BANK OF AMERICA INSTITUTE

BANK OF AMERICA

Small Business Checkpoint

The costs of doing business

16 May 2024

Key takeaways

- In April, the small business account inflow-to-outflow ratio, which we view as a proxy for profit margins, reached a five-year low, according to Bank of America internal data. Although the ratio was still positive, elevated automated clearing house (ACH) payments could point to higher operating costs, presenting a headwind to small businesses' overall profitability.
- Using Bank of America internal data, we find that beyond payroll, ACH transaction payments to financial commitments such as loans has been growing. Additionally, inflationary pressure on services appears to have contributed to elevated payment levels in the form of distributors and property insurance costs, the latter of which is up nearly 35% since 2019.
- Geographically, small businesses feel the pinch from elevated costs differently. In April, ACH payment growth was generally strongest in localities in the South, potentially as a reflection of increased payroll payments growth in line with domestic migration trends.

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.

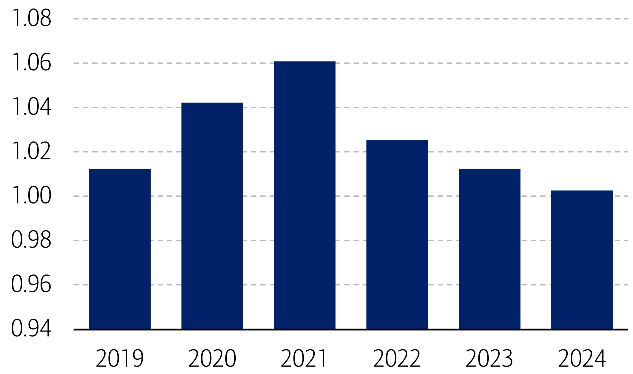
Operational costs are squeezing profit margins

Over the past five years, according to Bank of America internal data, the ratio of small businesses' payment inflows to their outflows, which we view as a proxy for profits, has remained above 1.0 on average during the first four months of the year (Exhibit 1). However, in 2024, this ratio declined to its lowest four-month average in the past five years, highlighting a possible squeeze of small firms' profitability. This may also help explain why small businesses owners may be feeling relatively downbeat (See: April Small Business Checkpoint).

Elevated operational costs are likely a driver behind these squeezed profit margins. Although credit cards can be used as a tool for financing, typically, automated clearing house (ACH) payments capture a broader portion of small business operating expenses, including payroll payments.

Exhibit 1: 2024 first four months' average inflow-to-outflow ratio is the lowest over the past five years

Small business account inflow-to-outflow ratio from January-April by year

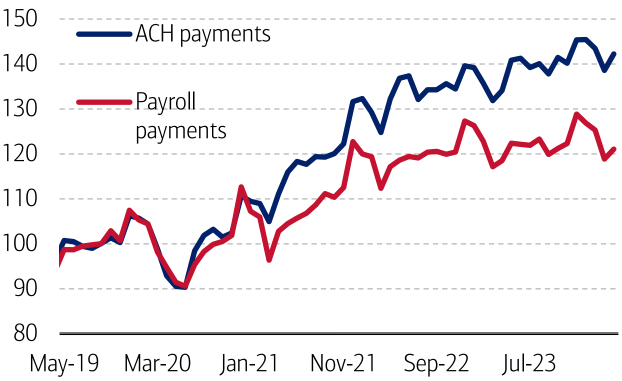


Source: Bank of America internal data

BANK OF AMERICA INSTITUTE

Exhibit 2: Higher payroll and other operating expenses have contributed to increased small business ACH payments

ACH and payroll payment per client (index, 2019 average = 100, 3-month moving average)



Source: Bank of America internal data

BANK OF AMERICA INSTITUTE

While Bank of America internal data has shown a general increase in payroll payment levels, in line with the overall positive hiring reports from the Bureau of Labor Statistics (BLS), we are seeing signs of small business hiring growth coming off its peak (See: March Small Business Checkpoint). But at the same time there has been a continued divergence opening up between ACH and payroll payments per Bank of America internal data (Exhibit 2). This suggests that, beyond the growth in payroll, other expenses are driving up ACH payment levels as well.

Putting the blame on financial obligations and services inflation

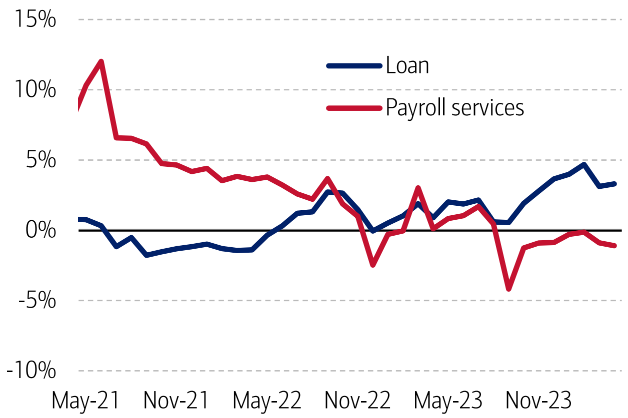
What other expenses are driving up ACH payment levels? Using Bank of America internal data, we find that in addition to payroll and rent, small businesses are facing increased financial pressures. Most notably, there has been a steady rise in ACH payment transactions per small business client towards loans on a three-month moving average whereas payment transactions for payrolls have cooled as hiring has moderated (Exhibit 3). Note that loans are comprised of small business clients making ACH payments to institutions both within and outside of Bank of America.

It's possible one reason for the rise in loan payments lies within the continued "higher for longer" interest rate hikes. Loans for small businesses can be used for many purposes such as financing new equipment or inventory and improving operations. As small firms look to renew or apply for a loan, the current environment makes costs more challenging in the near term compared to 2019.

In addition to financial obligations driving operational costs higher, inflated services costs appear to be putting pressure on small businesses. Along with payroll, ACH payments per small business client to services such as property insurance and distributors are elevated compared to 2019 average levels in April on a three-month moving average (Exhibit 4). Specifically, insurance costs hover around 35% higher than the 2019 average, which may be unsurprising given the cost continues to undergo persistent inflation as measured by the Consumer Price Index (See: May Consumer Checkpoint).

Exhibit 3: The growth in loan ACH transaction counts per small business client could indicate more borrowing and increased financial pressures

ACH payment transactions per small business client by type (year-over-year (YoY), %, 3-month average)

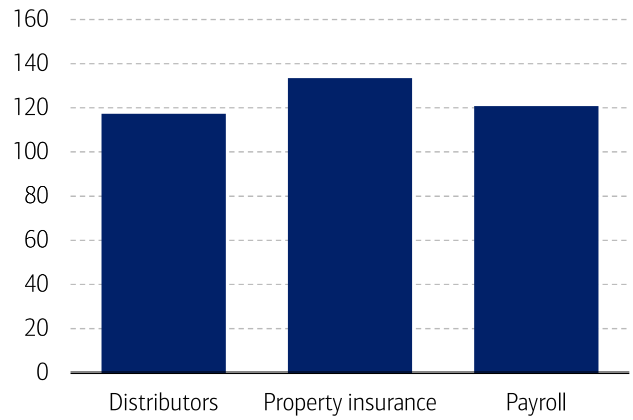


Source: Bank of America internal data

BANK OF AMERICA INSTITUTE

Exhibit 4: In addition to financial operational pressures, payments to services such as distributors and property insurance are elevated compared to 2019 levels

ACH payments per small business client by type as of April (indexed, 2019 average = 100, 3-month average)



Source: Bank of America internal data

BANK OF AMERICA INSTITUTE

Migration patterns might be driving ACH payment growth

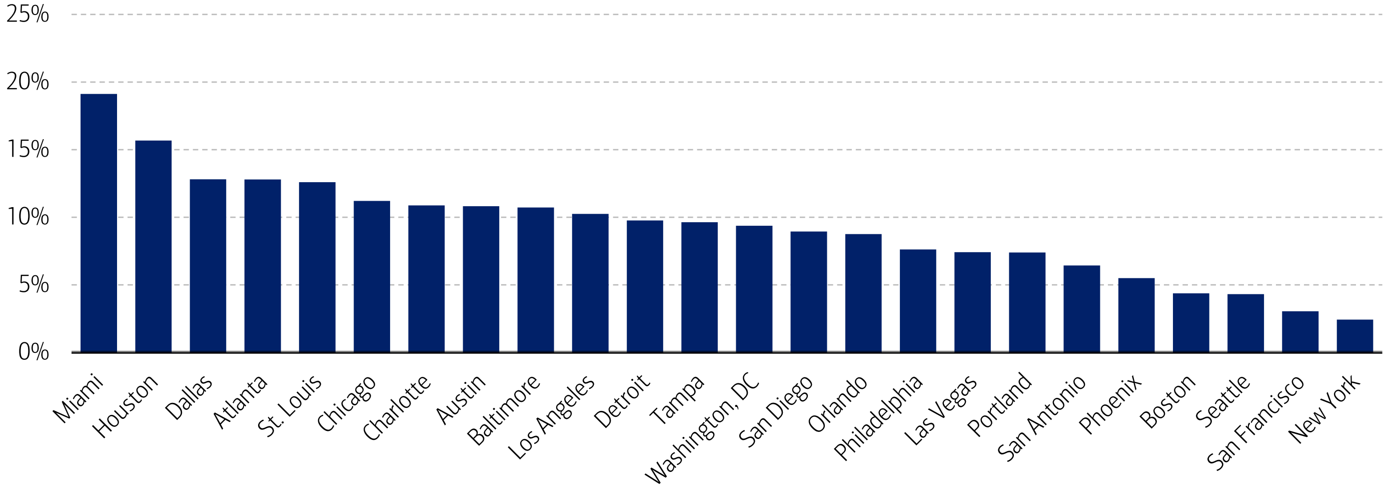
Geographically, small businesses feel the pinch from elevated costs differently. It's important to understand how firms are reacting across the United States as shifting populations can shape a local economy. According to Bank of America internal data, ACH payment growth, on a three-month moving average, has varied in strength across the US as of April (Exhibit 5). Plus, the Bank of America 2024 Business Owner Report (BOR) found that small businesses have increasingly made tradeoffs to maintain their business' profitability, and this too varies amongst localities (Exhibit 6). Such tradeoffs include working more hours, reducing their own salary, and/or reducing marketing costs.

In April, Miami and Houston had the highest ACH payment growth rate of select core-based statistical areas (CBSA), whereas San Francisco and New York had the lowest, albeit still positive, growth rate. It's possible that a component of this growth comes from increased payroll growth as career opportunities contribute to migration trends (See: On the Move: New city, new job, new pay), and the South has seen increased growth in populations relative to the West.

However, while small business profitability has been squeezed so far in 2024, the most recent April findings from the National Federation of Independent Business reported US small business optimism rebounded for the first time this year, driven in part by a six-point improvement in sales expectations. And according to Bank of America's BOR, small business owners do have a sense of optimism surrounding their profitability; the majority of US small business owners expect their revenue to increase over the next 12 months. And when we look at this measure by major local market, cities such as Dallas, Los Angeles, Atlanta, and Houston are most optimistic (Exhibit 7).

Exhibit 5: In April, ACH payment growth was generally strongest in CBSAs in the South, potentially as a reflection of increased payroll growth in line with migration trends

ACH payment growth per small business client by CBSA as of April (%YoY, 3-month average)

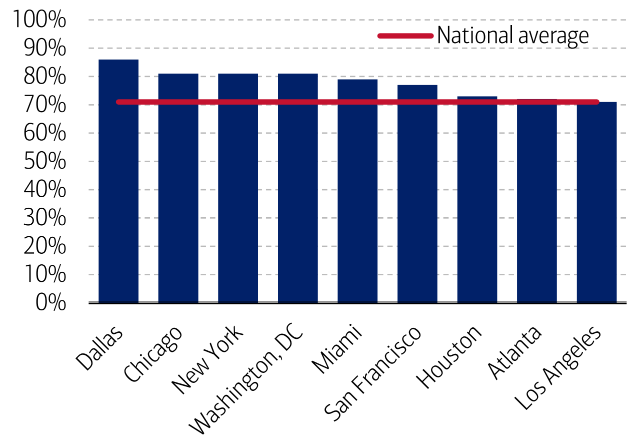


Source: Bank of America internal data

BANK OF AMERICA INSTITUTE

Exhibit 6: All major local markets are either in line with or above the national average of reported small business owners who have made tradeoffs to maintain their business profitability

Percentage of small business owners who have made tradeoffs to maintain their business' profitability (%)

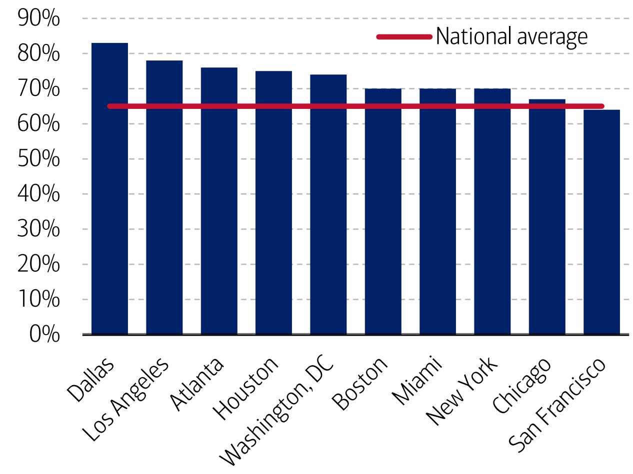


Source: Bank of America 2024 Business Owner Report

BANK OF AMERICA INSTITUTE

Exhibit 7: Dallas and Los Angeles are most expectant regarding their revenue increasing over the coming year

Percentage of small business owners who expect revenue to increase by city (%)



Source: Bank of America 2024 Business Owner Report

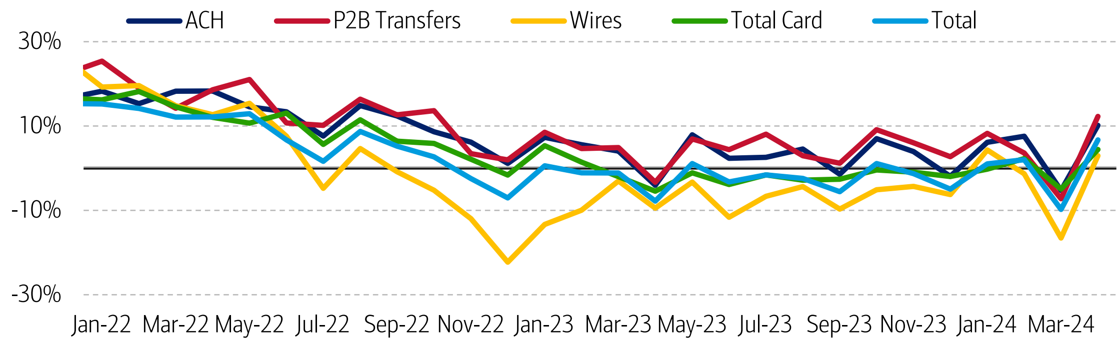
BANK OF AMERICA INSTITUTE

Monthly payments update

Looking more broadly at small business payments in April, according to Bank of America internal data, total payments per small business client increased 6.7% YoY after a -9.8% YoY fall in March (Exhibit 8). As noted in the latest Consumer Checkpoint (See: May Consumer Checkpoint), this year has been impacted by the leap year in February as well as Easter being earlier than in 2023, making for a lot of movement in the data.

Among the major components, ACH payments increased 10.2% YoY in April, and total card rose 4.4% YoY in April.

Exhibit 8: ACH payments growth remains in relatively better shape in comparison to other select channels in April
Payments per small business client by select channels (%YoY)



Source: Bank of America internal data
Note: P2B refers to peer-to-business payments

BANK OF AMERICA INSTITUTE

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.

Ipsos conducted the 2024 Bank of America Business Owner Report survey online between March 4 and March 28, 2024 using a pre-recruited online sample of small business owners. Ipsos contacted a national sample of 1,038 small business owners in the United States with annual revenue between $100,000 and $4,999,999 and employing between two and 99 employees. In addition, approximately 250 small business owners were surveyed in each of ten target markets: Atlanta, Boston, Chicago, Dallas, Houston, Los Angeles, Miami, New York, San Francisco and Washington, D.C. The final results for the national and designated market area segments were weighted to national benchmark standards for size, revenue and region.

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.

Contributors

Taylor Bowley

Economist, Bank of America Institute

Sources

Patrick Williams

Analytics, Modeling, & Insights

Josh Long

Consumer Product Strategy Manager, Consumer and Small Business

Kevin Burdette

Consumer Product Strategy Analyst, Consumer and Small Business

Michael Lutz

Strategy Executive, Small Business, Specialty Lending & Banking

Disclosures