐	

25. In calendar year 2015, in consultation with your bank's loan officers, in situations where an inquiry from a **small business** did not lead to a **commercial and industrial** loan (for any reason), did your bank do any of the following? Mark all that apply.
    a. Offer business financial counseling, provided directly by bank staff
    b. Place in contact with or share literature from third-party technical assistance providers
    c. Refer to another commercial loan product offered by the bank
    d. Refer to consumer loan products offered by the bank (e.g. a HELOC or personal credit card)
    e. Refer to an SBA or USDA-guaranteed product
    f. Suggest that customer find an investor/partner, for a stronger equity/capital position
    g. Suggest outside financial counseling (e.g. provided by professionals or by government authorities)
    h. Other _____________
    i. Other _____________
    j. Other _____________

26. In calendar year 2015, what were the challenges that your bank faced in providing **commercial and industrial** loan credit to **small businesses**?

Challenges to Providing C&I Loan Credit to Small Businesses (a)	Did *Your Bank* Face this Challenge? *Mark all that apply.* (b)	What were the Top 3 Challenges Faced by *Your Bank?* (c)
a. Borrowers' failure to meet underwriting criteria	☐	☐
b. Borrowers' lack of experience in industry	☐	☐
c. Caps on guaranteed programs	☐	☐
d. Competition	☐	***[Programmer's Note: Only allow options that were selected in Column (b)]***
e. Lack of demand	☐	
f. Insufficient funding sources for bank	☐	
g. Staffing	☐	
h. Secondary market conditions	☐	
i. Other _____________	☐	
j. Other _____________	☐	
k. Other _____________	☐	

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