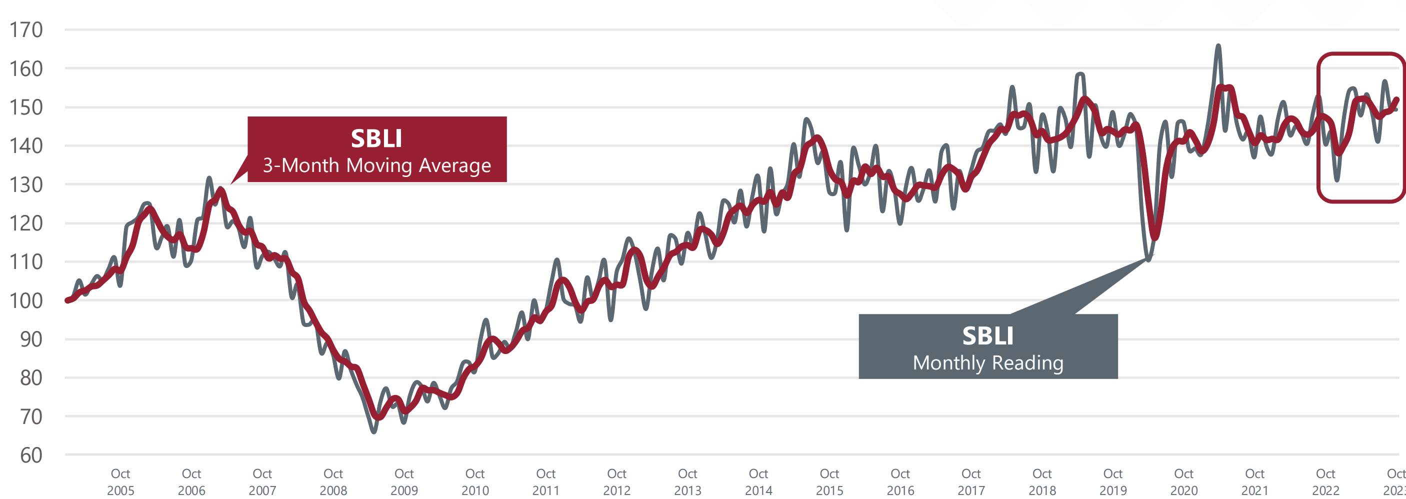
Equifax Commercial Strategic Insights: December 2023

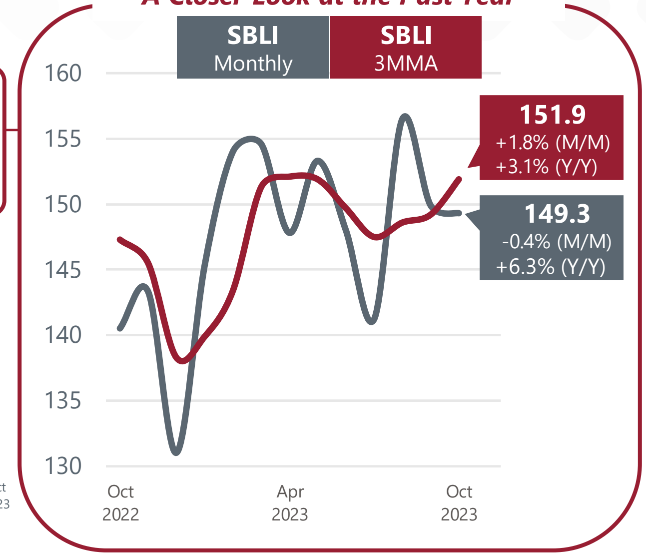
Small Business Lending Softens Amid Slower Demand and Tighter Credit

Equifax Small Business Lending Index (SBLI)*



*Volume of New Commercial Loans & Leases to Small Businesses, Seasonally Adjusted Index (January 2005 = 100)

A Closer Look at the Past Year



Index Analysis

The Equifax Small Business Lending Index (SBLI), a measure of nominal small business lending activity, dipped 0.6 points (-0.4%) in October to 149.3. The headline index is now 6.3% above its year-ago level. The SBLI 3-month moving average increased 1.8% in October to 151.9, up 3.1% Y/Y.

Regional Story: In October, small business lending rose in five of the ten largest states, including two that reached series highs: Georgia (+1.1% M/M) and Texas (+0.5% M/M). The largest month-over-month change was in Illinois (+1.8% M/M). Meanwhile, lending activity declined in Pennsylvania (-0.8% M/M), North Carolina (-0.4% M/M), and New York (-0.3% M/M). Measured on an annual basis, lending activity improved in eight of the ten largest states, led by Florida (+6.4% Y/Y), Michigan (+5.9% Y/Y), and North Carolina (+4.2% Y/Y). Lending activity declined in California (-2.2% Y/Y) and Pennsylvania (-0.5 Y/Y).

Industry Story: Small business lending rose on a monthly basis in 12 of 18 tracked industries in October, led by Construction (+2.1% M/M); Arts, Entertainment & Recreation (+1.7% M/M); and Health Care & Social Assistance (+1.2% M/M). Lending activity weakened the most in Mining, Oil & Gas (-5.4% M/M) and Professional, Scientific & Technical Services (-1.3% M/M). Compared to a year ago, lending rose in 14 of 18 industries, most notably in Arts, Entertainment & Recreation (+32.9% Y/Y) and Education (+26.7% Y/Y). In contrast, lending fell in Transportation & Warehousing (-13.8% Y/Y) and Agriculture (-11.3% Y/Y).

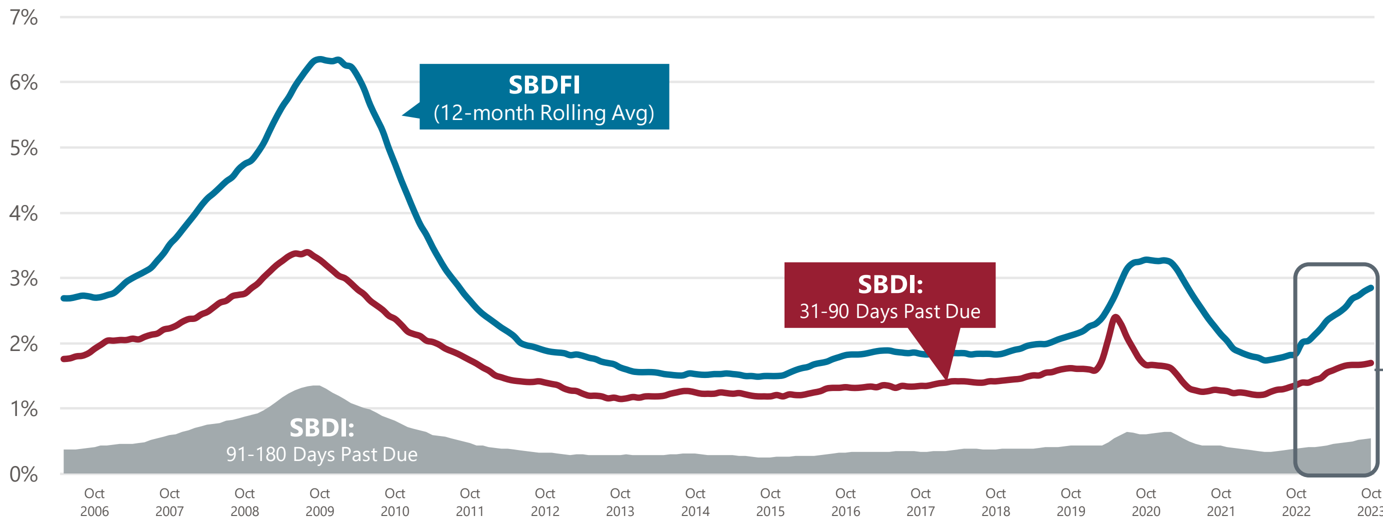
Economic Context

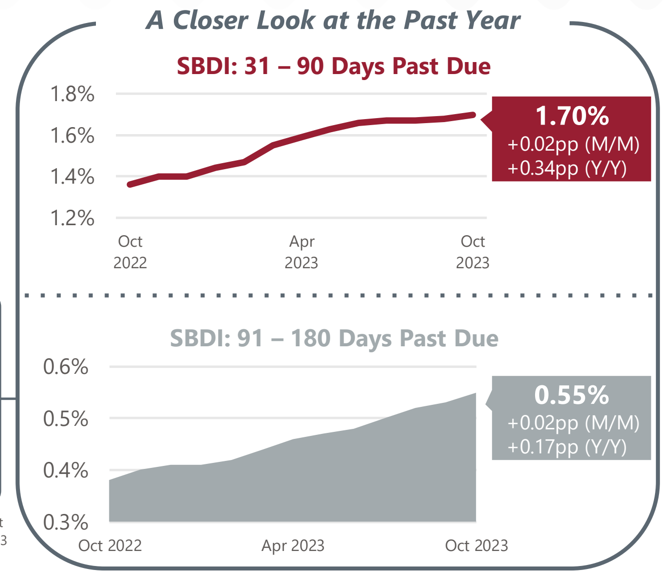
The Equifax Small Business Lending Index softened in October for the second consecutive month, providing additional evidence that nominal small business lending has slowed this fall. With financial stress rising and weaker economic growth expected in the near term, lenders appear to be pulling back: the Federal Reserve Senior Loan Officer Survey shows that nearly half of lenders tightened lending standards during the most recent quarter, while the Biz2Credit Small Business Loan Index indicates that loan approvals at large banks fell to 13% and 19.5% at large and small banks (respectively), roughly two percentage points below their year-ago levels.

In addition to tighter lending standards, the demand for commercial loans is also decreasing as high interest rates and weaker sales revenue combine to reduce small business owners' appetite for borrowing. Per NFIB, the net share of businesses that experienced higher sales over the last three months fell to -17%, the lowest reading since the height of the pandemic in mid-2020, while the net share of businesses who expect sales to improve in the next three months is -10%, the 22nd consecutive negative reading. These data suggest that while Main Street has benefitted from strong consumer activity over the last two years, consumers may finally be starting to pull back. Still, with inflation falling closer to acceptable levels, a mostly healthy labor market, lower interest rates on the horizon, and a "soft landing" scenario looking increasingly likely, there are reasons to be cautiously optimistic about the medium-term outlook for small business lending.

Main Street Delinquency and Default Rates Continue to Slowly Rise

Equifax Small Business Delinquency Index (SBDI)* & Default Index (SBDFI)**





*Delinquent Percentage of Small Business Loans, Seasonally Adjusted Index | **Default Percentage of Small Business Loans & Leases, Seasonally Adjusted Index*

Index Analysis

The Equifax Small Business Delinquency Index (SBDI) 31–90 Days Past Due increased 2bp in October to 1.70% and is now 34bp above its year-ago level. The SBDI 91–180 Days Past Due rose 2bp to 0.55% and is up 17bp Y/Y, while defaults rose 5bp in October to 2.85% and are now up 101bp Y/Y.

Regional Story: In October, delinquencies increased in seven of the ten largest states, led by Georgia (+9bp M/M) and California (+7bp M/M). Delinquencies eased in North Carolina (-4bp M/M) and were flat in Pennsylvania and New York. On an annual basis, delinquencies increased in nine of the ten of the largest states, led by Florida (+83bp Y/Y) and easing only in Illinois (-5bp Y/Y). Regarding defaults, nine of the ten of the largest states experienced an increase in October, led by New York (+54bp M/M). Defaults rose in all ten states on an annual basis, with triple-digit increases in six states, led by Georgia (+185bp Y/Y).

Industry Story: In October, delinquencies rose in five of the six tracked industries and were flat in Agriculture. As in previous months, delinquencies rose most notably for Transportation (+18bp M/M). On an annual basis, delinquencies climbed in all six tracked industries, led by a triple-digit increase in Transportation (+171bp Y/Y). Meanwhile, defaults increased in 11 of the 18 tracked industries in October, with sharp increases in Transportation (+29bp M/M) and Mining (+25bp M/M). Public Administration (-8bp M/M) and Information (-8bp M/M) saw the largest monthly declines. On an annual basis, defaults rose in 17 of the 18 tracked industries, led by Transportation (+444bp Y/Y).

Economic Context

Financial stress continues to build on Main Street, as both delinquency and default rates increased again in October across most states and industries, most notably in the transportation sector. According to the American Transportation Research Institute's annual survey, the greatest concern for carriers and commercial drivers was the unsteady U.S. economy, marking the first time the economy has been chosen as the top-ranked concern in the ATRI survey since the 2008-09 recession.

Outside the transportation sector, an increasing number of small firms are also struggling to keep up with payment obligations. One of the drivers for this increase in financial stress is high labor costs, which small business owners continue to cite as a key concern despite significantly lower inflation rates. The U.S. Chamber of Commerce's Q3 survey showed that roughly half of small businesses report that keeping up with salary expectations is a significant challenge. This cost burden is amplified by higher interest rates, which have increased the cost of monthly interest payments for some, including small firms that occasionally revolve credit to meet operational expenses. While the trends that are driving financial stress are not new, most small business owners have been able to overcome them due to a combination of strong consumer demand and government support, including the Employee Retention Tax Credit. With pandemic-era support programs winding down and consumer demand expected to slow, however, small business delinquency and default rates are likely to continue to climb in the months ahead.