

Small Business Checkpoint

Business formation boom

19 September 2023

Key takeaways

- Even as the economy moderates, new business applications remain elevated this year. The accommodation & food services and healthcare sectors show particular strength, likely fueled by continued consumer demand for leisure and the limited supply of healthcare services, respectively.
- According to Bank of America internal data, small business spending is strongest among healthcare firms with total payment per small business client up 8% year-over-year (YoY) in August. Moreover, these companies are also seeing stronger profits than the overall trend.
- Looking more broadly at small business activity in August, payments per small business client were down 2.4% YoY as high operating costs weigh on spending elsewhere. According to the Bank of America Summer 2023 Small Business Owner Pulse Survey, 70% of small businesses with a physical location have had to deal with rising utility bills and high property taxes.

Small Business Checkpoint is a regular publication from Bank of America Institute. It aims to provide a real-time assessment of small business spending activities and financial well-being, leveraging the depth and breadth of Bank of America's proprietary data. Such data is not intended to be reflective or indicative of, and should not be relied upon as, the results of operations, financial condition or performance of Bank of America

A start-up boom

While the pandemic brought major disruption to US businesses, it also led to a surge in new business formations. What is striking to us is that this elevated level has continued post-Covid. According to data from the Census Bureau, in July, high-propensity business applications, which include all those that are more likely to become businesses with a payroll, were 40% higher than the average level in 2019 (Exhibit 1). While not all of these businesses survive (the number of business deaths also rose in 2022 according to the Bureau of Labor Statistics), the net impact still points to strong growth in business formation.

Exhibit 1: High propensity business applications (index, 2019 average =100)

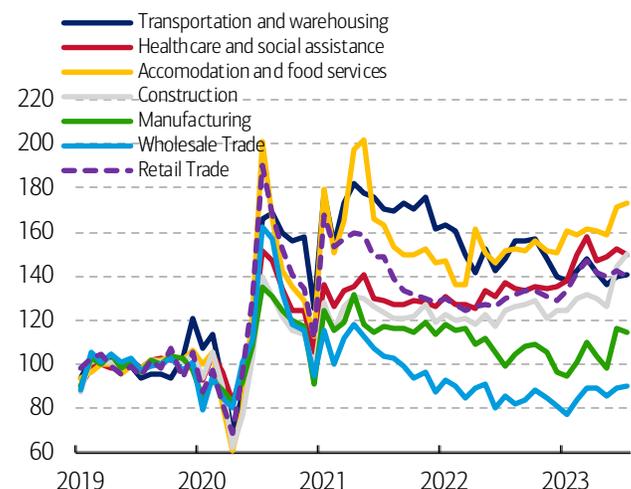
Applications were 40% higher than the average level in 2019 in July



Source: Census Bureau

Exhibit 2: High propensity business applications by major industries (index, 2019 average =100)

Business applications in each year are driven by a different sector



Source: Census Bureau

As Exhibit 2 shows, business applications each year seems to be driven by a different sector. At the start of the pandemic, retail trade saw the biggest surge, driven largely by the growing demand for e-commerce, according to commentaries from the Census Bureau. Meanwhile in 2021 and early 2022, supply chain bottlenecks emerged, likely leading to a surge in transportation and warehousing services demand.

More recently, three sectors have emerged as leading the growth in business formation: accommodation & food services, healthcare & social assistance, and construction. The rise in hotel and restaurant businesses formation is no surprise as the boom in consumer spending in these areas likely fueled the expansion. The construction sector, as we wrote in a prior [Small Business Checkpoint](#), is seeing a boom with manufacturing construction spending showing a record rate of increase of 80% YoY in June, according to the Census Bureau. This likely reflects the ongoing reshoring effort by the US to bring back manufacturing, as supported by policies such as the Creating Helpful Incentives to Produce Semiconductors and Science Act (CHIPS Act) and the Inflation Reduction Act (IRA).

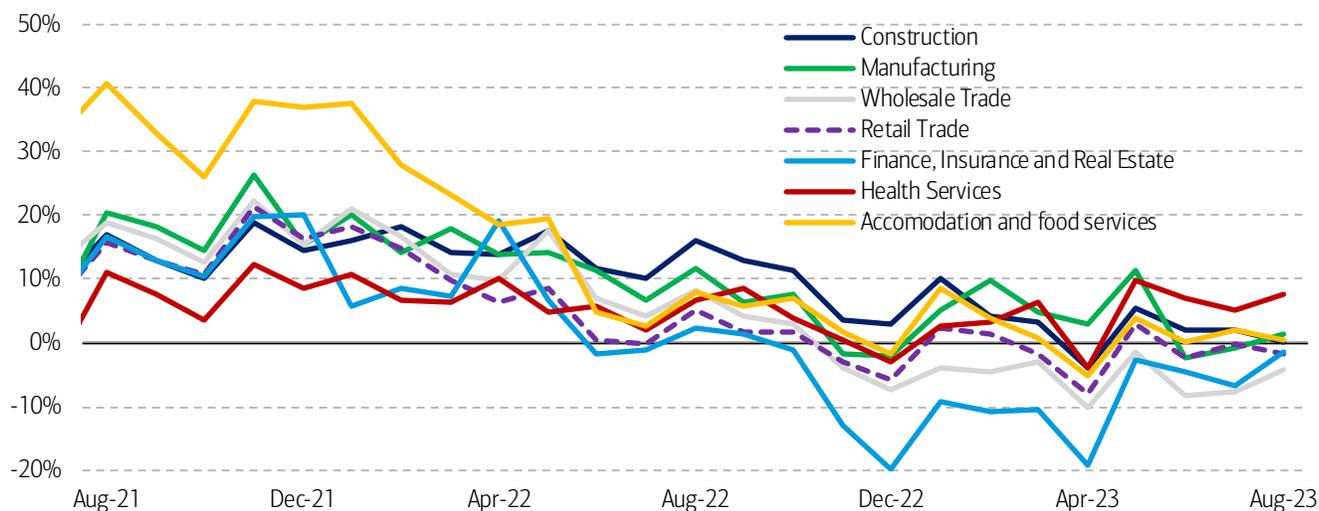
Healthcare wanted

The growing demand for healthcare services is partly attributable to ageing baby boomers and the pandemic aftermath. According to a study by the University of Pennsylvania, the number of home care workers per 100 Medicaid participants fell by more than 11% between 2013 and 2019. Preliminary estimates suggest further declines in 2020. As such, the gap between supply and demand in the healthcare space might be fueling more businesses formations.

With regards to existing healthcare companies, they might be expanding as well. According to Bank of America internal data, small business payments growth is the strongest among healthcare firms. Specifically, in August 2023, total payment per small business client, which includes automated clearing house (ACH), credit and debit cards, wires, checks and person-to-business payments, was up 8% YoY for the health services – the highest of all major sectors (Exhibit 3).

Exhibit 3: Small business payments growth by select industries, according to Bank of America internal data (monthly, %YoY)

Healthcare companies have strongest small business payments growth compared to other sectors since June



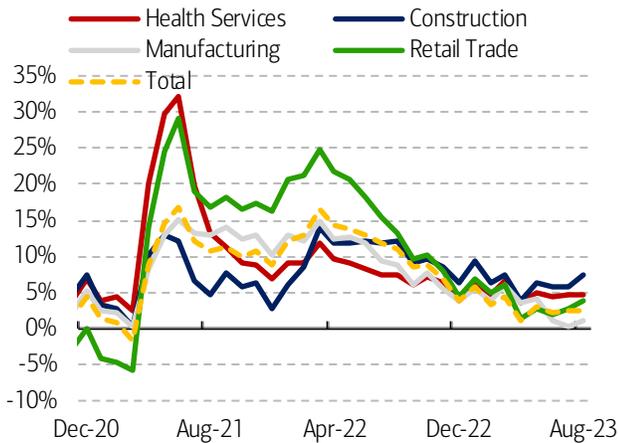
Source: Bank of America internal data

Expansion of businesses also means more hiring activity. We found that payroll spending per client is also increasing faster for health services companies than the overall trend (Exhibit 4). The only major sector seeing higher payroll spending growth is construction – another area with strong demand as discussed earlier.

In our view, demand for more business formations in the healthcare space could increase further as this sector continues to see stronger profit margins than other industries. According to Bank of America internal data, the ratio of inflows-to-outflows in small business checking and savings accounts, which we view as a proxy for profits, was well above 1 for the three-month period through August, the highest among the major sectors (Exhibit 5).

Exhibit 4: Growth in small business payroll payments by select sectors (% YoY, 3-month moving average)

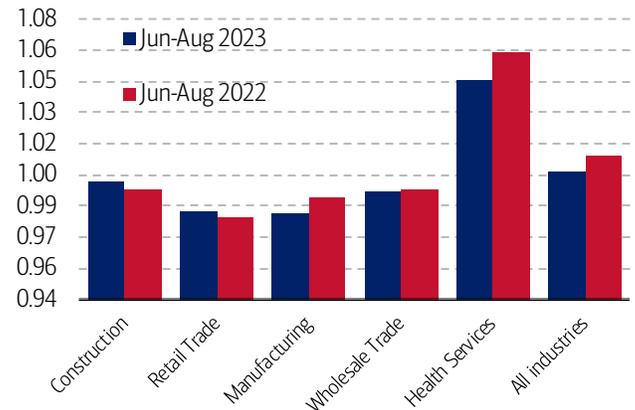
Payroll spending per small business client is increasing faster for health services companies than the overall trend



Source: Bank of America internal data

Exhibit 5: Inflow-to-outflow ratio for small businesses, based on Bank of America internal data (1+ = inflow greater than outflow)

Health services' ratio is well above the 2022 period



Source: Bank of America internal data

Challenges persist for small businesses

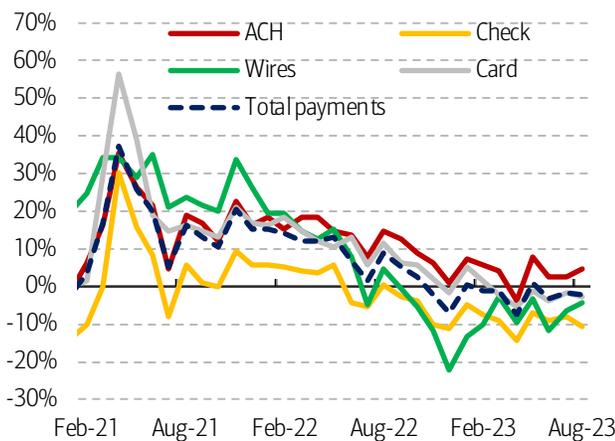
Looking more broadly at small business activities in August, total payments per small business client remained in negative territory at -2.4% YoY, broadly in line with the previous few months. Among the major components, ACH showed the largest increase, up 4.5% YoY in August.

Keep in mind that ACH captures a significant portion of small business operating expenses, including rent payments or other real estate expenses. Therefore, elevated ACH payments could point to high operating costs, which would be a headwind to small businesses.

In fact, the [Bank of America Summer 2023 Small Business Owner Pulse Survey](#) found that small business owners are indeed feeling challenges related to real estate. According to the survey, 65% currently use a physical location as their primary method of conducting business. But over the last 12 months, 70% of those have faced difficulties that are impacting business operations. High utility costs and high property taxes are the two most reported challenges (Exhibit 7). Finding the right space in terms of size and location as well as financing are also concerns.

Exhibit 6: Small business payments growth by channel, based on Bank of America internal data (monthly, %YoY)

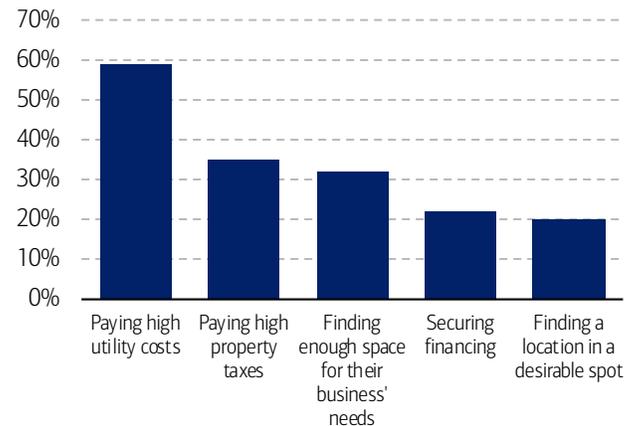
ACH showed the largest increase in August, up 4.5% YoY



Source: Bank of America internal data

Exhibit 7: Top challenges among small business owners with a physical location (% of respondents)

High utility costs are the top challenge for respondents



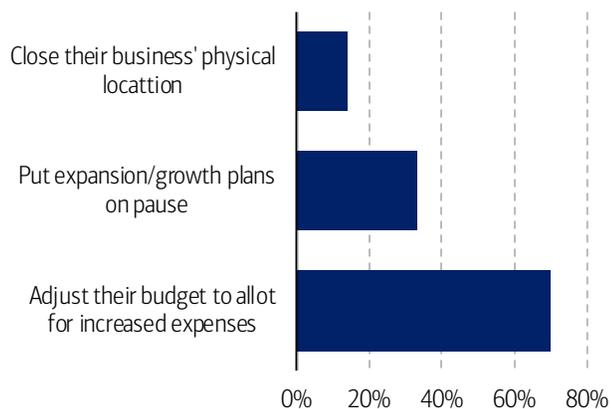
Source: Bank of America Summer 2023 Small Business Owner Pulse Survey

Since over half of small business owners in the Bank of America Summer 2023 Small Business Owner Pulse Survey report that costs from their physical location are impacting operations, many are having to adapt. How? 70% reported adjusting their budgets for increased expenses, but 14% have closed their physical location (Exhibit 8).

When looking to the rest of 2023, 68% of small business owners anticipate interest rates will increase. And 20% said rising interest rates are making them less likely to have a physical location. Given these concerns, it's fair to assume trends related to real estate will continue to change. Of the 84% of small business owners anticipating changes to small business real estate over the next five years, the biggest prediction is that more businesses will be fully online or digital (Exhibit 9).

Exhibit 8: Actions taken by small business owners due to costs from their physical location impacting business operations (% of respondents)

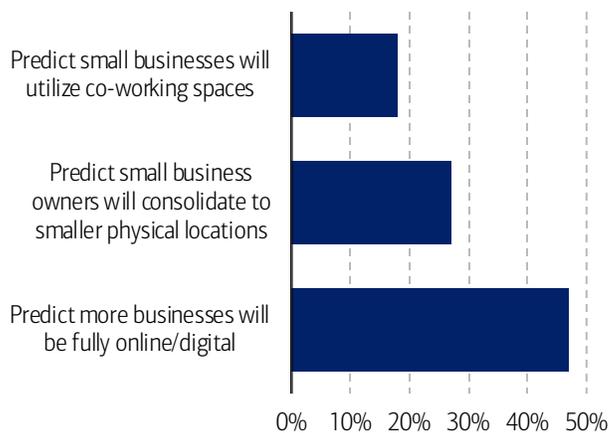
70% of respondents plan to adjust their budget to allot for increased expenses



Source: Bank of America Summer 2023 Small Business Pulse Survey

Exhibit 9: Anticipated changes in small business real estate over the next five years (% of respondents)

Their biggest prediction is that more businesses will be fully online or digital



Source: Bank of America Summer 2023 Small Business Pulse Survey

Methodology

Selected Bank of America transaction data is used to inform the macroeconomic views expressed in this report and should be considered in the context of other economic indicators and publicly available information. In certain instances, the data may provide directional and/or predictive value. The data used is not comprehensive; it is based on **aggregated and anonymized** selections of Bank of America data and may reflect a degree of selection bias and limitations on the data available.

Any **Small Business** payments data represents aggregate spend from Small Business clients with a deposit account or a Small Business credit card. Payroll payments data include channels such as ACH (automated clearing house), bill pay, checks and wire. Bank of America per Small Business client data represents activity spending from active Small Business clients with a deposit account or a Small Business credit card and at least one transaction in each month. Small businesses in this report include business clients within Bank of America and are generally defined as under \$5mm in annual sales revenue.

Payments to small business-focused hiring firms include both direct deposits through Automated Clearing House (ACH) and payments via credit and debit cards.

Unless otherwise stated, data is not adjusted for seasonality, processing days or portfolio changes, and may be subject to periodic revisions.

Data regarding merchants who receive payments are identified and classified by the Merchant Categorization Code (MCC) defined by financial services companies. The data are mapped using proprietary methods from the MCCs to the North American Industry Classification System (NAICS), which is also used by the Census Bureau, in order to classify spending data by subsector. Spending data may also be classified by other proprietary methods not using MCCs.

Ipsos conducted the Bank of America Summer 2023 Small Business Owner Pulse Survey online between July 19 and July 25, 2023 using a pre-recruited online sample of small business owners. Ipsos contacted a national sample of 542 small business owners in the United States with annual revenue between \$100,000 and \$4,999,999 and employing between two and 99 employees. The final results for the national sample were weighted to national benchmark standards for size, revenue and region.

Additional information about the methodology used to aggregate the data is available upon request.

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