

The Impact of COVID-19 on Communities and Small Businesses

Federal Reserve Connecting Communities
(a webinar hosted by the Federal Reserve System)

July 14, 2020

Patrick T. Harker

President and Chief Executive Officer
Federal Reserve Bank of Philadelphia



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Hello, everybody, and thank you to Matuschka for that introduction. This is a very important discussion, and I'm thrilled to be joined by so many of you.

But before we begin that very important discussion, I need to give you my standard Fed disclaimer: The views I express today are my own and do not necessarily reflect those of anyone else on the Federal Open Market Committee or in the Federal Reserve System.

Small Businesses in the Economy and Our Communities

In one sense, it's gratifying that there is so much interest in the Fed's COVID-19 Community Impact Survey and the economic effects of the virus more generally.

But the strong turnout today is also evidence that months after the coronavirus arrived on our shores and shut down vast swaths of the economy, we remain mired in a crisis the likes of which none of us has ever experienced.

Indeed, even as the economy is reopening in fits and starts, the pandemic's effects are proving not to be just a brief setback. We are in a downturn that is both exceptionally painful and stubbornly long-lasting.

Among those most affected by this crisis have been those small businesses across the country that are the lifeblood of our economy — and of so many of our own communities.

Small businesses define the landscape of our cities and towns. Small business owners and their employees are our neighbors, our friends, and oftentimes our family members. They're our plumbers, our grocers, and our barbers. (Though during the COVID-19 shutdown, some of us have become amateur barbers ourselves.)

Small businesses also define our economic landscape. The United States certainly boasts more than its fair share of corporate titans — American companies make up for more than a fifth of the Fortune Global 500 — but small businesses are integral to our economy and to the functioning of the labor force.

According to the Small Business Administration, as of 2018, there were more than 30 million American small businesses, employing nearly 60 million people. That means that nearly half of the country's private workforce is employed by small businesses. Small businesses are also an engine for building a more racially equitable economy: More than 8 million small businesses are owned by racial minorities.

Among small businesses, microenterprises — those employing fewer than five people — predominate. Nationally, some 59 percent of businesses are microenterprises. Here in the Third District, we are particularly sensitive to the concerns of these vital businesses.

In the City of Philadelphia, fully 99.5 percent of businesses are small businesses, meaning they employ fewer than 500 people. And of those, 54 percent employ fewer than five.

Small Business and the Pandemic

When the COVID-19 crisis hit, the economy was in quite good shape. But even then, many of our small businesses, especially those helmed by racial and ethnic minorities, faced a precarious existence.

According to Fed research, at the end of 2019, smaller firms, younger firms, and firms owned by Blacks or Latinos were more likely to be classified as “at risk” or “distressed” than other businesses.

And even those firms deemed financially healthy were often on a knife's edge. Late last year, the Fed found that only 1 in 5 healthy small businesses — and of course, far fewer less-healthy firms — had sufficient cash reserves to continue normal operations if they experienced a two-month revenue loss. A majority of small businesses of any level of health would be likely to reduce their workforce and operations, or delay payments, we found. Many firms would rely on personal funds or debt to bridge the gap.

And some said they would try to sell or close their businesses altogether.

So while it's tragic news, it ultimately isn't surprising that small businesses owned by minorities have been disproportionately affected by the COVID-19 crisis.

When we think about the challenges these businesses have historically faced as a result of the racial wealth gap, it becomes more understandable why minority-owned businesses are in the most

precarious financial situations. Just recently, the National Bureau of Economic Research found that the number of Black-owned small businesses nationwide has collapsed by a stunning 41 percent since the onset of the coronavirus crisis.

And at the Philadelphia Fed, our research has found that the disproportionate impact does not just fall on minorities who own small businesses, but among those who work for them as well.

Those who have lost jobs within small businesses because of the COVID-19 pandemic have been disproportionately young, disproportionately less educated, and are more likely to be a member of a racial or ethnic minority. Compounding the tragedy is the fact that racial minorities have also been disproportionately affected by the disease itself, with Blacks and Latinos in particular suffering from higher death rates than other groups.

Small Business and Banking

Back in March, Congress passed the CARES Act, which included the Paycheck Protection Program, or PPP. PPP was designed so that small businesses could obtain largely forgivable loans if they kept workers on their payroll through the crisis.

There is no doubt that PPP was an immense help to millions of businesses and that the employment crisis would be far worse without it. PPP has proven to be something of a blunt instrument, however. Fed researchers have found, for instance, no direct correlation between the disbursement of PPP loans and the level of infection in a given area. The State of Nebraska, for example, which has been left relatively unscathed by the coronavirus, has a far higher rate of small businesses receiving PPP loans than those in hard-hit New York, New Jersey, and Pennsylvania.

I think a big part of the problem is that the distribution of PPP loans was predicated on having existing banking relationships. Basically, small businesses went to the bank they had borrowed from before in order to get a PPP loan.

The trouble is that many small businesses, especially those microenterprises we've been talking about, don't have those established banking relationships — many have never banked at all. And so, when PPP loans became available, these business owners had no ability to access them. This is a problem that has disproportionately affected racial minorities and communities of color.

There are many historical and structural reasons why so many of our microenterprises remain unbanked. But that doesn't mean that this is a status quo we have to accept. This is why we launched a

series on equity in recovery: identifying those who are most at risk and putting them at the center of our work.

Across the System, something we should all be thinking about is this: How do we solve this problem? What are the existing impediments to those microenterprises having access to the banking system? How can we harness our country's CDFIs, large banks and community banks, and even microloan financiers and other financial institutions to serve our under-resourced communities and entrepreneurs?

This isn't just a problem to be diagnosed — it's one to work together to solve.

I've said many times that I refuse to call this current period of crisis "the new normal." None of this is normal. But that doesn't mean that when the COVID-19 pandemic passes that we are destined to go back to the old normal. Together, we can chart our way to a "better normal" — and discussions like these are going to be a part of that important task.

Thank you, again, and now I'm happy to take some questions.