TESTIMONY OF

ADMINISTRATOR STEVEN PRESTON

United States Senate

Small Business and Entrepreneurship Committee

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Chairman Kerry, Ranking Member Snowe, distinguished members of the Committee, thank you for inviting me here today to discuss the current state of our economy and the impact it is having on small businesses.

After 52 consecutive months (over 4 years) of job growth, our economy and our financial markets are going through a difficult time.

While the current state of our economy is under pressure, I continue to be optimistic that the ingenuity and resolve of American small business will help put our economy back on track.

Economic data shows that unemployment is still low at 5.1 percent and productivity remains strong. Exports are at an all-time high and growing, and for 2007 the federal deficit was 1.2 percent of the Gross Domestic Product which was well below the 40 year average of 2.4 percent of GDP.

However, real GDP growth fell to 0.6 percent in the fourth quarter of last year. Prices are up at the gas pump and in the supermarket, and home prices have declined.

These factors are clearly affecting the cost of running a small business and the markets for many of their products. In February, President Bush signed the bipartisan economic growth package which will inject over $152 billion into the economy. This package will support both consumer and business spending. The rebates that will begin distribution in May will support consumer spending, support job creation, and boost economic growth. The package also includes tax incentives for businesses to make investments in new equipment this year -- a 50 percent bonus deduction on new equipment that normally would be depreciated over a longer term, and an increase in the limit on expenses that small businesses can deduct from annual income. The boost from this stimulus will help buoy the economy in the coming months and strengthen consumer confidence.

Confidence in the economy is particularly important for small businesses. In deciding whether to invest in expanding their businesses, which may require taking on new debt, business owners want to be confident that the economy will be strong and customers will continue spending. We have seen some evidence that confidence among small businesses has declined in recent months and general concern about the state of the economy has increased. SBA has held numerous lender outreach meetings to discuss the situation with our lending partners. Many of these lenders have indicated that this uncertainty has resulted in a diminished demand for credit in the small business community. However, these lenders have not indicated a shortage of credit available for borrowers.

This is supported by the Federal Reserve Board's January 2008 Senior Loan Officer Opinion Survey on Bank Lending Practices, which shows one-fourth of both large and small domestic banks saw weaker demand for loans from small firms. Most domestic institutions that indicated a weakening of loan demand pointed to a decrease in customers' needs to finance inventories and investment in plant and equipment.

The survey also found that some domestic institutions have tightened their standards on commercial and industrial loans. This is consistent with Treasury Secretary Paulson's statement that sentiment has swung to risk aversion. While many lenders have experienced an increase in credit losses in the portfolio, they have responded by tightening their credit standards. We believe this will widen the pool of individuals who can be helped by SBA loans, and we are following up with new outreach and education efforts to reach these businesses. In addition, SBA is ready and available to help business owners who can no longer rely on their home equity lines of credit to finance business expansions.

As a reflection on the general economy SBA has seen a decline in its loan-guarantee volume both because of a lower demand for capital and because of a tightening of credit standards. Lenders generally have a strong desire to use the SBA guarantee to lessen their risk. We believe our programs will be a critical source of capital for small businesses in this environment.

The flow of capital between banks and small business borrowers is critical for economic growth. As I stated before, the Administration has been working diligently with lenders to ensure that much needed capital is available to small business owners. SBA has held roundtables around the country in cities including Boston, New York, Denver, Atlanta, San Francisco, Los Angeles, Philadelphia, and Washington as well as individual meetings around the country with hundreds of lenders in recent months to review their strategies and the quality of their portfolios, and to support their use of SBA products to reach small businesses. These sessions have given SBA the opportunity to both articulate the value of SBA's guarantee to lenders and discuss with lenders issues of concern to them.

SBA believes that our efforts in outreach are paying off. We have seen a 4 percent increase in new lenders using our programs. As these new avenues of lending open, we believe our programs will help lead to further economic growth.

You can be confident that the SBA is prepared to handle any increase in demand if lenders decide to rely more heavily on the government guaranteed lending products. Furthermore, SBA remains dedicated to its mission of providing capital to underserved markets and will continue to urge lenders to support this important segment of the market.

Thank you for the opportunity to share with you what SBA is doing to help borrowers face this current uncertainty and I look forward to answering any questions you many have.