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Nonmetro Businesses Get Federal Credit Assistance, in Some Areas More than Others

Nonmetro counties received 27 percent of Federal loans and loan guarantees during 1983-89, a slightly larger share than the nonmetro population's share of the national population (23.5 percent) and a much larger share than nonmetro income's share of national income (18.2 percent). The credit assistance was not evenly distributed among nonmetro counties, however. Poverty counties received less than other counties, and southern counties received less than counties elsewhere.

IN any financial market, a small business may be underserved because lenders lack information or because the risks inherent in the business are unknown. The cost of obtaining the information to make and service a loan may so outweigh the size of the loan that banks turn down otherwise creditworthy borrowers. The Government uses credit assistance to counteract some of the problems associated with small business loans. Government guarantees and insurance reduce the transaction cost of lending to small businesses. Furthermore, these programs provide a low-cost way for banks to learn about new customers and expand their private lending.

The Federal Government has established many credit assistance programs, but some are restricted to metro areas and many are administered indirectly through intermediaries whose locations are not necessarily the same as the locations of businesses receiving credit assistance. We examined six Federal programs that offered direct credit assistance and were available to nonfarm businesses in nonmetro areas during 1983-89 to see how well nonmetro businesses competed for available funding. See "Data and Methods" for an explanation of our selection process.

The six programs share the goal of helping small businesses, but they have different emphases and different requirements for beneficiaries and matching funds. The

Farmers Home Administration's Business and Industry Loans program is the only one that targets assistance to rural areas (Note: In 1992, this program was transferred to the Rural Development Administration). The four programs run by the Small Business Administration target businesses that have difficulty obtaining loans or surety bonds for various reasons. And, the Business Development Assistance program run by the Economic Development Administration targets businesses that will create or retain jobs in designated redevelopment areas. See "Program Characteristics" for more information on the programs.

Direct Loan or Guarantee?

Nearly all direct credit assistance in 1989 took the form of guaranteed loans. Guaranteed loans are administered by local financial intermediaries, and the Federal Government guarantees repayment of 70-90 percent of the loan amount. The guarantee shifts the risk for the insured portion of the loan from the financial intermediary to the Federal Government and allows the intermediary to sell the insured portion on a secondary market. The guarantee also allows the financial intermediary to make loans at or below market interest rates to businesses it otherwise would have deemed too risky. The uninsured portion of the loan gives the intermediary an incentive to choose and monitor the loan recipient carefully.

Loan guarantees also have advantages for the Government. First, guarantees allow the Government to achieve its goal of credit assistance without having to

make a payout unless the borrower defaults. Second, the involvement of professional lenders in the loan selection process ensures better quality loans. A lower proportion of guaranteed small business loans end in default than loans made directly by the Government (fig. 1).

Most Nonmetro Credit Assistance Comes from the Small Business Administration

Nonmetro counties received just under 27 percent of direct credit assistance expenditures during 1983-89, roughly the same percentage each year (fig. 2). However, the programs vary widely in the amount of assistance and the consistency of their disbursements to nonmetro counties (table 1).

The Small Business Loans Program (7(a) loans) provided \$4.5 billion in loans to nonmetro counties, accounting for 72 percent of Federal funding received by businesses in nonmetro counties during 1983-89. This program was the most important to nonmetro areas both in terms of dollar outlays and number of places in which loans were made. The program consistently provided about 27 percent of its funds to nonmetro counties. The Bond Guarantees for Surety Bonds program, which guarantees surety bonds for building contractors, guaranteed \$6.23 billion in bonds, 22.8 percent of which were with nonmetro surety companies. This amount, however, may not reflect the entire bond assistance to nonmetro contractors, because the payments and guarantees go to the surety company holding the bond and not to the contractor posting the bond.

The other two SBA direct programs, Loans for Small Businesses and Veterans' Loan Program, were in transition during the study period. The Veterans' Loan

Program was initiated in 1985. In 1990, both programs were incorporated into the Small Business Loans Program. They were relatively small, together accounting for about 1 percent of total nonmetro assistance.

The FmHA's Business and Industrial Loans Program, the only program that targets rural areas, gave 76.9 percent of its 1983-89 funding to nonmetro counties. However, this outlay amounted to only 4.2 percent of the funds that nonmetro counties received. The other non-SBA program, the Economic Development Administration's Business Development Assistance Program, provided only 0.3 percent of the direct credit assistance going to nonmetro businesses.

The main burden of Federal credit assistance is borne by the SBA's Small Business Loan Program, and nonmetro areas captured a proportionate share of the available assistance. But how did this assistance affect rural development?

Federal Credit Assistance Helps Developing Counties Most

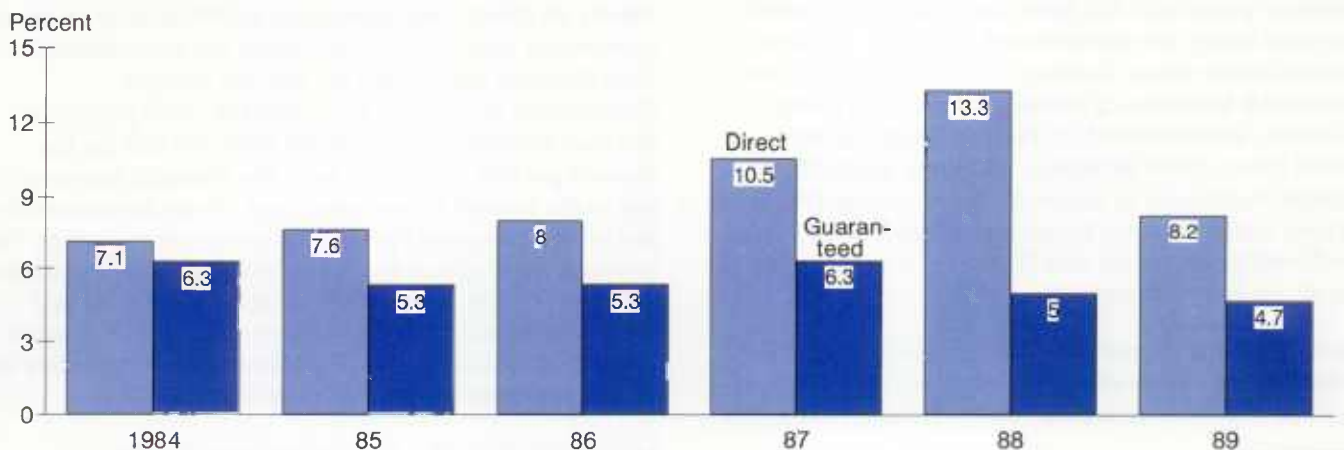
Federal credit assistance is available to the public, but funds go only to businesses that apply. The demand-driven nature of the programs means that funding is likely to sustain rather than seed development.

Since credit assistance programs are demand-driven, low levels of funding are likely in counties with low levels of economic activity or dominated by businesses not eligible for assistance. We used county classifications from the ERS typology to investigate which types of nonmetro counties received the most assistance. The farming-dependent, mining-dependent, manufacturing-dependent, poverty (persistent low income), and retirement-destination county types we used are defined in

Figure 1

Default rates on small business loans made directly or guaranteed by the Federal Government

Loan guarantees are more attractive to the Government because they less frequently end in default



Source: Office of Management and Budget, *Budget of the United States Government*, "Direct Loan Write-offs and Guaranteed Loan Terminations by Default," table in Special Analyses, Section F, 1986-90, and in Appendix, Section F, 1991.

"Data and Methods." We measured each county type's receipt of assistance in four ways: (1) amount of credit assistance per capita, (2) amount of credit assistance per county business, (3) amount of credit assistance per \$100 of total county income, and (4) percentage of counties receiving assistance.

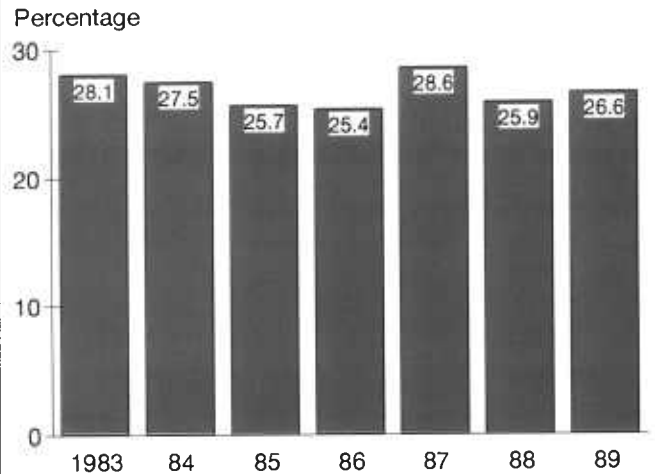
Manufacturing-dependent and poverty counties ranked lowest on all three monetary measures of credit assistance (table 2). Among nonmetro county types, manufacturing-dependent counties are likely to have larger businesses that are ineligible for assistance. Poverty counties are, by definition, counties where low per capita incomes have persisted for decades indicating low economic activity. Although assistance amounts were lower than average in manufacturing counties, assistance was widely distributed across counties. Only 3.2 percent of manufacturing counties did not receive assistance, a lower percentage than the percentage of all counties not receiving assistance. By contrast, 11.5 percent of the poverty counties did not receive credit assistance, the highest share of any county type. The difference in counties without assistance suggests that manufacturing-dependent counties are participating, but the amount of credit assistance is dwarfed by their larger economies, and that the poverty counties are not participating to the same extent as other county types because of the lack of business opportunities.

The farming-dependent, mining-dependent, and retirement-destination counties matched or exceeded national average levels of assistance. Only 3.6 percent of retirement-destination counties did not receive credit assistance, but the farming and mining groups each had about 9 percent of counties not receiving assistance.

Figure 2

Nonmetro share of direct Federal credit assistance

Nonmetro areas have received about 27 percent of direct Federal credit assistance each year since 1983



Source: Computed by ERS using data from the Consolidated Federal Funds Report.

Table 1

Nonmetro amount and share of direct Federal credit assistance by program

Nonmetro areas get a more than fair share of Small Business Loans (7(a)), by far the largest source of direct Federal credit assistance

Program	1983	1984	1985	1986	1987	1988	1989	1983-89
Million dollars								
All programs	786.2	877.0	866.5	795.2	920.7	943.1	1,108.2	6,296.8
Business and Industrial Loans	4.9	8.5	.6	0	109.7	58.9	79.9	262.6
Business Development Assistance	6.4	1.1	.5	9.7	0	0	.1	18.8
Loans for Small Businesses	4.5	5.5	1.9	3.7	7.6	8.9	16.4	48.5
Small Business Loans (7(a))	650.5	727.7	645.2	556.8	577.6	631.3	739.7	4,528.8
Bond Guarantees for Surety Companies	119.9	134.2	218.3	220.9	220.7	239.7	266.7	1,420.4
Veterans' Loans	NA	NA	NA	4.0	5.1	4.3	5.4	18.7
Percentage of total assistance								
All programs	28.1	27.5	25.7	25.4	28.6	25.9	26.6	26.8
Business and Industrial Loans	100.0	100.0	92.7	0	77.1	73.2	76.3	76.9
Business Development Assistance	17.4	5.7	4.6	28.0	0	0	5.3	16.3
Loans for Small Businesses	17.0	16.6	13.7	20.5	35.8	17.8	50.1	24.2
Small Business Loans (7(a))	30.0	28.4	26.9	26.1	27.8	26.2	26.1	27.3
Bond Guarantees for Surety Companies	21.3	23.5	22.9	23.5	22.9	22.4	22.8	22.8
Veterans' Loans	NA	NA	NA	27.2	27.0	25.4	29.7	27.4

NA = Not applicable, program did not start making loans until 1986.

Source: Calculated by ERS using data from Consolidated Federal Funds Reports.

The characteristics of counties that received no direct credit assistance also show that Federal credit assistance programs are demand driven. Of the 148 counties that received no assistance, 142 were nonmetro. Average per capita income and number of businesses were lower in nonmetro counties receiving no funding than for all nonmetro counties, and average population was one-third that for all nonmetro counties (table 3). These characteristics all point to there being fewer business projects that might qualify for funding in counties that received no assistance.

Less Federal Credit Assistance Goes to the Nonmetro South

Assistance is also unevenly distributed across nonmetro counties by region and State. The level of funding in the South was lower than in other regions by all three monetary measures (table 4). Again, the demand-driven nature of the programs appears to handicap the South, which has higher shares of poverty counties and counties receiving no assistance.

Per capita credit assistance also varies widely among nonmetro areas by State (fig. 3). Nonmetro

Table 2

Receipt of direct Federal credit assistance by county type, 1983-89

Manufacturing-dependent and persistent poverty counties received less assistance than other counties

County type	Counties	Amount of credit assistance			Counties receiving no assistance
		Per capita	Per business	Per \$100 of income	
	Number	Dollars			Percent
United States	3,063	14.65	676.28	1.27	4.8
Nonmetro county type:					
Farming-dependent	714	15.90	741.67	1.36	9.2
Mining-dependent	215	16.42	728.30	1.50	8.8
Manufacturing-dependent	942	10.71	549.43	.93	3.2
Persistent poverty	243	8.22	583.86	1.02	11.5
Retirement-destination	531	14.75	680.88	1.37	3.6

Source: Calculated by ERS using program data from Consolidated Federal Funds Report, population and income data from the Bureau of Economic Analysis, and business data from County Business Patterns.

Table 3

Characteristics of nonmetro counties receiving no direct Federal credit assistance, 1986

Counties receiving no assistance have smaller populations, lower incomes, and fewer businesses than average

County type	Counties	Population	Per capita income	Businesses per 100 persons
	Number		Dollars	Number
All nonmetro counties	2,366	23,781	11,228	2.18
Counties receiving no assistance	142	7,563	11,028	1.77

Source: Calculated by ERS using program data from Consolidated Federal Funds Report, population and income data from the Bureau of Economic Analysis, and business data from County Business Patterns.

counties in nine Southern States averaged \$8 or less in credit assistance per capita, and none of the Southern States averaged more than \$16 in non-metro credit assistance per capita. Nonmetro coun-

ties in only five States outside the South ranked in the lowest average assistance group.

The highest average nonmetro credit assistance is clustered in the Plains and Mountain States of

Table 4
Nonmetro receipt of direct Federal credit assistance by region, 1983-89

Nonmetro counties in the South average less assistance than counties in other regions at least partly because more southern counties are persistently poor and/or received no assistance

Region	Amount of credit assistance			Counties receiving no assistance	Poverty counties
	Per capita	Per business	Per \$100 of income		
	Dollars			Percent	
Northeast	19.76	663.62	1.44	3.0	.0
Midwest	18.02	730.51	1.49	2.6	1.8
South	7.93	404.78	0.77	9.5	21.0
West	25.80	999.42	2.25	4.2	1.2

Source: Calculated by ERS using program data from Consolidated Federal Funds Reports, population and income data from the Bureau of Economic Analysis, and business data from County Business Patterns.

Data and Methods

The *1989 Catalog of Federal Government Assistance* lists 1,139 Federal assistance programs. Using the catalog, we identified six direct programs that could be used by rural businesses to enhance their access to the credit market. Programs aimed solely at metro areas, such as programs for urban renewal, were not considered.

Direct participation programs are those in which the Government provides a loan, loan guarantee, grant, or insurance directly to the program beneficiary. Indirect participation programs are those in which the Government channels its funds through a non-Federal agency, such as a development company. This division determines how the money is administered and how the data are collected, but it does not affect the type of assistance provided. We analyzed only direct participation programs because data on the location of borrowers are not available for indirect participation programs.

Once the appropriate programs were identified, we went to the Consolidated Federal Funds Report (CFFR) data tapes to obtain data on program expenditures. The Bureau of the Census has produced the CFFR tapes annually since 1983. The CFFR reports Federal Government program expenditures on grants, salaries and wages, procurement, direct payments to individuals, other direct payments, direct loans, guaranteed or insured loans, and insurance.

We used the metro-nonmetro designation of counties as of the 1980 Census (announced by the Office of Management and Budget in 1983) and further disaggregated nonmetro counties using the original ERS typology codes. The county types we analyze are defined as:

Farming-dependent—Farming contributed a weighted annual average of 20 percent or more to total labor and proprietors' income during 1975-79

Mining-dependent—Mining contributed 20 percent or more to total labor and proprietors' income in 1979

Manufacturing-dependent—Manufacturing contributed 30 percent or more to total labor and proprietors' income in 1979

Poverty—Ranking in the lowest per capita income quintile of all counties in 1950, 1959, 1969, and 1979

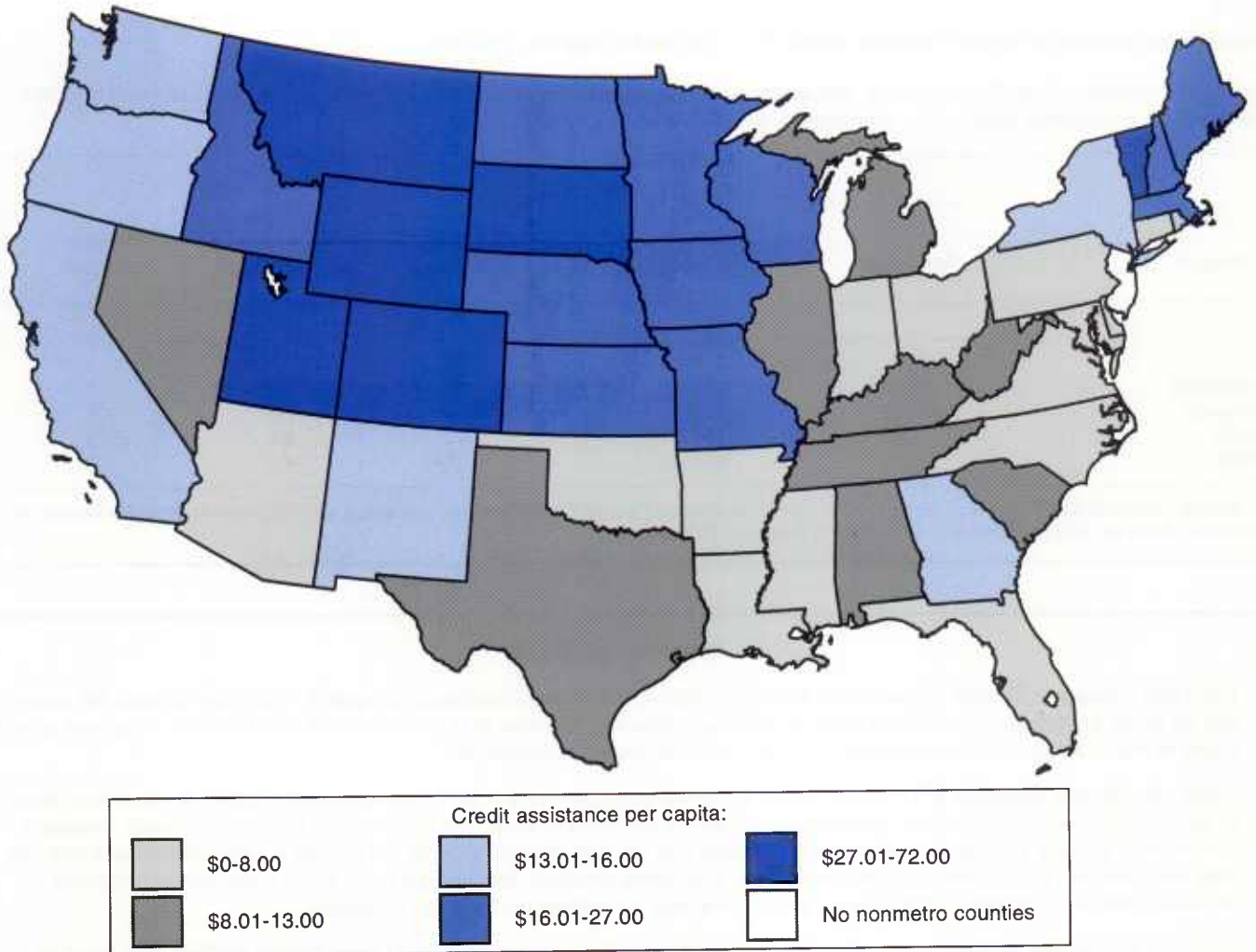
Retirement-destination—The population aged 60 or older in 1980 was at least 15 percent larger than the estimated population without migration

These county types were published in *The Diverse Social and Economic Structure of Nonmetropolitan America*, by L. D. Bender, B. L. Green, T. F. Hady, J. A. Kuehn, M. K. Nelson, L. B. Perkinson, and P. J. Ross, RDRR No. 49, USDA-ERS, Sept. 1985.

Figure 3

Per capita direct Federal credit assistance, nonmetro county average by State, 1983-89

Low nonmetro per capita credit assistance is concentrated in Southern and Eastern States; high assistance in Midwestern and Western States



Source: Calculated by ERS using data from the Consolidated Federal Funds Report.

Colorado, Montana, South Dakota, Utah, and Wyoming, with Vermont the only other State with nonmetro credit assistance averaging over \$27 per capita. Nonmetro counties in these States tend to be sparsely populated like many southern counties, but they average higher incomes than the southern nonmetro counties. Also, many counties in these States are outside the commuting range of metro areas, while many southern counties are adjacent to metro areas. Credit assistance may be going to businesses in smaller, nonmetro cities in these Plains and Mountain States while businesses in larger, metro cities may be the more likely recipients of credit assistance in the South. In a previous analysis, we found that nonmetro

counties that are not adjacent to metro areas average much higher credit assistance per capita than nonmetro counties that are adjacent to metro areas (see Marlor and McGlone in "For Further Reading...").

Implications for Rural Development

Our analysis indicates that nonmetro areas overall are receiving a share of Federal credit assistance proportional to their share of the national population. Thus, credit assistance programs can be and likely are being used to support rural development. However, the demand-driven nature of the programs means that smaller areas with fewer businesses are less likely to

Program Characteristics

Program: Business and Industrial Loans

Administering Agency: Farmers Home Administration, U.S. Department of Agriculture, during the period analyzed. Now administered by the Rural Business and Economic Development Service, U.S. Department of Agriculture. **Types of Assistance:** Guaranteed and insured loans **Objectives:** To help public, private, or cooperative (profit or nonprofit) organizations obtain quality loans for improving, developing, or financing business, industry, and employment and improving the economic and environmental climate in rural communities, including pollution abatement and control. Preference is given to rural areas and towns of 25,000 or fewer residents.

Program: Economic Development - Business Development Assistance

Administering Agency: Economic Development Administration, U.S. Department of Commerce **Types of Assistance:** Loan guarantees and grants **Objectives:** To sustain industrial and commercial viability by providing financial assistance to businesses that create or retain permanent jobs or expand/establish plants in redevelopment areas. Projects are funded when financial assistance is not available from other sources on terms and conditions that would permit accomplishment of the project and further economic development in the area.

Program: Loans for Small Businesses (Business Loans 7(a)(11))

Administering Agency: Small Business Administration **Types of Assistance:** Direct loans, guaranteed loans, advisory services, and counseling (Guaranteed loans were transferred to the Small Business Loans program in 1990, after our study period.) **Objectives:** To provide loans to small businesses owned by low-income persons or located in areas having high unemployment rates or high percentages of low-income individuals.

Program: Small Business Loans (Regular Business Loans 7(a))

Administering Agency: Small Business Administration **Types of Assistance:** Direct, guaranteed, and insured loans, including immediate participation loans (Direct loans were made during 1983-88. The program changed to guaranteed loans in 1989.) **Objectives:** To provide loans to small businesses which are unable to obtain financing in the private credit marketplace, but can demonstrate an ability to repay loans granted; to low-income business owners or businesses located in areas of high unemployment; to nonprofit sheltered workshops and other similar organizations which produce goods or services; to small businesses being established, acquired, or owned by handicapped individuals; and to small businesses manufacturing, designing, marketing, installing, or servicing specific energy-related equipment or procedures.

Program: Bond Guarantees for Surety Companies

Administering Agency: Small Business Administration **Types of Assistance:** Insurance **Objectives:** To guarantee up to 80 percent of surety bonds by commercial surety companies for small contractors unable to obtain a bond without a guarantee.

Program: Veterans Loan Program

Administering Agency: Small Business Administration **Types of Assistance:** Direct loans **Objectives:** To provide loans to small businesses at least 51 percent owned by Vietnam-era or disabled veterans.

receive assistance. The farming-dependent, mining-dependent, and poverty counties illustrate this point, with much higher percentages of those groups than of the larger manufacturing-dependent counties and the faster growing retirement-destination counties receiving no assistance.

To lead rural development efforts, Federal credit assistance would have to participate in the initiation of businesses, a role the programs are not designed to play. If local entrepreneurs, perhaps with the help of rural development specialists, can develop viable businesses in smaller rural counties, direct Federal credit assistance programs can provide the loans or loan guarantees they need to start up or expand.

For Further Reading . . .

Felice S. Marlor and James M. McGlone, *Federal Nonfarm Business Credit Assistance: An Analysis of Disbursements to Rural Areas*, AGES-9214, USDA-ERS-ARED, May 1992.

James M. McGlone, "Rural Businesses Voice Few Complaints About Their Banks," *Rural Development Perspectives*, Feb.-May 1991, pp. 33-38.

Ron Shaffer and Glen Pulver, "Rural Nonfarm Business' Access to Debt and Equity Capital," *Financial Market Intervention as a Rural Development Strategy*, AGES-9070, USDA-ERS-ARED, Dec. 1990, pp. 39-48.