STATEMENT
OF

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BEFORE THE
U.S. SENATE COMMITTEE ON SMALL BUSINESS & ENTREPRENEURSHIP

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ROUNDTABLE

ON
"THE STATE OF SMALL BUSINESS LENDING: IDENTIFYING OBSTACLES & EXPLORING SOLUTIONS"

Good afternoon Chairwoman Landrieu, Ranking Member Snowe, Members of the Committee and Committee staff. Thank you for the opportunity to participate in the Committee's roundtable on small business lending today—a crucially important topic for the U.S. recreational marine industry and all the member companies in my association.

Background

My name is Thom Dammrich. I am the President of the National Marine Manufacturers Association (NMMA), the nation's leading recreational marine industry trade association. NMMA represents more than 1,500 member companies involved in every aspect of the boating industry. NMMA members manufacture over 80 percent of recreational boats, engines, trailers, accessories and gear used by boaters and anglers in the United States, and the overwhelming majority of these companies are U.S-based small businesses. The recreational marine industry is a major consumer goods and services industry, generating $30.8 billion in sales and services in 2009 and supporting 353,618 American jobs.[1]

In 2008, there were 5,284 recreational marine manufacturers employing slightly more than 135,900 people and generating $31.3 billion in revenue. There were more than 33,000 retail/service boating businesses, employing 217,718 people in 2008.[2] The U.S. boating industry has for the last three years exported more boats and engines than imported. This positive trade

[1] National Marine Manufacturers Association (2010). 2009 Recreational Boating Statistical Abstract. Chicago, IL.
[2] Ibid.

balance demonstrates both the desirability of our products worldwide and the weakened U.S. economy and credit markets.

The economic downtown, which began for the boating industry in early 2007, has had severe impacts for our industry. In response to weakened economic conditions throughout 2009, the number of new boats sold decreased 19 percent to 572,500 units, with new boat and motor sales declining 24 percent from 2008 for a total of $8.5 billion in 2009. Following declines across most economic indicators in 2009, traditional powerboat sales (inboard, outboard and sterndrive boats) decreased 24 percent in units and 25 percent in retail sales. Wholesale shipments of powerboats and engines had a historic decline of 50.4 percent in 2009 compared to the previous year. The decline in sales for the traditional powerboat market reflected a recession in the U.S. economy throughout 2009, as well as the tightening of credit for consumers and floorplan financing for boat dealers.[3]

Marine Industry is in a Severe Credit Crisis

Disruptions in world capital markets caused by the sub–prime mortgage crisis impacted marine industry beginning in mid-2007. Increases in financial institutions' cost of borrowing flowed to marine dealers and consumers in 2008, as lenders grappled with thinner lending margins. Normal, functioning capital markets began to seize-up in early 2008, causing commercial paper markets to fail to operate effectively, as investors pulled away from lending to all but the most credit worthy organizations. "Normal" borrowing costs for financial institutions for two -year term debt went from Treasuries plus 40-60 bps Treasuries plus 500 to 600 bps. Almost overnight, lenders slowed or in some cases ceased originating new business.

Lenders traditionally active in consumer and dealer financing began to abruptly pull back or exit the marine space. Tight spreads, higher loss rates and concerns about borrowing in the capital markets all were a factor in lenders' exit or pullback decisions. To date, most efforts made by the federal government, including the Troubled Asset Relief Program (TARP), and other liquidity facilities have been ineffective in encouraging increased lending across many lending segments, including in the marine industry.

On the marine dealer side of the equation, in nearly all cases lenders have scaled back lending, dramatically increased interest rates, cracked down on curtailments, and are not issuing new loans or extending current lines of credit to enable marine dealers to finance any new inventory. In some cases that we are aware of, major lenders radically changed loan terms for dealers, resulting in a doubling of interest payment per month, adding a substantial percentage that drove up rates from under 4% to just under 8% on new inventory and over 10% on aged inventory. Certain lenders also added a surcharge to all new boat invoices as a service fee, with the overall effect of making capital too expensive for small dealers.

Although we fully understand that banks and lenders were forced to take dramatic actions of their own during the crisis, the cumulative impact of these aggressive actions by lenders made it

[3] Ibid.

virtually impossible for many dealers to finance current inventory or purchase new model inventory to display. Ultimately, this meant that manufacturers were forced to shut down production by more than 70 percent in our industry, causing a cascade of job losses throughout the U.S. related to our business.

Boat manufacturers are also being hit hard. Manufacturers must “buy back” or repurchase inventory of dealers driven out of business by the yanking of their credit. Although old inventory in the field has largely been depleted by aggressive manufacturer actions over the last two years, the consequence for many manufacturers was dire as much-needed operational capital evaporated in the face of massive marine dealer liquidations. Indeed, it has been reported that already over 1,400 boat dealers have gone out of business. NMMA estimates that more than 50 percent of marine dealers in the United States will have gone out of business by the end of 2010, and the industry has already seen bankruptcies from some of its largest and most storied manufacturing companies as a direct result of the lending crisis. Manufacturers are being required to put up significant cash reserves in order to make any inventory financing arrangements for their dealers. Manufacturers are in an increasing bind – needing cash to buy inputs, build product and fund dealer financing arrangements. This is all now being done in a significantly more restrictive credit environment.

Although other economic conditions, such as loss of demand and low consumer confidence, have certainly impact the ability of our industry to thrive, the credit crisis is the primary reason for the extent of the depression in the boating and similarly-situated industries. As capital became scarce, pressure mounted on dealers and manufacturers alike. Increases in rates and fees, reduced sales levels, tighter lending standards and reduced lender flexibility by lenders has and will continue to result in dealer and manufacturer liquidation unless additional steps are taken to ease credit liquidity pressures on small business. In the main, these pressures have not eased for our industry and for so many small businesses throughout the United States.

It is important to point out that this crisis forced the closure of many otherwise solid marine dealers and manufacturers who could have made it through this rough spot and would have been ready to rebuild their businesses in the recovery if they could keep their hands on reasonable credit. These were not failing businesses or companies with flawed business models—they relied in good faith on lenders for typical business credit, and when the financial markets collapsed, they had nowhere to turn.

Small Business Needs Help Through this Transition

There has been a fundamental shift in the lending environment. In the marine industry, credit for our small business member companies—and particularly for the product dealers of our manufacturers—remains highly constricted. Although major banks and financial institutions have taken to running ads in major news outlets about their increased small business lending, the facts on the ground are quite different. Data from the Federal Reserve indicated that the small business loan portfolios for major Wall Street banks declined by 9 percent between 2008 and

2009.[4] We see no significant evidence that lenders are more willing to lend so far in 2010. Indeed, one of the nation's largest banks recently announced that it was ending all indirect lending for the marine industry and its consumers. Although certainly loan demand, as has been pointed out by others, is an issue, the dealers and manufacturers in the recreational marine industry continue to need reasonably-priced credit to continue operations, purchase inputs and inventory.

The restrictive credit market is also impacting the BP Oil Spill containment and clean up efforts. Marine manufacturers who make the components used to deploy oil booms such as anchors, buoys, and navigation lights have been inundated with requests for product. Manufacturers have received a large volume of calls inquiring on product availability, but without firm orders. U.S. marine manufactures are otherwise ready and able to produce these important oil boom components. However, capital is absolutely necessary to ramp up production. Manufacturers are worried about using up precious cash on hand to build products that may not in the end be purchased. If they take the risk and BP do not turn these product inquiries into firm orders, they will be left holding over five years worth of inventory. In a different credit market perhaps this would be a safer risk. But, with cash being so scarce it is a much more difficult call.

What Congress could do to help the many small businesses in the boating industry, as well as other similarly situated industries, is to facilitate the creation of a new credit market. The exit of lenders over the last two years has convinced me that the boating industry, like many other industries, needs help to transition from relying on just a few large national financing companies to a network of regional and national banks that complement larger lenders and provide some competition.

My statement will focus on the following areas we believe could quickly enhance the small business lending environment.

Enhance SBA Dealer Floorplan Pilot Program

Specifically, boat dealers and manufacturers need help in encouraging regional banks to create or re-establish floorplan lending departments. The industry has overwhelmingly supported the Small Business Administration's (SBA) Dealer Floorplan Financing Pilot Program (DFP), which on July 6, 2009 established a floorplan lending program for boats, motor, and boat trailers.[5] The industry has welcomed this program as a critical lifeline, but problems remain. As NMMA suggested when the program was launched a year ago, it has been difficult to attract a lender to develop a floorplan program when the program is only slated to last a year. A quickly announced extension or a permanent program is necessary to attract new lenders in the floorplan, or inventory, space. The SBA lending program can serve as an important transition, but to date it has failed to attract sufficient participation for national, regional, or local banks, having guaranteed well under 100 dealer inventory loans.

[4] Congressional Oversight Panel. May Oversight Report. May 13, 2010.
[5] SBA Notice and Request for Comments on Dealer Floor Plan Pilot Initiative, 74 Fed. Reg. 32,006 (July 6, 2009).

Additionally, the terms of the SBA program are very conservative and will require boat dealers to make significantly more financial assurances than is typically required. This is going to be difficult for some dealers, but we understand the need to be cautious with government guarantees. It is the industry's view that an 80% loan guarantee with adequate inventory management controls will protect the SBA from incurring unreasonable losses.

NMMA recommends the following actions that, in our view, will enhance the small business lending environment.

1. **The SBA 7(a) Dealer Floorplan Financing Program (DFP) Must be Extended Quickly.** In order to increase participation of banks, SBA should immediately announce the floorplan program as a five-year program. The current one-year program is too short to attract new players and is ending soon Banks will not take on this new line of business because the program timeframe is too short. If the DFP pilot program timeframe is not extended to at least five years, the program is likely to fail to attract new lenders, as is currently the case, which would directly undermine the program's stated goal of getting more diversification of lenders in this floorplan lending space, and more regional/local lenders who have a direct relationship with the borrower. The failure to increase the number and types of lenders engaged in floorplan financing means that large, non-bank financial institutions will continue to dominate the space and exert monopolistic price control. Senators Landrieu and Snowe have recently sent a letter to SBA Administrator Karen Mills requesting this program be extended. We continue to strongly urge the SBA and the Administration to make this change quickly.

2. **Eliminate the restriction on "Less Experienced Floorplan Lenders" in the SBA DFP Program.** As currently drafted, SBA has limited lenders who have less than $15 million in floor plan lines of credit in its current portfolio or that has been making floorplan lines of credit for less than 5 years (so called "Less Experienced Floor Plan Lenders") to making loans only to "customers with which [the lender] has a banking relationship that existed prior to the effective date of this pilot initiative." In addition, these lenders must submit all Dealer Floorplan applications to the Standard 7(a) Processing Center for approval over the life of the pilot." *See* 74 Fed. Reg. at 32,008. The boating industry is faced with the challenge of attracting new lenders while at the same time existing lenders are exiting the boat industry lending business. Because of the reliance on national finance companies, few boat industry dealers have existing relationship with the community and regional banks that typically provide SBA loans. This existing customer provision has made it extremely difficult for such a dealer to find a new lender by severely limiting the available pool of lenders the dealer may choose from. Lenders should be able to market floorplan loans to any willing and qualified customer. The "Less Experience Lender" restriction directly contradicts the goal of diversifying lenders in the floorplan space, unduly restricting participation by banks. There is no justification for this restraint on trade. Plenty of mechanisms to ensure sound lending exist to guarantee banks are not engaging in risky lending to unqualified borrowers.

3. **Temporary Change in Business Size Standards should be Made Permanent.** In addition to making the SBA floor plan program permanent, we also support the changing

of the size standards for all businesses. This is an important change that reflects the marketplace. The traditional standard for marine dealers (receipts of $7 million or less a year) is far too low to include dealers who sell high-cost products, but do so with a small staff. Selling a couple of larger yachts would put many dealers over that limit and yet there is no question they are small businesses. We urge that these temporary size standards be retained permanently. SBA has proposed changing the size standard for a host of retail businesses including boat dealers. Boat dealers under the proposal would see their size standard increase to $14 million. We support increasing the size standard, but noted in our comments to SBA that boat and personal watercraft dealers should have a size standard the same as was proposed for RV dealers ($30 million). Such an increase would also provide flexibility to those dealerships that are selling both products.

4. **Loan Limits should be Increased.** Currently, SBA 7(a) loans are capped at $2 million. This level is not sufficient to provide financing for the majority of small dealers and manufacturers. Typically, in the marine industry one dealer will carry multiple types and lines of boats. It is common for a small boat dealer to have inventory in the $5 million range. In addition, boat manufacturers would need far more than $2 million to build a new manufacturing facility or to purchase specialized equipment. NMMA strongly supports the Committee's legislation in S. 2869 to raise the loan limits from $2M to $5M and urges the quick enactment of this legislation.

5. **DFP Program should be Equitable Among Asset Classes.** SBA is allowing for a higher guarantee level for new autos than other inventory. NMMA appreciates SBA's decision to allow for a 100% advance rate for boats and boat trailers as this allows for current industry practices to be maintained. However, NMMA urges SBA to afford boats and boat trailers the same level of guarantee provided to new autos. Indeed, the mere fact that SBA has treated these inventory types differently has inadvertently sent the message to lenders that marine products are riskier than new auto products. In our discussions with local SBA offices, there is anecdotal evidence that this is serving to restrict the availability of financing for boat dealers. Collateral is collateral and should be treated as such. SBA has provided no rationale for this disparity in treatment of asset classes.

6. **Guarantee should be Increased.** SBA should increase the guarantee to 90% (or higher) for floor plan loans with a 100% advance rate. Floor plan loans need the same incentive provided to other SBA 7(a) loans. Lenders will have to establish whole new lending programs and need incentives to do so. Economist Mark Zandi recently advocated for a guarantee of up to 97.5% in order to grow small business jobs.

NMMA Supports Small Business Lending Fund

NMMA supports the Obama Administration's initiative in the Small Business Lending Fund (SBLF) to provide community banks access to $30 billion in low-cost funds tied to specific plans for small business lending with quarterly reporting. This program, should Congress pass enacting legislation, would incentivize small- and mid-sized banks to increase lending to small businesses by requiring recipients to pay a dividend on their borrowed money and linking the dividend rate to the recipient's lending activity. According to some reports, the dividend rate for participating lenders could drop from 5 percent to as low as 1 percent based on the amount of small business lending they undertake.

NMMA supports the SBLF conceptually but encourages Congress and the Treasury to specifically incentivize floorplan, or inventory, financing as part of the incentive structure from the Fund when it is launched. In order for any new effort to utilize TARP monies to increase small business lending to be truly effective, it should include incentives for lenders to utilize these monies for inventory financing as part of that lending plan—in other words, a more favorable rate could be provided more quickly for participating banks who elect to utilize the TARP fund to engage in floorplan lending. Inventory financing is crucial to all aspects of the distribution chain for a broad, diverse range of industries. If product dealers cannot secure financing to buy inventory, manufacturers cannot produce products. This ensures that no new jobs will be created.

Financial Statement Forgiveness

According to the Congressional Oversight Panel (COP), a major concern in terms of the small business environment is a regulatory climate that makes it difficult for banks to lend. Consistent with numerous reports I have heard from my member companies, the COP reports that "[t]here have been anecdotal reports that bank examiners have become more conservative and have required increasing levels of capital in the last year."[6] According to the COP, there is evidence that banks may have become too conservative as a result from overly aggressive requirements imposed by bank examiners, with the consequent reduction in lending to small businesses.

Although we appreciate the need to prevent overly permissive lending, the fact of the matter is that small business balance sheets are decimated. Congress and the Treasury Department need to work with bank regulators so these companies can get credit to rebuild their balance sheets. Providing small businesses with reduced payment schedules in the first six –twelve months of the loan will assist firms in getting their cash flows stabilized.

Additionally, NMMA recommends temporarily changing the financial statements requirements in some cases to enable new lending. Many lenders are willing to provide loans to manufacturers but are unable to do so because of the enforcement by bank regulators of capital reserve requirements. With the SBA programs, SBA currently looks back two years in reviewing a company's financials. This guarantees minimal lending as company's balance books have been hit hard by the downtown. Bank regulators and SBA should temporarily implement new metrics to determine a company's need and future viability, such as forward-looking trend lines, or a six-month look forward in addition to the two-year look back.

While, many of my comments have focused on the credit environment for our member manufacturer dealer network, we do continue to have concerns about the availability of credit for small manufacturers to fund their operations. SBA 7(a) loans can be a critical life line. However, the use of these loans by manufacturing operations is limited by their size. Raising the cap

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[6] Testimony of Paul Adkins, Member, Congressional Oversight Panel, before the House Financial Services Committee. May 18, 2010.

would also assist manufacturing businesses. In addition, in today's cash poor environment extending the fee relief would especially welcome.

Allow Refinancing of Real Estate & Equipment under SBA 504 Program

The SBA 504 program is a fixed asset program that provides long term financing for real estate or equipment with a minimum 10-year useful life. This program utilizes two loans: a 1st trust issued by a bank or non-bank lender and a 2nd trust issued by a Certified Development Company (CDC). Unfortunately, this program is not currently available for refinancing. The only program where a business can gain an SBA guarantee on a refinance is through the 7(a) program and that is solely available through banks. But, 504 programs offer greater flexibility as they are primarily funded through a CDC.

How does this impact the marine industry? Typical commercial real estate loans are structured with a long term amortization schedule, between 10 and 30 years, with a shorter actual term of three to seven years. In an average economic environment, businesses would refinance the note upon maturity for the remaining amortization. Often they encourage banks to bid for the renewal to gain the best rates and terms. In today's environment, the banks can't justify making the new loan as the value is less than the remaining balance on the note. Unfortunately, this may mean a forced foreclosure based on a bank's unwillingness or inability to refinance the note. Many of these would be refinanced if they could obtain an SBA guarantee. Like many industries, the marine industry—from manufacturers to dealers to marinas—is a commercial real estate-heavy business. Unlocking refinancing through the 504 Program would expand refinancing options for many businesses and help prevent unneeded closures.

NMMA encourages Congress to pass pending legislation that would allow SBA 504 financing to help responsibly refinance good companies with conventional financing that already own their own facilities but have balloon payments coming due, or are saddled with loans with poor loan terms with their banks unable to renew or refinance the loans because of the bank's own financial issues. A refinancing change could help some companies unlock the equity in their buildings and put these funds to use as working capital to help their companies survive and then grow.

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I appreciate the opportunity to participate in this extremely important roundtable today and thank the Committee for holding this event. Like many industries, the U.S. marine industry has been hit extremely hard by the economic downturn and even more so by the meltdown in the credit markets. Already, the marine industry expects to end 2010 with the loss of at least 50 percent of marine dealers—a major disruption to the distribution chain that will having lasting effects. We estimate that nearly 20,000 manufacturing jobs have already vanished and roughly 135,000 jobs related to the marine industry are gone since the onset of this crisis. NMMA urges the Committee to support in every way possible the rehabilitation of the credit markets for the small businesses on Main Street that are the real engine and job-producers of the American economy.