Advancing Innovation and Fairness in Small Business Finance
— A Conversation with Michael Barr

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About

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Panelists

- Michael Barr, Federal Reserve Board of Governors
- Joyce Klein, Senior Director, Business Ownership Initiative, The Aspen Institute

Transcript

Joyce Klein (00:04)

What a great room today. Thank you, everyone, for being here, and welcome to The Aspen Institute. I'm Joyce Klein and I'm the Senior Director of the Business Ownership Initiative at The Aspen Institute, which is part of our Economic Opportunities Program here. It's my pleasure to welcome you to today's event.

This is a special event for us. It represents the 10th anniversary of the founding of the Responsible Business Lending Coalition. Yay! And the Coalition, or the RBLC, as we call it, is our co-sponsor for today's event, and the topic of today's event, Advancing Innovation and Fairness in Small Business Lending, is really what the RBLC's mission is all about. We've always centered our work in ensuring that the market for small business financing is increasingly accessible to small businesses, but is also fair at the same time. And when we think about how to create and shape a market in small business finance, our aim is first and foremost that the primary beneficiaries of that market are the small business owners themselves because really what finance is is but a tool to help businesses to thrive and grow.

So in a minute, you're going to hear from Louis Caditz-Peck, who is the executive director of the Coalition, and he'll give you an overview of our work. But first, I just wanted to share a little bit about the Business Ownership Initiative and our connection to the Responsible Business Lending Coalition.

At The Aspen Institute, we believe in the power of dialogue and action, particularly when it involves cross-sector groups, to identify principles, policies, practices that move us towards a more free, just, and equitable society. And in the work of the Business Ownership Initiative, we really work to expand economic opportunity in the United States through business ownership, and we do that by focusing on the businesses that face the greatest challenges in accessing the capital and the resources that they need, and what are, again, the policies, practices, programs that really can help to meet their needs and help them to grow and thrive? And we have been a proud member of the Coalition since its inception because it's deeply aligned with our mission at the Responsible Business Lending Coalition.

So with that welcome, I'm going to introduce Louis Caditz-Peck, the Executive Director of the RBLC. Louis has been in that role for about a year now, maybe a little more, but he's been part of the RBLC since its inception and a critical part of it. Before stepping into this role, Louis was a practitioner and a policy advocate in FinTech, in banks, in CDFIs, and in nonprofit advocacy organizations. Early in his career, he worked as a commercial lender at Self-Help Credit Union, which is a community development financial institution. He then joined the FinTech company LendingClub where he helped to launch its expansion into small business lending. The financing program that he proposed served more than 10,000 small businesses, and one of the most exciting things they did was create a partnership with Accion Opportunity Fund, one of the nation's largest CDFI small business lenders, and that partnership really leveraged both the strengths of FinTech and of community development financial institutions. And as I said, from its inception, Louis has been, in many ways, kind of the core and the heart and soul of the RBLC, so I'm delighted to welcome him to the stage.

Louis Caditz-Peck (03:47)

Thank you, Joyce. Something unusual has happened. Something got for-profit small business lenders to get together with non-profit advocacy groups and CDFIs and civil rights groups, together with small business groups, to run one organization together, the Responsible Business Lending Coalition. I think it's pretty unusual that we have one board of directors here ranging as broad as Small Business Majority, representing 85,000 small businesses, to for-profit financing companies like Quantum Lending, Camino Financial, FinTech company Bluevine, digital bank LendingClub, to non-profits like Accion Opportunity Fund, the largest non-profit lender to small businesses, and Opportunity Finance Network, the National Association of CDFIs, National Association for Latino Community Asset Builders, representing 400-plus community groups and lenders, and the National Community Reinvestment Coalition, representing over 700 civil rights and community groups.

So, what brought all these organizations together? It was a recognition that we have an unprecedented opportunity to finally close the gap in access to capital for small businesses, and FinTechs and banks and CDFIs are trying, using technology, new ways of creating more and better small business lending. But this group also got together, and maybe with equal urgency, out of a recognition that we are at risk of squandering that opportunity because over the last decade, so much of the investment and energy into small business lending has gone into financing products that are unaffordable with prices that are never disclosed to the borrower that draw on practices from payday lending and pre-crisis subprime mortgage lending that strip wealth out of the borrower businesses instead of helping them create it.

And so we're at a crossroads. We're at a crossroads between what could be creating a more prosperous world of business growth, of economic opportunity, of inclusive prosperity, or watching a new cycle of innovative ways to strip wealth out of those communities. And the Responsible Business Lending Coalition has a strategy to get us to the future that we all want, and that strategy has four parts. It's setting industry standards, changing the market, changing the laws, and in doing so, changing lives.

It started 10 years ago with setting the industry standards, the Small Business Borrower's Bill of Rights. These for-profits and non-profits and small business groups got together because of a recognition that something wasn't quite going right, but we didn't have a way to talk about it together yet with the same language because some folks were saying, "Online lending is predatory and traditional lending is good," and some people were saying, "traditional lending is exclusionary and online lending is good." And so these for-profits and non-profits and small business groups got together and said, "Both of those are wrong. Responsible lending is good and irresponsible lending is bad," and together, they created the Small Business Borrower's Bill of Rights to tell the difference.

This is the first consensus standard that delineates responsible from irresponsible business lending. It's 24 specific practices organized into six rights that we believe all small businesses deserve, like the right to transparent pricing in terms, the right to responsible underwriting, and so on. I'm very honored that Governor Barr is here today and will be speaking to us. Prior to his time at the Federal Reserve, Governor Barr was one of the leaders that gave input to help shape this industry standards document.

The second part of this strategy is to change the market. A hundred organizations have signed on to the Small Business Borrower's Bill of Rights saying, "We stand for this, we follow these standards, and this is the right direction for the market to go." And that's the base for the third part of the strategy, which is changing the laws because it's not enough for the good actors to voluntarily agree to treat businesses fairly. We need the whole market to treat businesses fairly and we need a level playing field so that good actors are not at a competitive disadvantage if they do things like tell their customers what the price is going to be in a transparent way.

And so glad to say that the RBLC together has helped pass and propose eight laws, two federal and six state laws, that are doing exactly that, helping foster innovation for more and better lending and set standards that protect small businesses and good actors in the market. And that is producing the fourth part and the most important part of the strategy, which is changing people's lives. By our analysis, these laws are helping keep billions of dollars in the hands of the small business owners that are creating that wealth instead of seeing that pulled out of communities unnecessarily by lending companies that are overcharging them.

A couple months ago, I was having coffee with the CEO of a trade association representing finance companies that is opposing the work of the Responsible Business Lending Coalition to set industry standards, and this CEO encouraged me to stop trying, actually. And they said to me, this is a true story, they said, "Why do you even care about this so much? It just, it seems like it's personal to you," and it is personal. It's personal to a lot of us because small business ownership is one of the three pathways of economic opportunity in this country, alongside education and homeownership, and each one of those pathways is getting more expensive and more out of reach for people, and small business ownership is the pathway that my family took.

My grandmother grew up in Chicago, really poor. Her dad was an immigrant taxi driver, a single dad. And the way that she tells it, she said that she decided she wasn't going to be poor and she decided she was going to be rich and so she became a small business owner. She started preschools and I grew up working as a handyman and a payroll clerk and a preschool teacher in this family business. And her success as a small business owner is what put me and the rest of my family through college.

And so it is personal. It's personal to all of us that have a connection to a small business and it matters to everyone because if we are going to have a country where people can start a business and build family wealth and make that down payment and send their kids to college, we have got to figure this out, and that is what all of the speakers here today are here to talk about.

And so with that, let's welcome Joyce back to describe how the rest of the day will flow and introduce our speakers to the stage.

Joyce Klein (10:40)

Thanks, Louis. I'm just going to take a few minutes to talk about our agenda and logistics. We had agendas out there. I'm not sure people picked them up, so it's a good thing I'm going to go over this for you.

First, we're going to start... We have three different conversations for you today. First, we're going to start with Governor Michael S. Barr from the Federal Reserve Board, who's going to do some opening remarks and then I'll have a conversation with him about our topic for today. Then we're going to take a quick break and have a second panel that's really going to focus on that opportunity in front of us on how to drive innovation in small business lending. That panel will last about 35 minutes. Then we'll take another just two to five-minute break, reset the stage, and come back for our last conversation, which is really focused on how do we make sure that innovation benefits small businesses? We're not going to do formal bio reads for most of the speakers today. The bios are out there if you want to grab those later if you don't have them.

We do have a virtual audience today, and so a few things about that for those of you who joined us virtually. All attendees are muted. If you do want to ask a question, there is a Q&A function in Evite and you can share your questions or you can upvote other people's questions and we will have a way to filter some of those into the conversation today. We also encourage those of you who are joining virtually to think about using that chat function as a way to share your own perspectives, experiences, resources that you have on this topic with other folks who are joining virtually.

If you have any technical issues while the event is going on, you can either message us in the chat or you can email us at eop.program@aspeninstitute.org because our team is monitoring that email. And then the final thing, just want to let folks know that the event is being recorded and we'll share it later via email and it'll be posted on our website.

So with that, I'm going to introduce our first guest for today, who is Governor Michael S. Barr. He took office as a member of the Board of Governors of the Federal Reserve on January 19th of 2022 for an unexpired term that ends January 31st of 2032, and he served as vice chair for supervision for the board from the time he joined until February 28th of this year.

Prior to his appointment at the board, Mr. Barr was the Joan and Sanford Weill Dean of the Gerald R. Ford School of Public Policy at the University of Michigan. He was also the Frank, you had a lot of nice titles there, Michael, the Frank Murphy Collegiate Professor of Public Policy and the Roy F. and Jean Humphrey Proffitt Professor of Law at the University of Michigan Law School. He was also the founder and faculty director of the University of Michigan's Center on Finance, Law & Policy, and at the law school, he taught financial regulation and international finance and co-founded the International Transactions Clinic and the Detroit Neighborhood Entrepreneurship Program.

Mr. Barr also served as the U.S. Department of Treasury's Assistant Secretary for Financial Institutions in 2009 and 2010, and he also served under President William J. Clinton as the Treasury Secretary's Special Assistant, a deputy assistant Secretary of the Treasury, a special advisor to the president, and as a special advisor and counsel on the Policy Planning Staff at the U.S. Department of State. He also served as a law clerk for U.S. Supreme Court Judge David H. Souter, and also Pierre N. Leval who was with the Southern District of New York.

And finally, Michael has a BA from Yale University and MPhil in international relations from Oxford and a JD from Yale Law School. Governor Barr, welcome.

Michael Barr (14:34)

Thanks very much, Joyce, and thanks to Louis for this just terrific event. Really just honored to be able to be with you here today and see so many familiar faces in the room and to see some new faces as well, which is always part of good coalition building. The work that you all are doing, I think, is really extraordinary. I'm going to give some opening remarks, not too long, I hope, and then look forward to joining Joyce in a conversation.

The United States has a really unmatched entrepreneurial culture and a strong record of building new companies. Yet new and small business owners often navigate significant challenges from establishment to growth. These challenges typically include limitations in accessing capital, in developing robust business and professional networks for peer support and opportunities, and in building the comprehensive skills, resources, and social connections that contribute greatly to business resiliency and sustainability. Women and minority entrepreneurs may face even greater obstacles. While business formation is, of course, primarily a matter for the private sector, public policy can and should encourage increased rates of entrepreneurship and business formation and the capital networks and skills essential for success for all business owners.

Today, I want to highlight the vital role that small business play in driving the U.S. economy, consider the challenges in accessing credit that some small business owners face, and offer some practical solutions to help small businesses thrive.

Small businesses are the heart of the U.S. economy. They produce nearly half of the country's gross domestic product and employ just under half of all private sector workers. Small businesses have created more than 60% of net new jobs since 1995, and business applications have remained consistently elevated at around 5 million annually since mid-2020. In recent years, women-owned businesses and minority-owned businesses were two of the fastest-growing segments of small businesses. The number of small businesses owned by minorities increased by almost 60%, and the growth rate for women-owned businesses was not far behind at 50% during this time period.

We should all be encouraged by these statistics, as several studies suggest that improving business ownership and entrepreneurship across demographic groups would help grow our economy faster, and from an individual perspective, entrepreneurship and small business ownership may offer meaningful economic advantages. Research suggests that entrepreneurship often correlates with enhanced job satisfaction and improved economic mobility for business owners, though outcomes naturally vary based on multiple factors including market conditions, industry, and individual characteristics.

As we recognize the value of small businesses, it's also important to recognize that surviving as a small business is not easy. About one in six new businesses fail during their first year and almost half fail by their fifth year. When a small business struggles or fails, the repercussions often extend beyond the enterprise itself. Entrepreneurs who have invested personal savings and assets in their ventures may face significant financial strain, creating ripple effects that impact their family's stability as well as the broader economic health of their communities. In light of these dynamics, it's essential to understand the fundamental challenges that small businesses face and develop targeted tools and policies that can effectively support entrepreneurs as they start and scale their businesses.

Today, let me focus on credit access and the need for more transparency in lending terms. Many small businesses need credit to launch and grow their businesses. Small businesses access financing from diverse sources, including banks of all sizes, credit unions, online lenders, and other non-bank financial companies. Despite this range of sources, the Federal Reserve Small Business Credit Survey identified credit availability as a challenge faced by over a quarter of small businesses. In addition, many small businesses face problems with the credit that they do obtain.

While access to credit poses challenges for many small businesses, these hurdles can be even more pronounced for women and minority business owners. Research consistently shows that women-owned businesses typically start with smaller amounts of initial capital compared to other firms, even when accounting for factors such as education, experience, credit scores, and business characteristics, such as industry and growth potential. Furthermore, women and minority-owned businesses often encounter distinct obstacles when seeking financing. Minority business owners often have lower credit scores compared to non-minority business owners, which can lead to lower approved rates for terms. Banks, non-banks, and online lenders have the potential to fill these financing needs, but to be effective, they need to understand consumer preferences and behavior to provide credit products that meet these needs in a safe and fair way.

A significant challenge facing small businesses is the absence of policies providing essential tools and protection for small business owners. Despite the fact that many small businesses function more like households than Fortune 500 companies, they generally fall outside regulatory disclosure requirements intended to ensure transparency in pricing, facilitate comparison shopping, and protect the financial interest of borrowers. Consider the Truth in Lending Act implemented in Regulation Z, which does not extend protection to small business owners. This exclusion stems partly from the assumption that small business owners possess financial sophistication or can access professional assistance when needed. This regulatory gap matters because business financing offers may present pricing structures that differ substantially from the standardized disclosures that small business owners may be accustomed to in seeing consumer credit disclosures.

Research from focus groups conducted by the Federal Reserve Board and the Federal Reserve Bank of Cleveland revealed that many small business owners struggle with understanding the specialized terminology used by certain non-bank lenders. For instance, instead of providing familiar metrics like an annualized percentage rate or an interest rate, some non-bank providers present a factor rate, a fundamentally different metric that cannot be directly compared to an APR or interest rate. The research identified a lender's website that advertised a factor rate of 1.15, which translated to an undisclosed estimated APR of approximately 70%. Further complicating matters, some lenders may disclose an interest rate without including an APR, meaning that various fees and additional costs may not be reflected in the stated rate that borrowers often use to evaluate their financing options.

While complexity sometimes serves a business purpose, in many cases, it also may obfuscate the costs and can lead to poor financial decisions by small business owners. More broadly, products designed by banks and non-banks should help to counter, not lean into, biases that can lead to poor financial decision-making. For instance, present bias describes our natural tendency to prioritize immediate benefits over long-term considerations. This might lead business owners to focus more on quick access to funds or low initial payments rather than evaluating the complete long-term cost structure. Similarly, status quo bias suggests that once a small business owner establishes a lending relationship, they may be less inclined to explore alternatives, even when more favorable options become available.

The perceived complexity or uncertainty of refinancing or switching lenders can reinforce this tendency to maintain existing relationships. Understanding psychological factors and cognitive biases can help small business borrowers make more informed financial decisions by recognizing how the presentation of lending terms might affect their evaluation process.

In light of these realities, banks, small business advocates, and industry stakeholders, as well as non-bank providers and community funders, should support policies that help small businesses better understand risks and to drive the market towards products that are designed to overcome and not exacerbate these problems. Potential policies would include enhancing transparency in loan terms, thus enabling business owners to make more informed financial decisions. Additional borrower safeguards worth consideration include ensuring that loan products are sustainably repayable and don't lead businesses into costly re-borrowing cycles, as well as ensuring fair treatment both during the loan origination process and throughout any restructuring efforts or collection proceedings.

Some states are moving forward with policies that protect small businesses. California and New York, for example, now require many lenders to offer clear disclosure of the

APR and estimated monthly payments. This requirement gives borrowers the opportunity to understand the financing being offered in a clear, concise manner, enabling informed comparisons across different product options. Several other states have passed versions of disclosure laws for small business financing transactions with some variability over the range of financing transactions covered and the types of disclosures required.

I want to recognize the importance that community-based programs can play in supporting entrepreneurs. These programs provide accessible tools, technical assistance, and educational resources that help entrepreneurs reach their full potential. Local organizations such as small business development centers, educational institutions, and community development financial institutions are connecting small business owners with personalized consulting, technical assistance, education, and entrepreneurial skills development.

The most successful of these types of programs deliver practical technical assistance and education while fostering collaboration within local entrepreneurial ecosystems. These include university or community college-based initiatives, connecting business owners with volunteer consultants, resources, offering workshops, role development centers, and providing specialized support. By emphasizing both skill building and community connections, these programs help small businesses and entrepreneurs overcome barriers to success.

In conclusion, small businesses are engines of innovation, job creation, and economic mobility in our society. Great work has been done to understand what it takes to help small businesses thrive and grow, including access to sound and affordable credit, skills building, and business networks. I encourage us to build on this work by enhancing financial transparency, implementing supportive policies, and leveraging community-based programs to enhance business opportunities. These collective efforts to support entrepreneurs and small business owners and the like can really benefit individual businesses and can also contribute to a healthy and dynamic economy that works for all of us. Thank you very much.

Joyce Klein (27:00)

It should be on. We don't have-

Michael Barr (27:02)

It should be. Yeah. Okay, good. Well, thank you for those opening remarks and we'll play off of those hopefully a little bit as we have the conversation.

So the place that I wanted to start was by having you talk a little bit about your personal connection to this issue. We first met when you were working in the Clinton administration working for Secretary Rubin, and you were doing work on this topic then, among other things, and I know it's something that we've connected on, but you've been working on throughout your career. So tell us a little bit about the work you've done in this small business and entrepreneurship space.

Michael Barr (27:36)

Thanks, Joyce, and thanks again for having me.

You know, I was thinking as I was listening to Louis's remarks, the image that flooded into my own brain was thinking about being a young boy and going into my grandfather's, my grandfather had a little pharmacy in Bridgeport, Connecticut, and watching him work in this pharmacy and there was an immense pleasure that we had as young children to go and he would give us, this is back in the day when people had cigars, he would give us an empty cigar box and we could fill it with some candy from the pharmacy. And I think that memory has kept with me in the work that I've done in this space for many, many years.

Back in the Clinton administration, when we first met, I was working with Secretary Rubin, and one of the things that we were working on was the growth of the Community Development Financial Institutions Fund and really getting it off the ground and helping it to better serve communities. We were working on strengthening the Community Reinvestment Act, including the role that CRA plays in supporting bank lending to small businesses. And we were working on an initiative to help expand access to capital in economically disadvantaged communities. That became the New Markets Tax Credit, which we were able to get passed at the end of the Clinton administration, and I think has served communities quite well in expanding access to capital over the years.

And one of the things that we did also at that time was not big then, but was very helpful later, we did research. And one of the things we did research on was state-run Capital Access Programs, and we issued a series of reports on these CAP programs around the country, and that ended up being really helpful a number of years later. I went back to Michigan at the end of the Clinton administration. I continued to work as an academic in this space and to do research, among other things, on small business credit.

Well, I went back into the administration under President Obama, and most of the time I was there I was focused on the Dodd-Frank Act, but I also got a chance to think about this question again because in the wake of the Global Financial Crisis, small businesses were having a hard time getting access to credit and the administration tried to figure out what to do, and I said, "Well, we had these reports on state-run Capital Access Programs, they work really well, why don't we fund them?" And that's what became the State Small Business Credit Initiative that I think also has served us well over time.

Then I went back into academics again, and when I returned to Michigan, I really wanted to work much more in communities on these activities. I had been working on it as an academic and as a policymaker. And so I got together with a former student of mine, James Walls at the Kellogg Foundation, and we worked to create, along with a lot of other partners, something that became the Entrepreneurs of Color Fund in Detroit, which was set up to provide much more risky capital to minority entrepreneurs in Detroit proper. And that, I think, has been going really great. Ray Waters runs it, and he's been in this field for many, many decades doing terrific work.

And then at Michigan, we decided that, as I mentioned in my opening remarks, businesses don't only need access to credit, they need access to skills, and they need access to business networks to be successful. We said, "Well, we're at the University of Michigan. What could we do to work on that?"

We set up an interdisciplinary program at the university called the Detroit Neighborhood Entrepreneurs Program. It's a mouthful. We call it DNEP. But the idea of it was, "Let's provide wraparound kinds of support for small businesses." So there's long been business clinics and there have been legal clinics. We said, "What if we just clinic-ed everything and gave students the opportunity to partner with small businesses, not just on legal problems and marketing problems, but maybe also design and physical space and engineering issues and user interface that they were working on or modeling exercise or sales, whatever the business needed?" So we started that program and now it is serving hundreds of businesses in Detroit, it's operated across the university, and I think really has provided some beneficial activities for that purpose.

And now back at the Fed, sorry, not back at the Fed, now at the Fed, my first time at the Fed, I've had a chance to engage in these issues and also in a very different way. So one of the things that we're charged with doing at the Fed is figuring out what is going on in the economy as a whole, and one of the really striking things is the important role that new business formation has played since the pandemic in the excellence of the United States economy. And maybe I'm happy to follow up, but that's a longish answer to your question.

Joyce Klein (33:08)

No, it's a great answer. And some really important things that are still really, programs like SSBCI, they're still really important tools for banks and for community lenders who are trying to get small business credit into the hands of small businesses, so thank you for that. So I'll pick up on this huge growth in business starts, which has been something amazing that we've seen since the pandemic. What's your take on what's happening in the small business credit markets and is that keeping up and how is it keeping up?

Michael Barr (33:38)

Yeah. Well, let me just say, for those of you who are not following this closely, just start with the overall stats. So as I mentioned in my speech, the rate of business formation in the last five years has been very, very high. It jumped up in the pandemic and it has stayed high, over 5 million new businesses a year. And also, the share of that is our businesses that have a high propensity to hire workers has also stayed very high, and that's been great for the U.S. economy, and it's been also great for productivity.

So productivity went up a lot in the last five years. There are lots of reasons for that, but one of those reasons is the new business formation has meant higher-productivity new firms, and more competition with incumbents, which makes them more productive in turn, and that's great for the U.S. economy.

What hasn't been great is credit access. So when you look at the credit access numbers, they've remained muted even though there's much higher business activity, and that's true really across lots of different kinds of lenders. Lending standards have been pretty tight. They're still pretty tight today. They became tight in the pandemic and they stayed pretty tight. And then just to state the obvious, interest rates are still quite high. Interest rates are high because we needed to increase interest rates to combat inflation, which had become quite high. Inflation has now come down quite a bit, so basically on a core basis, cut in half from its height several years ago, and that's fantastic. And the Federal Reserve has been able to cut interest rates by a hundred basis points as a result of that, but interest rates overall are still high for businesses, and that means there's more muted demand.

Joyce Klein (35:37)

One of the trends we've seen as we've looked at what's happening in the small business credit market is the rapid growth in lending outside in the non-bank sector. So among various kinds of commercial finance companies, and even in lending that's embedded in technology companies or companies that provide services to small businesses. And just a little bit of data for the audience, in 2021, merchant cash advance companies provided more than $19 billion in small business financing, FinTechs, about $25 billion in small business financing. The level of merchant cash advance is about six times what small SBA lending is in the non-real estate sector.

So how is that trend affecting and whose lending is affecting small businesses and their ability to access the kind of credit they need to grow?

Michael Barr (36:33)

Well, let me say in general, I think that competition in this space is good. It's good that we have banks of all sizes competing to make small business loans. It's good that there are non-banks of all different kinds of shapes and sizes and variety competing to provide small business loans. It's good that we have government involved in supporting these activities. It's good that there's community development financial institutions, CDFIs, around the country who are specializing in small business lending or partnering between CDFIs and non-bank lenders or banks in providing small business lending. So that competition in general is very good.

I think the thing to watch out for is you want to make sure that the lending that's being done is meeting the credit needs of the small business community, and that means not just providing access to credit, but providing access to credit on terms that make sense for the kind of business that the businesses are trying to run and that are offered in a transparent way so that businesses can make decisions that will be in their long-term interest.

And I mentioned in my opening remarks that it's often the case that small businesses, particularly very small businesses, are run more like a family than they are like a big Fortune 500 company, but our system of thinking about these issues has historically been to think of these businesses as sophisticated players with access to infinite resources, and that's not a small business. Most small businesses can't invest all that they should in the skills that are required to make these good financing choices, and so they need help. And they could have help with better standards, and they can help with community-based organizations offering assistance or university or community college, places offering assistance.

But we should make it easy, not hard, for small businesses to be able to thrive so that if you're a cupcake maker in Detroit, you can focus on making cupcakes and not worrying about whether you have the financing arrangements all locked in.

Joyce Klein (39:00)

Probably your grandfather or Louis's grandmother would've struggled to figure out some of what these products are. So that was a little bit about the micro level and how what's happening in the market is affecting the firms. One of the things that you've focused on at the Federal Reserve is financial stability risks. So I think about, do you have concerns about what happens when we see the growth in financing for small businesses outside of the traditional bank regulatory system and structure?

Michael Barr (39:31)

Look, in general, I'm somebody who worries all the time about everything, so I don't have a particular worry that we're in a bad space right now in that world. Historically, we haven't seen the cycles of financial instability arise from that type of market, but the thing I do worry about is that if we don't get the financial stability of the system right overall, that you can have a pullback on small business lending and then that harms the economy.

So it's really important that we have strong capital in the banking system, for example, so that lenders can lend throughout the economic cycle and not have a credit crunch when there's a problem. So it's in the long-term interests of small business owners for there to be a sound financial system that they can rely on and trust throughout the economic cycle.

Joyce Klein (40:29)

So the last thing I want to ask you about is one of the Fed's goals is to create a safe, sound, and efficient financial system. You also have key goals around consumer protection and around community development. So is there a set of principles or way you would think about what we should be doing in the small business lending market that get us to that goal of efficiency and credit allocation, but also making sure about consumer protection and who's getting access?

Michael Barr (41:02)

I think when this is done right, these goals all align. So if you have a financial system that is working efficiently and fairly, then consumers are protected and you've got a growing economy. It's when you let those goals get in conflict that you get into trouble.

I've often said, and I'll say it again here, for example, fair lending is safe and sound lending. That's what we mean by saying fair lending is safe and sound lending. And so if you put the country in a situation where small business owners, for example, are taken advantage of and are not getting the products and services that they need, that's bad for the individual small business owner, it's bad for safety and soundness, and it's bad for the economic growth of our country. So we've got to get all these things lined up in the same direction.

Joyce Klein (42:02)

Thank you so much for being with us today. Really appreciate it.
I forgot to mention that you were with us when we first announced the Responsible Business Lending Coalition, so it's a particular honor that you're back with us today at our 10-year anniversary. Thank you.

Michael Barr (42:17)

Great to be back.