

Celebrating National Small Business Week??

by Charles Wendel

This week the Small Business Administration (SBA) has been celebrating National Small Business Week with webinars and other events aimed at 30 million small businesses. However, most banks have little to celebrate related to this group as banks avoid or underserve most of this segment in search of larger loans and deposits.

Small businesses continue to play a critical role in job creation and economic development and can provide substantial loan and fee income to banks. Still, most banks play lip service to this group rather than actively pursue them.

WHY?

- ✓ Small businesses are, well, small. No one small business is going to move a bank's revenue needle. Banks pursuing growth believe they are better off focusing on larger companies with larger loan needs and deposit potential than trying to focus on smaller companies. That is despite the higher margins these companies provide a bank.
- ✓ Banks can lose money from working with small businesses. Loans less than \$250K can be unprofitable unless a bank exploits streamlined processes and risk-base pricing, among other changes. To make lending profitable bank need to invest in digital IT and/or partner with Fintech-oriented third parties that can help them close technology gaps quickly and improve the customer experience.
- ✓ To generate profitability banks need to pursue small businesses differently versus larger companies. Banks always talk about relationship profitability and capturing more wallet share from each company. And, *finally*, many banks are making real progress in doing so. However, with small businesses, grabbing as much of the household-related revenues as possible is not an option; it is a necessity. From Day One with a new customer banks should have a process in place to capture all loan, deposit, and related business from the company. In addition, they need to focus on the owner's personal requirements, that is, deposits, credit cards, mortgages, investments, etc. Too often, banks fool themselves into believing that they can accomplish this focus or, even worse, believe they have already done so. But, most banks have only scratched the surface of relationship selling. Without that type of emphasis, they should avoid small businesses.
- ✓ Rather than the customized tailoring approach than many commercial bankers offer, small business is an off-the-shelf business in which a factory-like mentality has to prevail. For many banks this is outside their cultural comfort zone.

- ✓ What is small business anyway? Recently, during one day I heard bankers at the same bank describe small business as, in one case, involving loans up to \$500K and in another loans from \$50-100K. Other banks define small business based upon revenues or employee size. Still others refer to this group as SMEs, small and medium sized companies. But SMEs can incorporate everything from SOHOs to billion dollar companies. That range is way to large to be useful. Banks that want to serve small businesses need to determine which small businesses they want to serve.
- ✓ Following up on the above, segmentation is likely critical for small business success. Banks can base their segmentation discipline on industry, product type, life stage, etc.
- ✓ Applying commercial or corporate banking policies to small businesses will not work. Small businesses have neither the ability nor the inclination to provide extensive financial results or pro formas to their banks. Banks need to adjust their expectations and requirements in light of the realities of small business operations.
- ✓ Most senior bankers come from a corporate or commercial banking background, not retail or small business. Top management does not have the experience that would make them comfortable lending to companies where character is often more important than balance sheet. Further, small business often lacks a senior champion who understands the requirements for succeed as well as the time and “pain” required to achieve the payoff.
- ✓ Small businesses often need to be serviced and sold to by branch personnel. Many branch staff lack the knowledge to approach small businesses; other bankers are intimidated by them.
- ✓ Small business success takes years not months. It cannot be the “flavor of the month” but often is and, then, gets replaced by the next flavor such as wealth management.

Given all these and other challenges, why should banks celebrate small businesses?

Small businesses provide banks with a deposit rich segment, many of which will borrow at attractive rates and generate multiple fee opportunities. Many company owners are also open to their bankers as advisors and will use a bank for both personal and business needs.

As a segment they remain largely bank-dependent rather than being able to disintermediate banks as many larger companies have already done. In short they need banks more than most other segments, and the wiser banks know they may need these customers to build sustainable profitability.