Ambidextrous Community Banks Lending More

regulatory lending business customers

Summary: The most recent FDIC survey found that small business lending by banks has been significantly underestimated. We provide the interesting findings.

As a reader of this publication, you know we enjoy pointing out interesting statistics to help keep you engaged. With that in mind, take a look around your office today. As you do, consider that about 10% of your coworkers are left handed, while a mere 1% are officially ambidextrous (no dominant hand whatsoever). Enjoy the day no matter which hand is dominant for you.

Speaking of dominance, the ICBA reports that community banks make almost 50% of small business loans, so it remains big business. Just how big wasn't really known, until recently. A new FDIC survey found that small business lending by banks has been significantly underestimated, particularly when it comes to banks with assets under $10B.

This survey looked at past estimates of small business commercial and industrial (C&I) bank lending and updated the numbers based on the new survey of banks. The estimate of small business lending in 2015 was at least $37B too low, a 12% error, while community bank lending was understated by 29%.

The underestimate of small business lending at community banks is the result of the way loan data has been captured by the FDIC. After examining data more closely, the FDIC determined that loan definitions and banking practices ended up overlooking loans, especially made by smaller banks to small businesses.

For starters, the FDIC defined a small business C&I loan as being under $1mm. That loan limit was adopted in the early 1990s and never adjusted for inflation. If it had been, the same loan limit would have been $1.5mm by 2015. As a result, loans above $1mm in later years, if adjusted for inflation, should have been included in the original definition.

Another factor that may have caused underreporting is that small business loans that are collateralized by the owner's residence are not counted as small business loans, but rather as home mortgages. Here again, the use of residences as collateral for small business loans is more prevalent at community banks.

Also significant is the fact that community banks use a variety of different criteria to help define who their small business customers are, including ownership structure (the mom-and-pop business) and local footprint. Larger banks tend to stick closer to FDIC criteria for defining small businesses, like loan size and borrower size. This makes it more likely the loans will be captured by the FDIC as small business loans.

In fact, the smaller a bank is, the more concentrated its loan portfolio is to small businesses. The survey found that 90% of banks with <$250mm in assets made C&I loans almost solely to small businesses. Meanwhile, about 75% of banks with assets of $250mm to $1B said the same.

That concentration has the FDIC reconsidering how it captures statistical data on small business loans. One suggested solution - declare all C&I loans at smaller banks to be small business loans.

This readjustment of data gives a nice boost for community banks, at a time when your small business lending faces increasing competition, as we covered most recently in the article, "Lyfting SMB Lending". The new FDIC survey reaffirmed that community banks are truly ambidextrous and operate squarely in the middle of the small business world.

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