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Small-Business Lending Jumps, But Credit Struggles Linger

By **EMILY MALTBY**

Small businesses received more government-backed loans last year than ever before. Even so, access to capital remains a major hurdle for a significant number of U.S. entrepreneurs, new data show.

A record \$19.6 billion were issued through the Small Business Administration's flagship program in fiscal 2011, the government agency reported Wednesday. Those funds, however, were distributed to 53,706 businesses, roughly the same number as in 2010.



Marsha Margolis

Todd and Pam Turkin in their firm's kitchen in Livonia Mich.

SBA loans, which are issued through banks, are intended to help small firms grow and hire. A portion of each loan is guaranteed by the federal agency to cover a bank if a borrower defaults, thereby reducing the bank's risk. In turn, the agency reasons that the program encourages banks lend to more money to more small businesses.

Last October, the SBA expanded the pool of eligible small businesses by raising the loan amounts it would back to a maximum of \$5 million from \$2 million. But that larger pool made smaller loans less attractive to banks. As larger and stronger businesses applied for the higher loan amounts, some smaller businesses were left behind.

It takes as much work for a bank to underwrite small loan as a large loan, says Bob Coleman, an SBA-loan analyst in La Canada, Calif., and owner of Coleman Publishing, a trade publisher for SBA lenders.

"The amount of man hours they need to put into the analysis and documentation – they are losing money on that process," he says. "Banks are chartered to make money and if I can only do four deals a month, I'd rather work on deals that can make a larger profit."

The result: Loans of less than \$150,000 were issued to 29,682 businesses in 2011, down from 34,238 last year, according to agency documents.

Loans of less than \$150,000 are often critical for small, growing businesses that can use such financing to hire, buy equipment and make other capital improvements necessary to expand.

SBA Administrator Karen Mills said last week that she was pleased with the 2011 loan figures. The dollar volume is a 58% increase from last year and a 113% increase from 2009 – the worst year of the credit crunch.

"We've had an extremely successful year... and we are back to pre-recession lending levels," she said. "But we still have some gaps. We're not back in [the terms of] small loans and loans to underserved markets."

Ms. Mills said the primary hindrance for banks is the work and costs associated with making smaller loans and that the agency is reducing and streamlining paperwork.

In February, the SBA also rolled out two initiatives, the Community Advantage and the Small Loan Advantage programs, to address the gap. Both offer fast approval times, minimal application paperwork and government guarantees of up to 85% for the smallest loans. The Community Advantage program is open to mission-based lenders such as Community Development Financial Institutions, Certified Development Companies and nonprofit microlenders, which tend to target lower-income communities.

Still, getting loans to the smaller businesses remains a challenge.

SBA-backed loans have traditionally made up a fraction of overall small-business loans. But they often indicate how small businesses are faring in the broader capital markets.

Pam and Todd Turkin, co-founders of the Just Baked Shop LLC, have struggled for years to secure a bank loan in order to open new locations and buy equipment.

The couple's first cupcake bakery in Livonia, Mich., took off in late 2008 and they were immediately strapped for financing. In 2009, just as they were poised to open their second store, they were denied a \$20,000 credit line from their primary bank. So they self-financed and borrowed funds from family. In mid 2010, as the bakery hit \$1 million in sales and the Turkins were opening their fourth store, they tried another bank for a \$60,000 credit line. Again, they were denied, but the bank allowed them to lend against a \$20,000 certificate of deposit.

Such financing struggles aren't unique. Among businesses with less than \$1 million in revenue that tried raising capital in the past 12 months, 36% had success at the bank. Among businesses with \$100 million to \$500 million in revenue, the success rate was 96%, according to an upcoming study from Pepperdine University that surveyed 10,637 privately-held businesses.

For the Turkins, things are finally starting to look up. Their business today has 75 employees and seven locations, three of which are franchises. Earlier this year, the Turkins partnered with a mid-size salsa company, which now has a sizable interest in the bakery, and changed over to the partner's bank. Recently, they sought a six-figure line of credit.

"There's no credit yet, but it's imminent, and the bank is putting together a program to accommodate future franchisees," says Mr. Turkin. But, he adds, "There's no question, we could have moved quicker if we'd had the credit earlier."

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