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Small Business Checkpoint

Dealing with inflation

24 April 2024

Key takeaways

- According to the latest National Federation of Independent Business (NFIB) survey, small businesses report inflation as the single most important problem in operating their business. This is likely a strong driver behind the recent slide in small business optimism which reached the lowest level in 11 years.
- How are small businesses reacting to inflationary pressures? Bank of America aggregated and anonymized small business credit card data signals small businesses are increasingly reliant on credit cards to finance their operations, with small business credit card balances up 18% since 2019.
- While rising credit card balances raises some concerns, the inflation-adjusted credit card balance is comparable to or even lower than 2019 levels. Additionally, balance sheet conditions remain relatively healthy for small businesses.

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.

Inflation continues to weigh on small businesses

In March, according to the National Federation of Independent Business (NFIB), small business optimism fell to the lowest level in over a decade, decreasing to 88.5, the lowest level since December 2012 (Exhibit 1).

What's behind this slide in sentiment? The NFIB survey suggests that a strong factor behind small business owners' decline in confidence is due to inflation, with 25% of owners having reported inflation as the single most important problem in operating their business (Exhibit 2). In response to rising inflation, it appears firms are reacting by raising their average selling prices, although the percent of small businesses doing so has come down from its peak in March 2022.

Exhibit 1: In March, small business optimism reached the lowest level since 2012

NFIB Small Business Optimism Index (monthly, SA, 1986 = 100)

Source: NFIB

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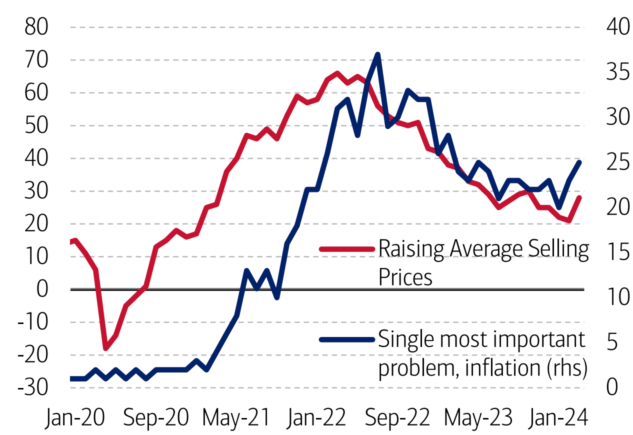
Exhibit 2: In response to rising inflation, it appears small businesses are raising average selling prices

Percent of firms raising average selling prices (seasonally adjusted, %), percent of firms reporting inflation single most important problem (%)



Source: NFIB

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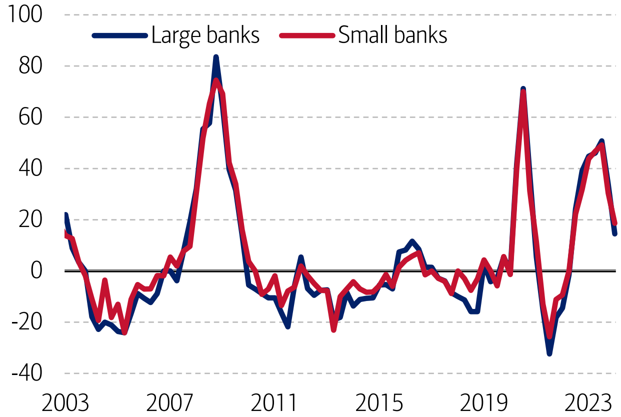
Credit cards as a financing tool

Inflationary pressures also appear to be impacting the way in which small businesses obtain funding and finance their firms. The most recent Federal Reserve Board Senior Loan Officer Opinion Survey (SLOOS) found that the net percentage of surveyed banks that were tightening commercial and industrial (C&I) loans to small firms has eased considerably from the peaks in 2023 Q1, but the current levels are still comparable to prior recession periods (2000 and 2008).

With the SLOOS data suggesting it is more difficult for some small businesses to access a bank loan, they may be turning to alternative sources of funding. For example, according to the latest Biz2Credit Small Business Lending survey, which is based on 1,000 monthly respondents, loan approval rates moderated at big banks, institutional investors (i.e., private equity) and credit unions, whereas approval rates at alternative lenders (i.e., online lending fintech companies) reached the highest level since March 2020.

Exhibit 3: The latest reading of SLOOS data shows tightening standards have eased as of 1Q24

Reported banks tightening commercial and industrial (C&I) loans: large banks vs. small banks (%)



Source: Federal Reserve Board

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Exhibit 4: Small business credit card spending growth has been gradually stabilizing since the second half of 2023

Small business credit card spending per small business client (%YoY, 3-month moving average)

Source: Bank of America internal data

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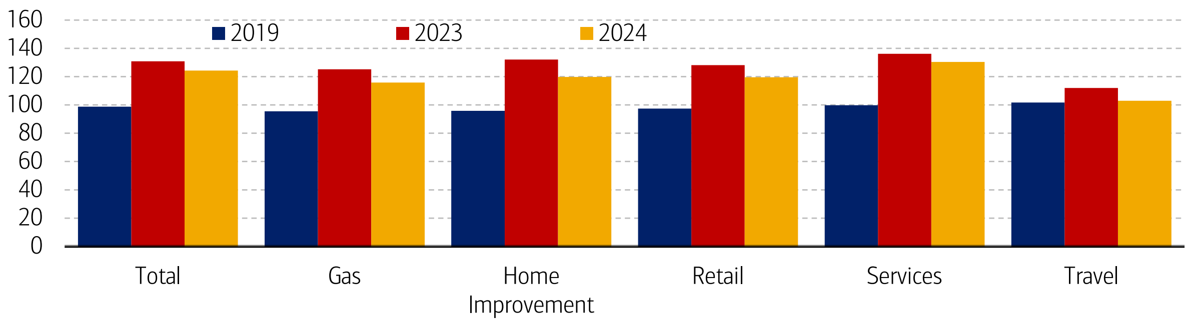
Credit balances are also rising

Alongside alternative financing, small businesses are also making greater use of credit card balances. Bank of America small business data on credit card balances are around 18% higher than 2019 average levels (Exhibit 6). This is despite credit card spending growth being largely flat since mid-2023 and starting to decline slightly on a per small business client basis in March (Exhibit 4). Moreover, an increasing portion of balances are revolving, carrying from one month to the next while accruing interest, after a decline in this behavior during and post-pandemic.

Exhibit 5: Small business credit card spending increased significantly in March 2023, especially on services spending, but has eased in March 2024 across all categories

Small business credit card spending by category (indexed, 2019 = 100)



Source: Bank of America internal data

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While rising credit card balances could raise some concerns, we note a few reasons to be less pessimistic. First, inflation increased over 22% since 2019, as measured by the Consumer Price Index (CPI), so the inflation-adjusted credit card balance is comparable to, or even lower than, 2019 levels. Second, across all categories of small business credit card spending, levels have come down since 2023, suggesting small businesses are taking steps to manage spending and reallocate or optimize cash flow (Exhibit 5).

Finally, the ratio of total bank loans, including credit card loans, and net worth for nonfinancial, noncorporate businesses – most of which are small – remains at historically low levels (Exhibit 7). In our view, the overall balance sheet conditions are therefore relatively healthy for small businesses.

Exhibit 6: Credit card balances are up approximately 18% compared to 2019 average

Credit card balances per small business client (indexed, 2019 average = 100)

Source: Bank of America internal data

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Exhibit 7: Ratio of bank loans to net worth for nonfinancial noncorporate businesses remains low by historical standards

Ratio of bank loans to net worth for nonfinancial noncorporate businesses (%, quarterly data through 4Q 2023)

Source: Federal Reserve

Note: nonfinancial noncorporate businesses include sole proprietorships and limited partnerships, which are mostly small businesses.

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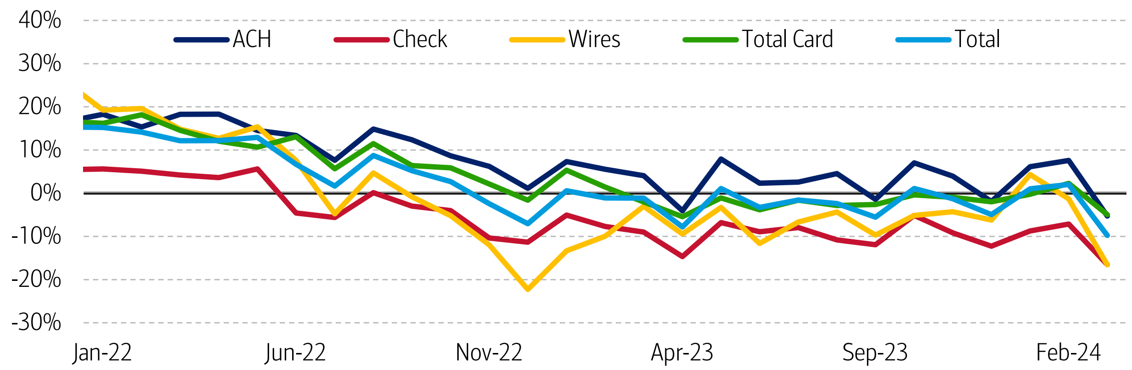
Monthly payments update

Looking more broadly at small business payments in March, according to Bank of America internal data, total payments per small business client fell -9.8% in March (Exhibit 8). Note that the relative weakness in the March reading was largely due to the month ending on a weekend, which pushed the transaction processing for the last day into April.

Among the major components, Automated Clearing House (ACH) payments declined -5.3% YoY in March. The largest decreases %YoY were payments by wires and check.

Exhibit 8: ACH payments growth remains in relatively better shape in comparison to other select channels

Payments per small business client by select channels (%YoY)



Source: Bank of America internal data

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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.

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

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

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.

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

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