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Small Business Checkpoint

End of year countdown

16 December 2024

Key takeaways

- Small business confidence jumped above the 50-year average for the first time in nearly three years to 101.7, according to the National Federation of Independent Businesses. But perception isn't the whole story, and Bank of America internal deposit account data finds small business profitability has remained in fair shape throughout the year.
- That's not to say there haven't been challenges - small business debt levels are rising alongside a cooling labor market. But credit availability is increasing as are capital expenditures, suggesting some of this rise can be attributed to future expansion and growth. Plus, Bank of America small business payroll growth remains positive and hiring was more than 16% above 2019 levels in November.
- Inflation might pose the greatest risk to small businesses as we head into 2025, given Bank of America internal data shows a higher rate of acceleration in payments towards overall operating expenses compared to their payroll costs. And since shelter inflation has remained particularly sticky, it's likely rent continues to put pressure on 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.

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Small businesses appear to be ending 2024 in reasonable shape, despite having faced a myriad of financial headwinds. We highlight four themes that we think are critical to the health of small businesses as we close out this year and look to the next.

#4 Confidence doesn't tell us everything

The Small Business Optimism Index, published by the National Federation of Independent Business (NFIB), which had remained at low levels throughout most of 2024, jumped above the 50-year average in November to 101.7. This was the highest level since June 2021 (Exhibit 1). NFIB indicated that the election results led to a surge in optimism, as small business owners expect tax and regulation policies that favor strong economic growth.

Exhibit 1: Small business optimism has remained at low levels throughout most of 2024 but jumped significantly in November
Small business optimism index (seasonally adjusted, 1986=100)

Source: NFIB

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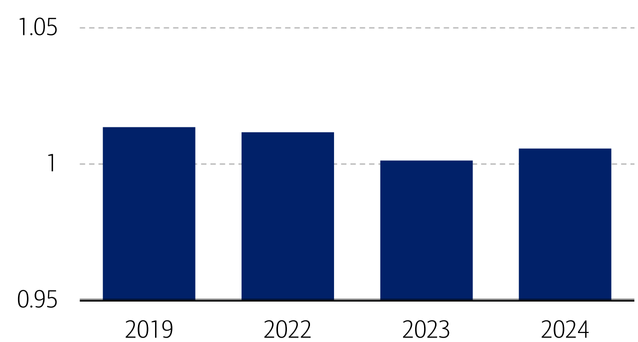
Exhibit 2: For 2024, a ratio of small business profitability has increased compared to last year, though remains below 2019 levels
Small business account inflow-to-outflow ratio (annual average through November of each year) from Bank of America deposit accounts



Source: Bank of America internal data

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But how does confidence translate to profitability? According to Bank of America small business deposit account data, profits in 2024 through November were in better shape than last year, though not quite comparable to 2019 or 2022 (Exhibit 2). However, the differences between years are relatively small, so profitability has remained relatively stable, suggesting that perception isn't the whole story.

We have seen a similar theme amongst consumers, with low confidence but robust spending (see: [November Consumer Checkpoint]). Small business revenue is highly dependent on the state of the consumer, because consumer spending directly translates into profits. And with consumer spending continuing to grow, albeit at a slower pace than last year, and the possibility of economic policy shifting, in our view small business confidence and profitability could continue to trend upwards in 2025.

#3 Debt is rising, but so is investment and credit availability

One reason for low confidence over the past couple of years could be that outstanding debt levels are rising in a historically high interest rate environment, according to the Kansas City Federal Reserve's Small Business Lending Survey. More small businesses appear to have been using credit cards as a source of financing this year, with an increasing portion of balances carrying interest.

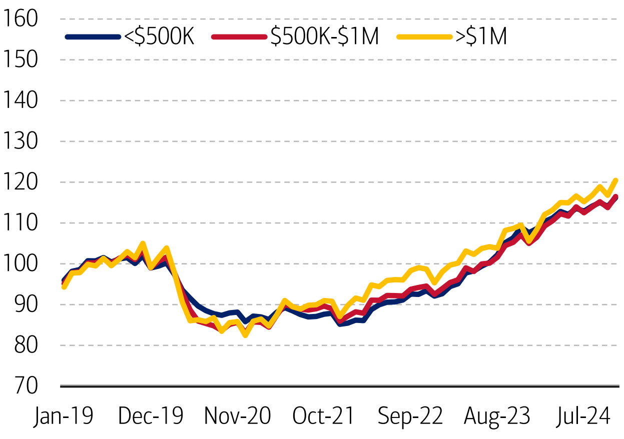
As Exhibit 3 shows, the average Bank of America small business credit card balance rose throughout 2024, and the degree of increase did not vary too much across business revenue tiers. The largest increase was amongst the largest small businesses (annual revenue greater than $1 million), with the average credit card balance as of November 2024 just over 20% higher than its 2019 average. On the flip side, for the smallest firms, those with annual revenue less than $500k, the latest credit card balances were around 16% higher than 2019 levels, per Bank of America aggregated credit card data.

While rising credit card balances could raise some concerns, across all revenue tiers, the rise in balances has stayed below the rate of inflation. Additionally, particularly for those small firms with annual revenue greater than $1 million, spending growth is a strong contributor to this rise as they are often 'transactors' as opposed to 'revolvers' (i.e., pay off their balance each month vs. carrying some or all of their balance over to the next month).

Plus, 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 despite having increased slightly from last year (Exhibit 4). This suggests to us that the overall balance sheet conditions are healthy for small businesses.

Exhibit 3: Average credit card balances have risen generally at the same pace across all revenue tiers, with those small firms with annual revenue greater than $1 million slightly higher

Average small business credit card balance per account by business annual revenue tiers, according to Bank of America card data (monthly, index, 2019 annual average=100 for each respective revenue tier)



Source: Bank of America internal data

Note: Balances are non-seasonally adjusted end of period values

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Exhibit 4: Though increasing slightly since last year, the 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 2Q 2024)

Source: Federal Reserve

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

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Additionally, although there is evidence of small businesses carrying debt, there are also signs of increased expansion. In fact, according to the NFIB, the net percent of small business owners that believe it is a good time to expand their business rose eight points in November – the highest reading since June 2021.

There has also been an uptick in capital investment in recent years. According to BofA Global Research, the first phase was software investment, which accelerated in the early stages of the pandemic and has since slowed (Exhibit 5). Then, there was a surge in structures investment driven by fiscal policy, and now we may be entering the early stages of a pick-up in equipment

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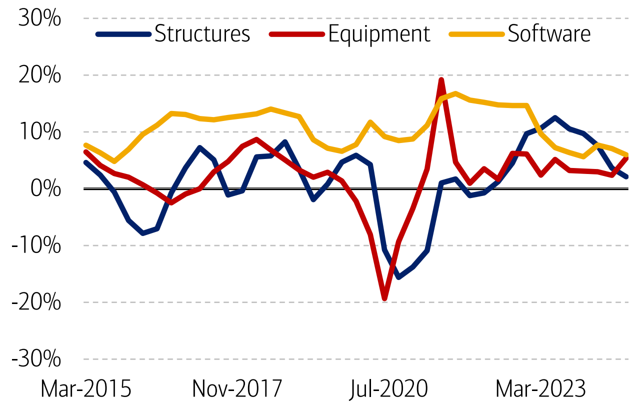
investment. AI could help drive further investment that should eventually help productivity, and investment means businesses are capitalizing on future growth opportunities, which requires funding to do so.

Credit availability has also improved significantly over 2024. 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 peak in Q3 2023 (Exhibit 6). This corresponds to the findings discussed in our October Small Business Checkpoint, with small business owners' demand for traditional loans and lines of credit having increased, while preparing for future expansion into the new year.

Exhibit 5: Growth in nonresidential investment has come in phases starting with software, then structures and now potentially equipment

Nonresidential investment ($2017, %YoY, monthly)



Source: Bureau of Economic Analysis, Haver Analytics BofA Global Research

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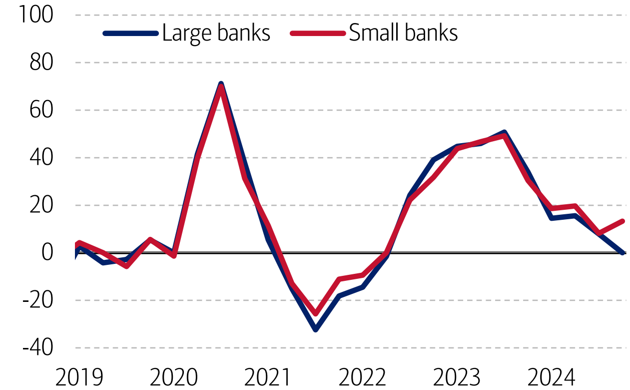
Exhibit 6: The latest reading of SLOOS data shows tightening standards have eased for small firms over the course of the year

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



Source: Federal Reserve

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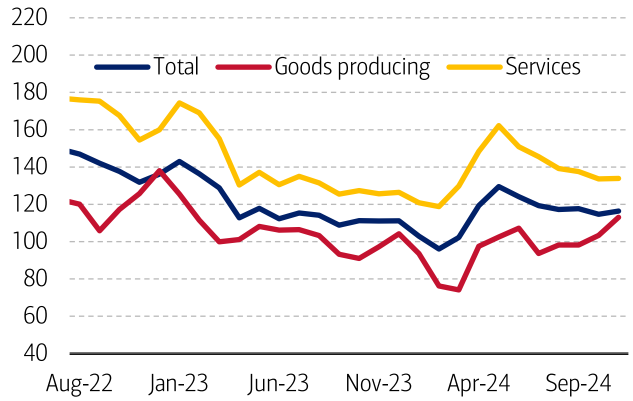
#2 Services are the exception to a moderating labor market

An additional element of business expansion is hiring. Our alternative hiring analysis (see Methodology) has shown that small business payments to hiring firms have moderated steadily through this year and could presage a further slowdown in small firm job openings (Exhibit 7). But overall small business hiring in November still remained more than 16% above 2019 levels.

Plus, payroll payments growth per small business client has remained positive and relatively steady throughout 2024, suggesting continued, albeit soft, labor market strength (Exhibit 8). Why? This has primarily been a services story.

Exhibit 7: Goods hiring saw an increase in hiring payments in November, but services hiring is still stronger

Small business (SB) payments volume to SB-focused hiring firms by industry group through November (index, three-month moving average, 2019 average =100)



Source: Bank of America internal data

Note: Goods producing includes retail and wholesale trade. Services includes all services plus restaurants and financial services firms.

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Exhibit 8: Payroll payment growth was up 3% YoY in November

Payroll payments per small business client (monthly, YoY%, three-month moving average)

Source: Bank of America internal data

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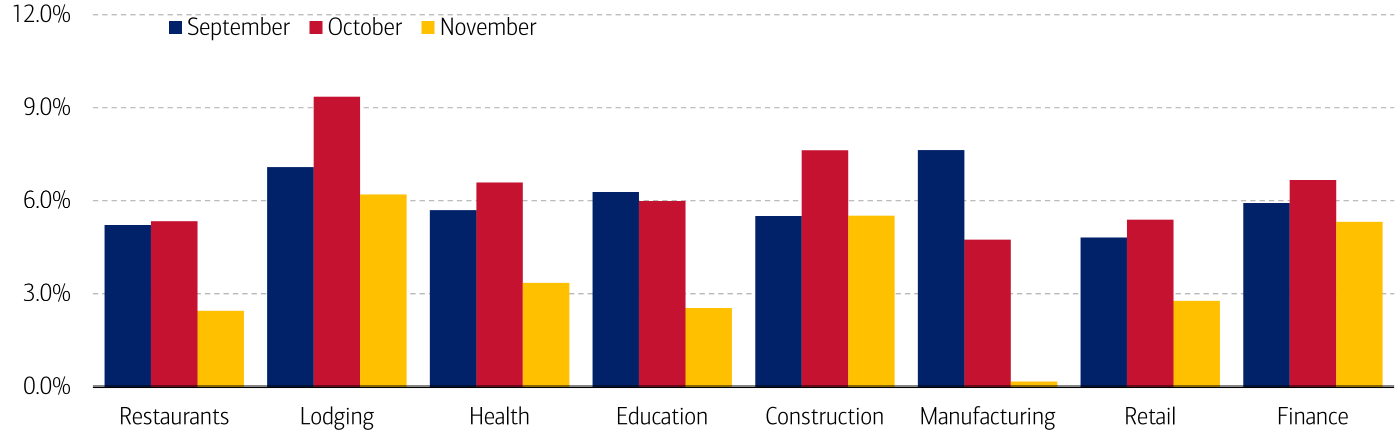
Services' payroll growth continues to show healthy expansion. Bank of America data for small business payrolls is consistent with the Bureau of Labor Statistics reported job gains in November. And when we look by industry, lodging remains the industry with the strongest payroll growth on average over the past three months (Exhibit 9).

In our view, these trends are supported by the fact that overall employment in these industries remains slightly below pre-pandemic levels, suggesting a continued post-pandemic recovery may still be in play. But there are some sectors showing rising strength such as construction and finance. This could be due to rising residential investment from fiscal stimulus (see: Reshoring grows roots in the South and Midwest) and mild recovery in "white-collar" industries (see: Renaissance out West?).

At the same time, consumer spending strength is primarily tied to services and leisure (see: December Consumer Checkpoint), which also supports hiring in these related sectors. Over time, hiring growth may cool if consumer momentum slows further or if labor market turnover cools. But for now, in our view, the outlook remains relatively positive heading into 2025.

Exhibit 9: Lodging, construction and finance sectors saw the greatest payroll payment growth in November
Payroll payments per small business client by industry (monthly, YoY%, three-month moving average)



Source: Bank of America internal data

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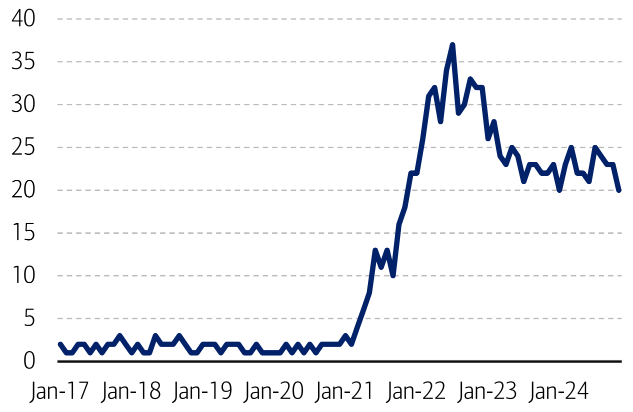
#1 Inflation remains the top concern for small businesses

The greatest challenge for small businesses in 2025 could be found in their greatest concern: inflation, according to the NFIB. Though inflation has come down from last year, it has persistently been a pressure on small businesses' profitability (Exhibit 10).

Typically, Automated Clearing House (ACH) payments capture a significant portion of small business operating expenses, such as payroll payments. Over the year, there has been a continued divergence between ACH and payroll payments in Bank of America internal data (Exhibit 11). This suggests that, despite growth in payroll, other expenses are driving up ACH payment levels as well. Elevated ACH payments could therefore point to inflation impacting particular operating costs.

Exhibit 10: The percentage of small business respondents reporting inflation is the single most important has come down over 2024
Single most important problem: percent reporting inflation (%)



Source: NFIB

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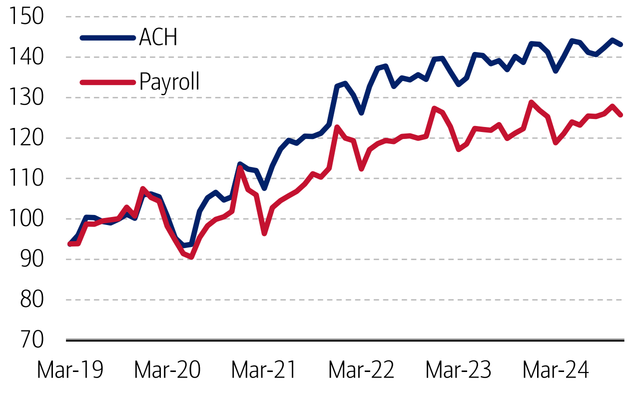
Exhibit 11: A divergence in ACH and payroll payment levels suggests other expenses are driving up operational costs
ACH payments per small business client and payroll payments per small business client (monthly, indexed, 2019 average = 100)



Source: Bank of America internal data

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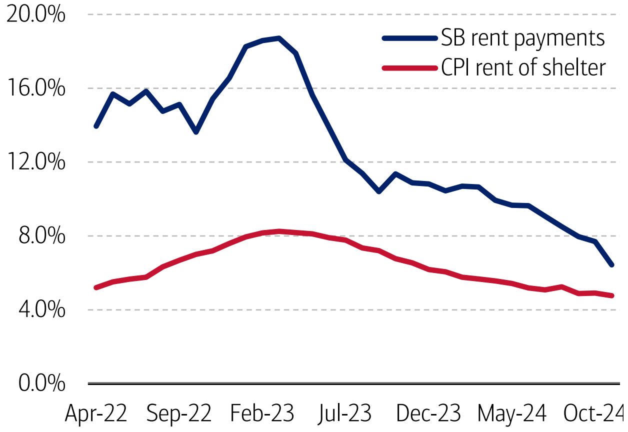
Notably, shelter inflation has remained relatively sticky throughout 2024. Looking at Bank of America internal data on small businesses, focusing on accounts making ACH payments, we find that monthly rent payment growth per small business client was up around 6% YoY in November on a three-month moving average basis (Exhibit 12). This is still above the official Consumer Price Index (CPI) measure but is coming down.

Looking across industries, Bank of America internal data indicates that many industries have declined from peak rent payment growth, per small business client, in line with the overall trend. Yet, for small businesses in the retail sector, there has been a renewed rise in rental payment growth over 2024 and in November; rent grew nearly 18% YoY (Exhibit 13).

Exhibit 12: Small business rent payment growth is down from its peak in early 2023, but is still greater than the CPI measure

Rent payment growth per small business client (three-month moving average, %YoY) and CPI rent of shelter (seasonally adjusted (SA), YoY%)



Source: Bank of America internal data, Bureau of Labor Statistics

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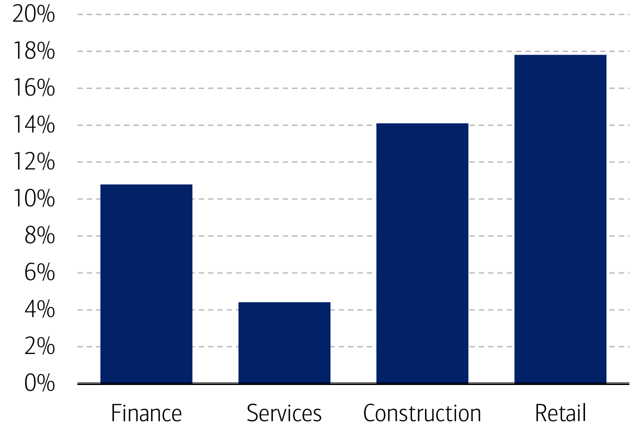
Exhibit 13: Retail sector experienced the strongest rent growth in November, followed by construction

Rent payments per small business client in November by sector (%YoY, three-month moving average)



Source: Bank of America internal data

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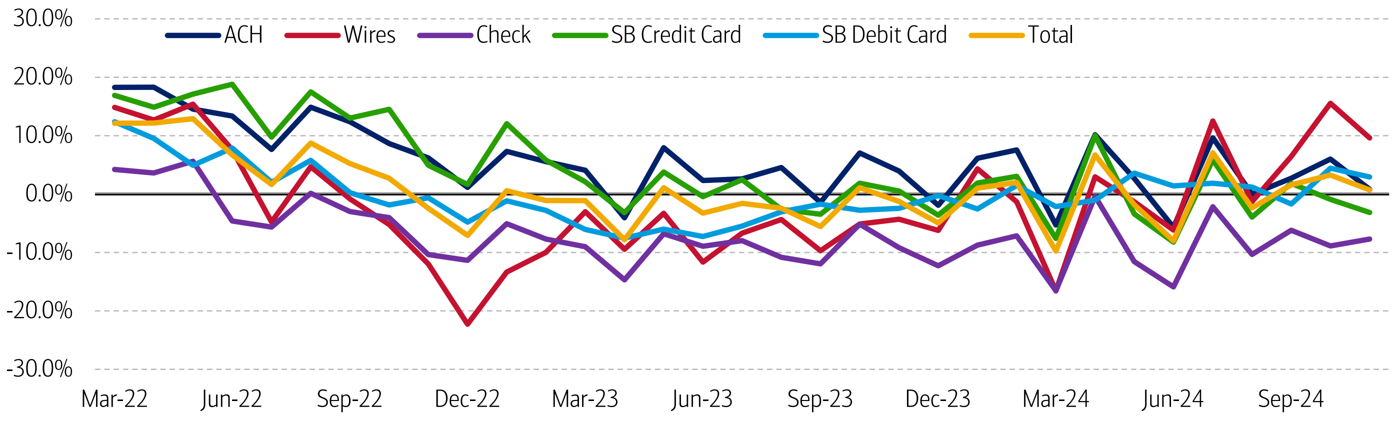
Monthly payments update

Looking more broadly at small business activities in November, total payments per small business client were up 0.7% YoY (Exhibit 14). Among the major components, wires showed the largest increase, up around 10% YoY in November, though down from 16% YoY in October. Conversely, the largest decrease %YoY was by check. Note that for November, there was a calendar-day affect as the month ended on a Saturday.

Exhibit 14: Wires continued to exhibit the strongest growth by channel, and total payments grew 0.7% YoY in November

Payments per small business client by channel (monthly, %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.

Revenue tiers are determined by the combination of following factors: 1) stated revenue on small businesses credit or Paycheck Protection Program applications, 2) actual account inflow into Bank of America Deposit Accounts, and 3) third party revenue estimation.

The alternative hiring indicator consists of payments from Bank of America small business clients to small business-focused hiring firms which 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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Disclosures