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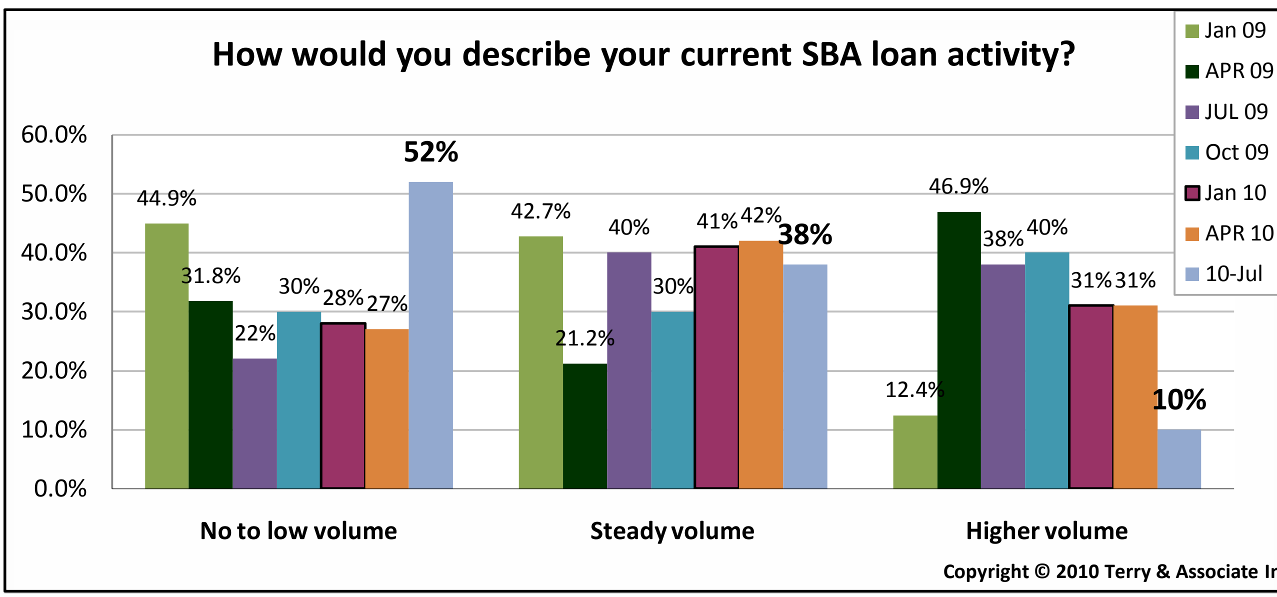
Small Business Lender Sentiment Survey
On Lending and Employment
Third Quarter 2010

"Dear Mr. Bernanke,
Thank you for your robust support of Small Business that generates new employment. But, why now and not last February '09 when you gave the SBA less than 1% of the entire Stimulus Fund?"

In this issue:

- **Lenders show dramatic impact of stimulus funds "cut-off"**
- **What small business lending looks like without the stimulus funds**
- **504 loans making a rebound with new secondary market improvements**
- **Most new SBA lender hires on hold or no go without renewed stimulus**



The second quarter SBA loan growth was right on track until stimulus funds dried up in late May. Then as seen above, the industry experienced its greatest negative change since October 2008. Current lending activity shifted dramatically. No-to-low volume lenders jumped to over half of all respondents. Higher volume lenders dropped to just 10% of all respondents. The SBA reported that lending was off a whopping 73% from May to June. And that has not changed in July.

This is not news to the Fed's. They have been pushing Congress for SBA stimulus extensions since last November when the original provisions ran out. That is greatly appreciated by the industry. However, the question must be asked, *"Mr. Bernanke, if you feel strongly about Small Business being the engine to lead the recovery and provide significant new job growth, why did you give Small Business less than 1% of the stimulus money in February of 2009?"*

If credit to Small Business had been properly address in the original stimulus funds, would there have been a need for the Fed's to hold 40 regional meetings around the country to try to encourage small business lending?

The real issue here is not loan volume. Reports show that there are over 600 loans that have been approved by lenders but, are in "the que" at SBA. Both customers and lenders are waiting to see if the stimulus provisions are renewed by Congress, which will save customers thousands of dollars and give lenders much higher loan guarantees.

The real question is how many of these approved loans would be approved or even wanted by the customer without these stimulus provisions. Let's take a look at what small business department managers from all over the country have to say.

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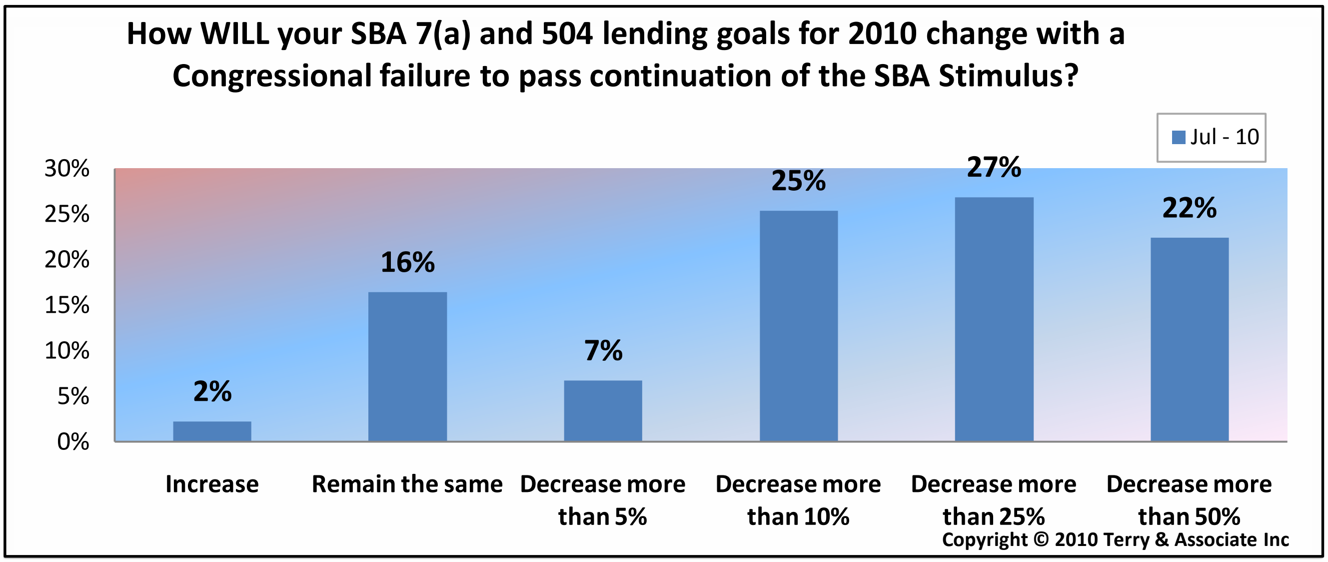
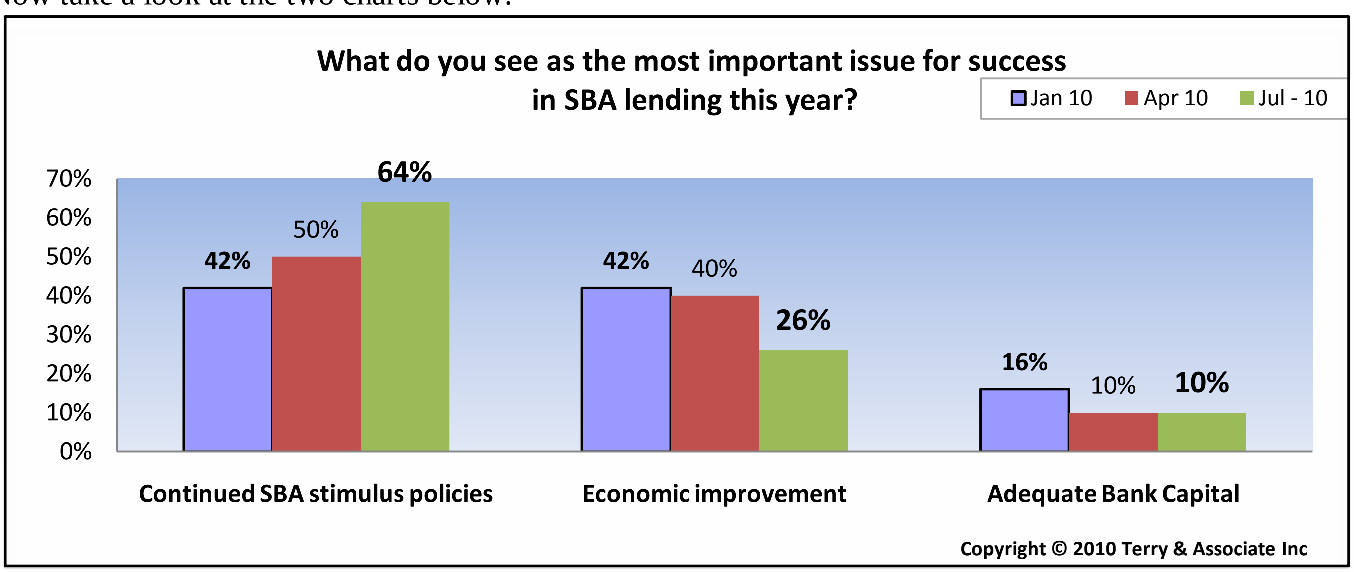
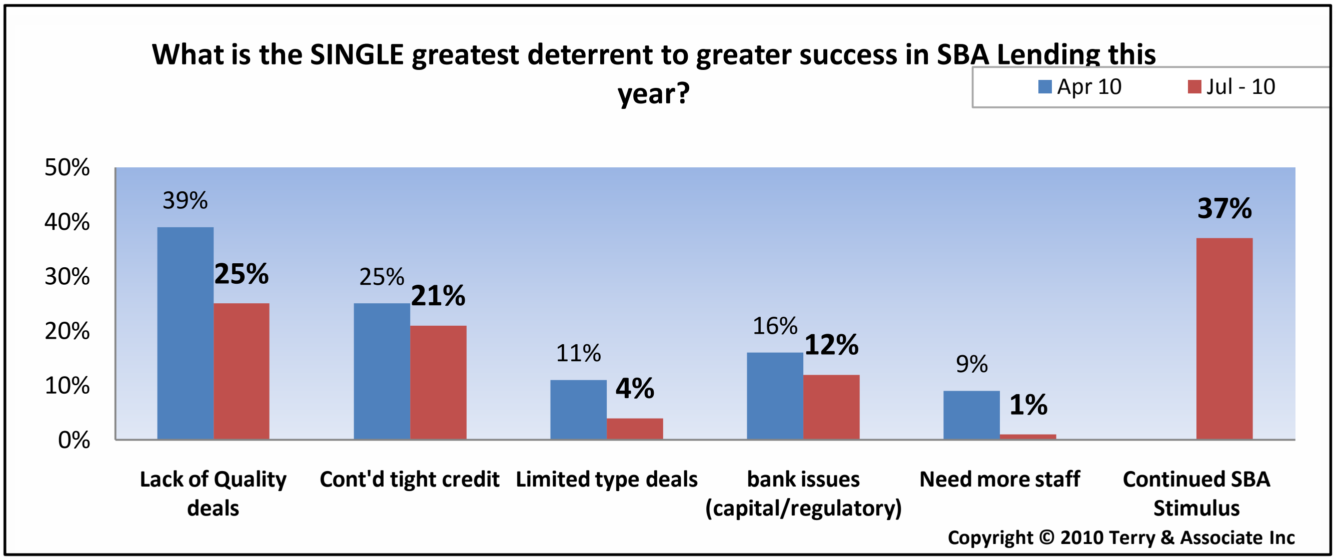


Take a good look at the chart above. This is an indication of the small business credit crunch that is inevitable once SBA stimulus funds are gone. The good news is that there are a few banks that will not let the change in Federal stimulus funds affect their lending plans. The bad news is that lending to small businesses will be dramatically impacted if 82% of active lenders curtail their lending plans.

Now take a look at the two charts below.





Continued SBA stimulus provisions remain the most significant issue in SBA lending. **In an economic environment like we are experiencing, it is amazing to see a Federal plan that actually works.** These provisions have brought about a historical record recovery in small business lending, bringing the industry back to pre-recession rates. Even the secondary market for SBA loans has seen a dramatic recovery with 10 year + 2 loans selling for an average of 107.9 and 25 year +2 selling at an average of 109.7.

<u>Given the fact that both sides of the Hill want to see these provisions extended, it is shameful that these small business credit initiatives have not been stripped out of other bills and passed as a stand-alone bill.</u> **If you have not called your Congressman or Senator, what are you waiting for?** As a stand-alone legislative initiative, passage could take place on both sides of the Hill by the end of July. As it stands now, the best chance for passage will not be until just before the August recess. And there is real concern that it may not happen then.

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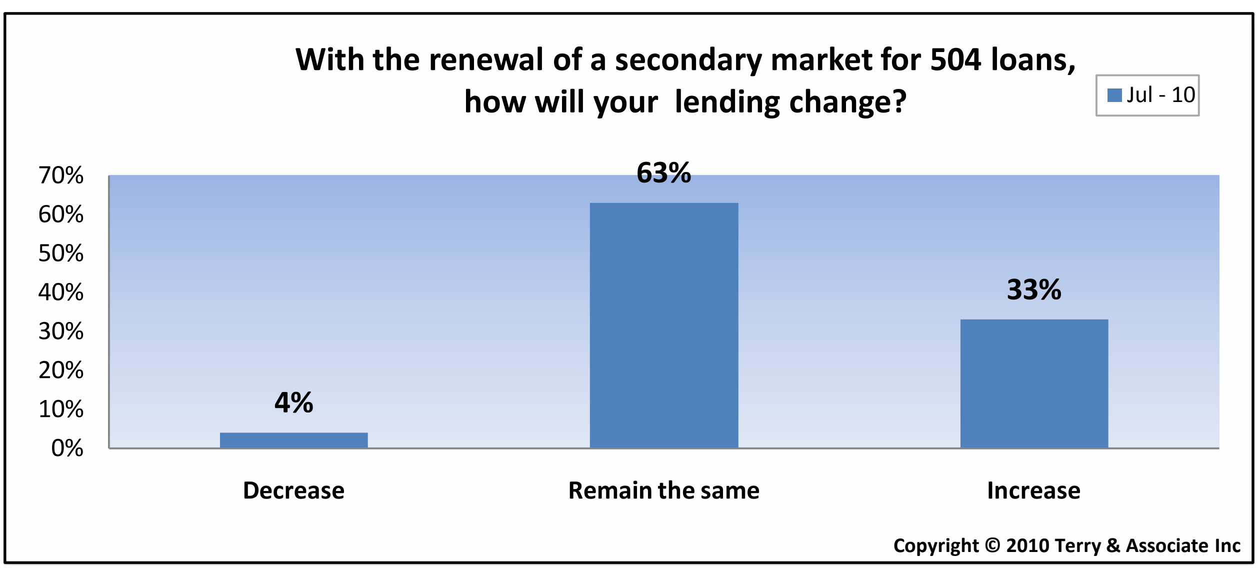
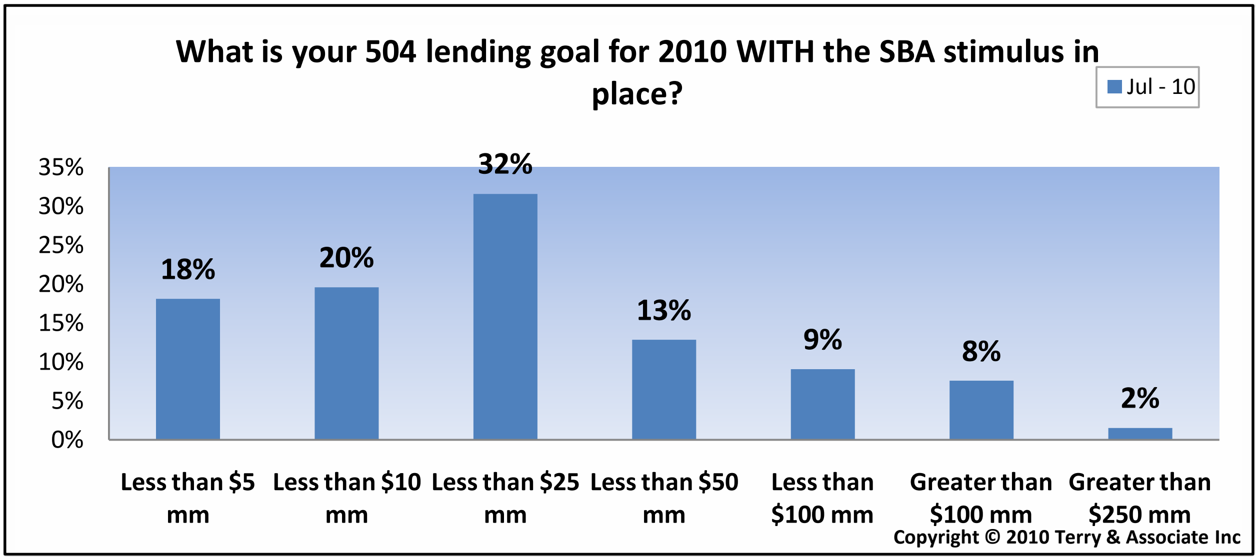
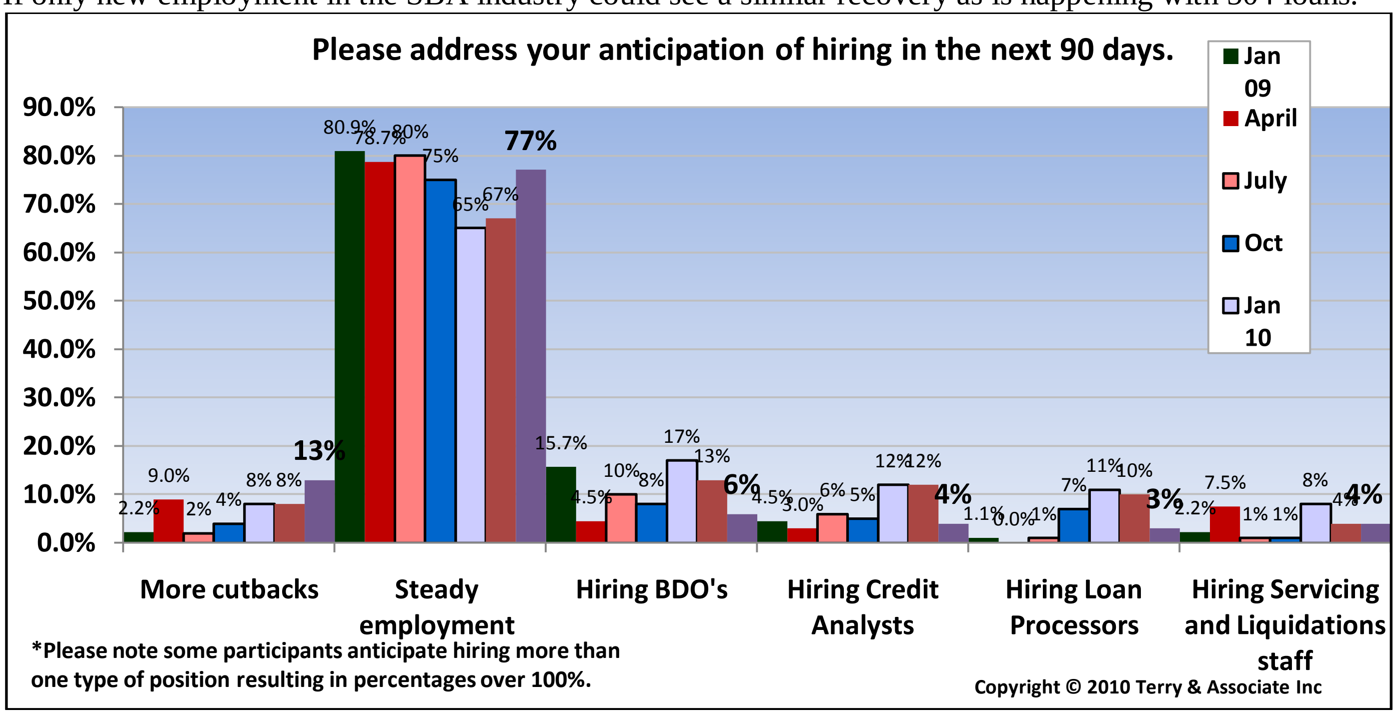
Wait, could there still be more good news? There are indications of a resurgent secondary market for 504 loans. Talk with any CDC and discover that there is not a lack of customers for this loan product. But, it takes 'two to tango" with a 504 loan. The CDC may want to make the loan, but finding a lender to participate has been a real challenge. Clearly, bank capital continues to be a real concern. With a secondary market, lenders can sell their participation, recapture the dollars and lend again. The third quarter of this year looks to be the best 504 loan quarter since the recession started.





As the chart shows, 504 lending should see a significant recovery. Even if 70% of respondents plan 504 loan growth of less than $25mm, it is still a strong indicator of good prospects for more credit to small business that was not there before.

If only new employment in the SBA industry could see a similar recovery as is happening with 504 loans.



The “more cutbacks” category is higher than in any previous survey. However, the number of employees involved in the cutbacks is substantially smaller than when the recession began. Yet, the number of new hires is much smaller as well. The year started with a lot of optimism regarding a recovery, especially in small business lending. And there was a small but significant improvement in hiring during the first 6 months of this year. Most new hires that are planned now appear to be on hold until Capital Hill reaches a decision on further assistance to small business credit. The good news is that banks and credit unions continue to start up new SBA loan programs. These small shops may only hire one or two people at first. But if they hire the right people, there is a good chance it will lead to further new employment in coming months.

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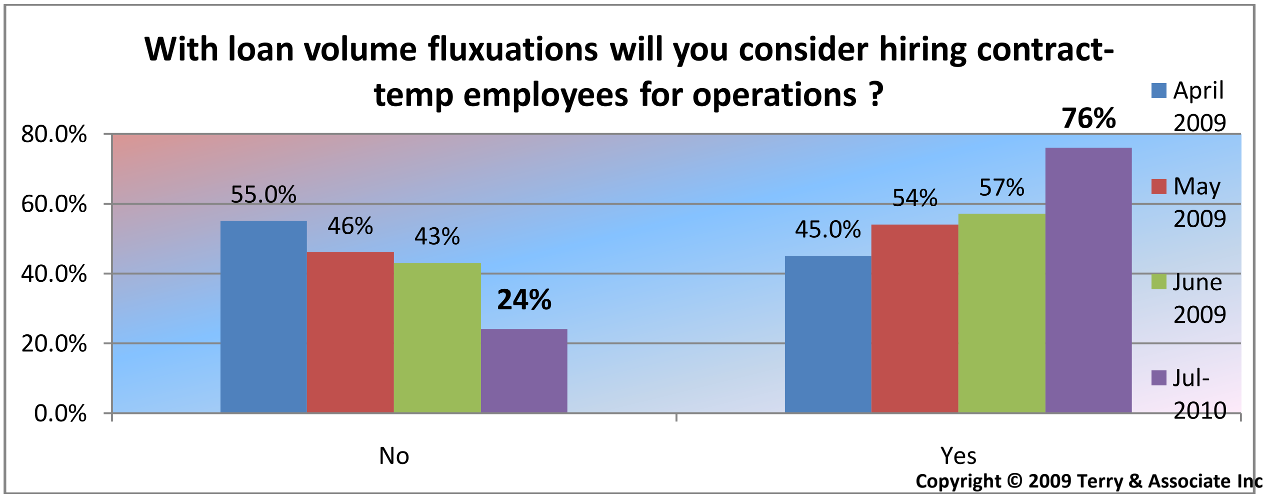
In the meantime, it appears that the utilization of temporary / contract workers is growing as a solution to the fluxuations in loan volume. Apparently, in comments from the survey, temp workers have been a very cost effective alternative, especially with those lending programs dealing with budgetary constraints and hiring freezes.



Summary

- The continued SBA stimulus policies are a mandate by lenders if there is to be a vibrant growth in available credit to small business. Capital Hill will eventually figure out how to pass a continuation of the stimulus program. The question is WHEN? The concern is a major drop off in available credit at a critical time in the overall economic recovery.

- Reports show a slight improvement in credit quality. However, it also demonstrates that less credit exists. Banks are cleaning up under-performing loans, while at the same time tightening credit standards. In fact, credit standards are tighter than ever reported. The reality of this is evidenced by the 73% drop off in small business lending in just one month. Without the continuation of the SBA stimulus, expect available credit to adjust downward.

- The 504 loan program has new reason for optimism with the beginnings of a renewed secondary market. Expect this program to see gains through this quarter and possibly through the remainder of this year.

- SBA industry employment has taken a turn for the worse after seeing some significant gains in the first half of this year. As the SBA stimulus policies go, so goes new employment. It is hopeful that a quick restart to hiring could occur if Capital Hill comes through for the industry soon.

- While temporary staffing is not new to the banking community, it was not an acceptable alternative for SBA lending programs until this year. Department managers are apparently utilizing temp workers to offset demands during the ups and downs of loan volume. With great uncertainties about the timing of a lasting economic recovery, expect the temp workers to become a mainstay in the industry.

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About Terry & Associates, Inc.

Since 1992 Terry & Associates, Inc. has been providing executive search and consulting services to banks and non-banks who provide Small Business Administration (SBA) government guaranteed loans. The company has also set up new SBA lending departments for banks interested in the many incentives and market advantages that SBA lending can provide. Tim is also a frequent speaker on the SBA industry and has testified before Congress on behalf of small business lending.

Terry & Associates, Inc. is publishing a quarterly survey report which offers a national perspective on the status of lending to the small business sector. For more information, contact Tim Terry at 940.381.6200 or tim@sbasearch.com.