

SMALL BUSINESS MARKET INSIGHTS



Reliance on Home Equity and Cards for Financing: A Disaster in the Making for Small Business Owners?

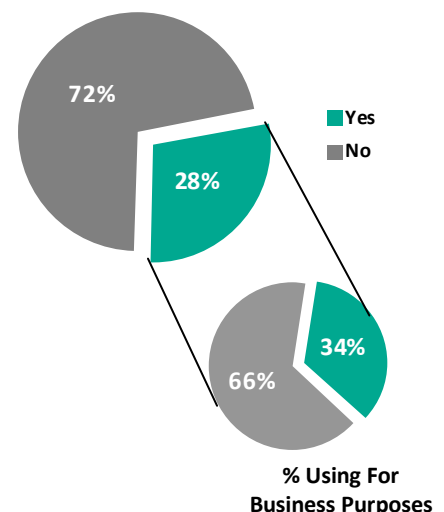
For the large number of small business owners reliant on home equity and credit card financing to support cash flow needs, the converging forces of the economic downturn and the housing meltdown may create a tsunami of problems for both these entrepreneurs and their lenders this year and into the near future.

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For many years small companies have used personal credit and credit cards to finance business activities. Up until the 2008 downturn, issuers aggressively courted the segment with Business cards to the tune of an estimated 720 million offers annually. Using home equity lines of credit and cash-out refinancings for business purposes became widespread in recent years as eager lenders offered these options to business owners and the self-employed. While some lenders marketed a HELOC for business product, others took a “don’t ask, don’t tell” approach during better economic times.

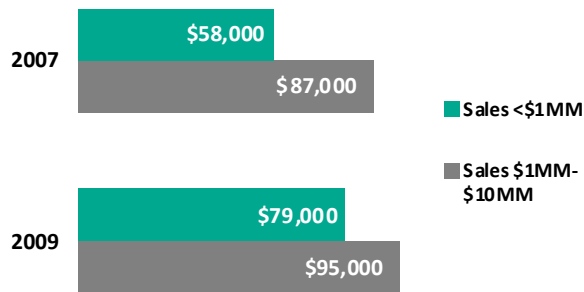
Now, more than a quarter of small business owners (28%) have personal home equity loans, lines or second mortgages. Thirty-five percent of those admit to using them for business financing, representing roughly 2.3 million businesses. While this hasn’t changed dramatically since 2007, the face of the borrower and the size of the balances have. Nearly twice as many companies in the \$1MM-\$10MM revenue segment use a HELOC exclusively for business compared to two years ago. These are not fledgling enterprises. More than a third of these companies have been in business longer than 10 years. Many of the owners are juggling more than one established business or in business-to-business sectors being squeezed by customers taking longer to pay.

% of Small Businesses Using Home Equity LOC/HE Loans/Second Mortgages



Balances on home equity loans and lines have ballooned 31% since 2007 to an average of \$79,000 for borrowers with sales <\$1MM and \$95,000 for companies in the \$1MM-\$10MM segment. Some of the leading small business providers have a large number of these retail lines and loans on the books. Borrowers cite using Wells Fargo/Wachovia (11%), Bank of America (9%) or Chase (8%) most commonly. Additionally, Capital One is a leading provider of other unsecured lines to this leveraged group.

**Average Balances on Home Equity Products
(Among those using for business)**



Credit-Hungry and Cash-Starved

The immediate future is not bright for many of these borrowers. Half expect the current economic climate to have a significant negative impact on their business. For the first time in more than a decade, small business owners say longer-term personal concerns such as preparing for a comfortable retirement are taking a back seat to boosting revenue in order to maintain a standard of living for themselves and their families – and to just pay the bills.

The segment of borrowers leaning on home equity and cards is credit-hungry and cash-starved:

- Most say managing cash flow is their greatest challenge.
- Sixty percent hold revolving balances on their cards and expect to carry those balances for more than two years.
- Half admit to missing a loan or credit card payment more than 6 times in the past year, a rate twice as high as the average small business.

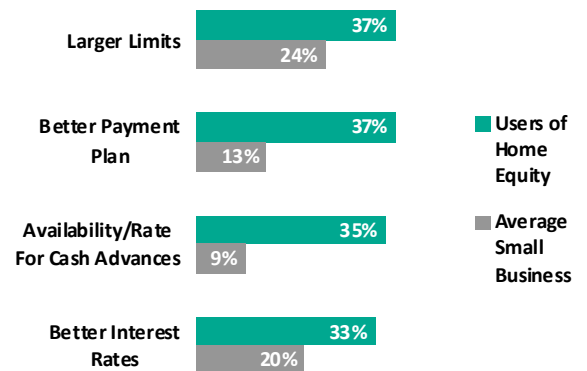
To improve the top-line, half plan to invest capital in marketing, sales and/or product development. To improve the bottom-line, payrolls are being trimmed.

Seeking relief from their credit crunch, these borrowers are three times as likely as average to have switched credit or card providers in the past year. Despite having challenges recently securing credit for the company, half will apply for a new line of credit or a SBA loan this year.

Praying Cards will be a Safe Haven

Unpredictable interest rates make it impossible to lean on cards as a way to finance growth. Despite growing costs and shrinking lines, business and personal card products are still viewed by these borrowers as an attractive (and necessary) way to deal with their short-term credit challenges. Many don't feel they have large enough lines and are actively looking at card offers. Frequently this means moving from business to personal card accounts to secure better payment plans or interest rates, more attractive cash advances, or larger limits. After the *Credit Card Accountability, Responsibility and Disclosure Act* goes into effect early next year, personal cards may provide a greater safe haven, if owners can hang on to them now.

**Reasons for Using Personal Cards
Instead of Business Cards
(Users of Home Equity for
Business vs. Other Small Business)**



Banks are actively seeking to mitigate risk and improve balance sheets by restricting or eliminating these critical sources of financing to millions of small businesses. Repercussions will be felt across the nation as the viability of many enterprises may be threatened, compounding the risk for both retail and small business lenders as the sector awaits economic recovery.

Sources

TNS Micro and Small Business Research conducts a comprehensive research study of 2000 companies with sales up to \$10MM each year. The study, founded in 1997, covers both business and personal banking relationships, behavior and attitudes.

TNS Omnibus Research conducts frequent studies of 400-500 mass small business owners using a weekly omnibus fielded to a national audience.

About TNS

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