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Chairman Risch, Ranking Member Cardin, and Members of the Committee, On behalf of our Chairman and Chief Executive Officer, Joseph Haskins, Jr., thank you for inviting The Harbor Bank of Maryland to testify at today's field hearing. My name is John Lewis and I serve as the Executive Vice President and Chief Administrative Officer of The Harbor Bank of Maryland.

The Harbor Bank of Maryland

Founded in 1982, The Harbor Bank of Maryland is a Maryland Chartered Commercial Bank headquartered in Baltimore, Maryland. The Harbor Bank of Maryland is one of few remaining Baltimore-based community banks and was founded, in part, to make capital available to creditworthy borrowers who were otherwise unable to access bank capital. Our portfolio has always been reflective of Baltimore and all of its communities. A point of pride and distinction is that we have been recognized an unprecedented twelve times by the United States Treasury with the Bank Enterprise Award for demonstrating increased lending, investment, and service activities in distressed communities within our footprint.¹ The Harbor Bank of Maryland is a US Treasury Certified Community Development Financial Institution ("CDFI"), a designation which requires greater than 60% of our loans to be made in low-income communities. Our designation also lists our CDFI target populations as low-income areas of Greater Baltimore and African-Americans. The Harbor Bank of Maryland continues to work with the US Small Business Administration as a 7(a) lender, two time awardee under the Program for Investment in Microentrepreneurs ("PRIME"), and Baltimore Co-Chair of the Partnership for Lending in Underserved Markets ("PLUM") along with the US Small Business Administration and the Milken Institute.

Since its founding, The Harbor Bank of Maryland and its affiliates have been innovative in providing capital access, advice, and financial services to underserved areas throughout its regional footprint of Maryland, Washington, D.C., and Northern Virginia. Its subsidiary, Harbor Financial Services, is the first community bank-owned investment subsidiary. Its holding company, Harbor Bankshares Corporation ("Harbor"), expanded the organization's ability to provide gap capital by winning competitive New Markets Tax Credit awards seven times for a total allocation of \$299 million. These awards have created over 4,000 jobs and attracted over \$2 billion in investment into local projects, which, by definition, would not have happened but for Harbor's investment. The provision of capital has continued with the growth of Harbor's mission-based non-profit affiliate, The Harbor Bank of Maryland Community Development Corporation, also a US Treasury designated CDFI. This affiliate provides gap capital in forms which range from patient debt capital to equity. Its innovations include the formation of an EB-5 Immigrant Investor Program Regional Center and the creation of the Minority Business Pre-seed Venture Capital Fund. It also has dedicated technical assistance and acceleration programs for small businesses, neighborhood community development corporations, non-profits, and small real estate developers. These

¹ BEA Distressed Communities are defined as those where at least 30 percent of residents have incomes that are less than the national poverty level and where the unemployment rate is at least 1.5 times the national unemployment rate.

programs are all housed at the Joseph Haskins, Jr. Center for Community and Economic Development, a 6,000 SF co-working space located at The Harbor Bank of Maryland's Baltimore, Maryland, headquarters. Harbor expects to continue its innovations in providing capital to underserved markets with its platform for Opportunity Funds, which were created by the Tax Cuts and Jobs Act of 2017.

The Capital Gap for Minority-Owned Small Businesses

In September 2016, The Harbor Bank of Maryland began a two-year pilot program, The Partnership for Lending in Underserved Markets, co-chairing the initiative with the US Small Business Administration and the Milken Institute. I request that the two white papers produced by the initiative ("Phase I Summary: Developing Action-Oriented Solutions to the Financing Challenges Facing Minority-Owned Small Businesses" and "Phase II: Summary Lessons Learned for Advancing Minority Small Business Capital Access") be added to the record.

Data shows a persistent gap in the percentage minority small employer firms and their employees relative to percentages of the U.S. Population. In 2012 Blacks comprised 13.1% of the population and only 2.1% of small employer firms and 1.9% of employees. Hispanics comprised 16.9% of the population and only 5.6% of small employer firms and 4.5% of employees.² Conversely, non-minorities comprised 62.9% of the population and 80.9% of small employer firms and 84.6% of employees.³ This under-indexing of minority business ownership and employment is relevant to our discussion of the capital gap for two primary reasons. First, community wealth disparities lead to major disparities in access to critical early-stage equity that can be leveraged to grow businesses and share risk. A Stanford Institute for Policy and Economic Research Study on Access to Capital for Minority-Owned Startups calculated the average outside equity of a black-owned business to be \$500 at founding as compared to \$18,500 for a white-owned business.⁴ Another reflection of the disparity in access to outside equity is the fact that the median net worth of black business owners is (most likely by necessity) twelve times that of black non-business owners.⁵ The second reason why the under-indexing of minority businesses is relevant is because it is reflective of the disparity in the flows of capital and resources to minority entrepreneurs to successfully grow their businesses. Across the capital spectrum, minorities show relatively smaller levels of capital access. For example, 1% of venture capital dollars go to African Americans, as compared to 87% going to non-minorities.⁶ 2.5% of US Small Business Administration 7(a) approvals went to African Americans and 67.9% went to non-minorities.⁷

² Small businesses employ half of the country's private sector workforce and have created approximately 60 percent of net new jobs since 1995.

³ Karo, Carolyn, "Phase I Summary: Developing Action Oriented Solutions to the Financing Challenges Facing Minority-Owned Small Businesses" Partnership for Lending in Urban Markets. Milken Institute, September 2017.

⁴ Fairlie, Robert, "Black and White: Access to Capital among Minority-Owned Startups" Stanford Institute for Economic Policy Research, 15 December 2016

⁵ Gorman, Ingrid, "The Tapestry of Black Business Ownership in America: Untapped Opportunities for Success" Association for Enterprise Opportunity, 16 February 2017.

⁶ American Sustainable Business Council, Fact Sheet: *Closing the Funding and Opportunity Gaps for women and Minority-Owned Businesses* (2015)

⁷ Dilger, Robert, Congressional Research Service, Small Business Administration 7(a) Loan Guarantee Program, 27 June 2018

These factors affect the ultimate growth and success of minority businesses. A recent research report showed 28.4% of Black business owners responding reported that the lack of access to capital negatively impacted their profits, as compared to 10.1% of white respondents. It also showed 22.6% of Black business owners responding reported that the cost of capital negatively impacted their profits, as compared to 10.6% of white respondents.⁸ Undercapitalization is also a leading cause of business failure.⁹

Recommendations for Improving Access to Capital for Minority-Owned Small Businesses

The Partnership for Lending in Underserved Markets generated the following key considerations for increasing capital access:

1. “A committed local partner, who knows the market and its players well, is essential to advancing any capital access solution”¹⁰

The Harbor Bank of Maryland reintroduced SBA 7(a) lending in calendar year 2017 and is currently on track to close ten deals totaling approximately \$5 million (with deal sizes ranging from \$100,000 to \$1,500,000). Over 85% of those loans are to minority-led companies based in Baltimore. Even with this measured reentry (we have spent \$0 on advertising to date), Harbor will close the year as one of the most active lenders in the market by number of deals. Community banks are essential to small business capital access solutions; small banks lend to small businesses. Expert knowledge of local market (and sub market) conditions allows banks to properly assess risk and provide capital where other banks may be challenged.

2. “Minority businesses benefit from targeted networks that prioritize their needs”¹¹

In minority communities, providing access to capital often means confronting two challenges. The first challenge is having the capital (in the right form) to provide to businesses. Debt is the wrong form of capital for many businesses with significant operating risk in underserved communities. The second challenge is preparing the businesses for capital. The SBA’s offerings through SCORE and similar technical assistance programs are key to meeting the specific needs of minority businesses. Minority businesses, just like start-ups in Silicon Valley, often need supplements to their human capital. The Harbor Bank of Maryland provides technical assistance through its various programs and co-working space. Those programs were greatly aided by the receipt of operating grant funding through the SBA’s Program for Investment in Microentrepreneurs (“PRIME”), allowing Harbor to impact hundreds of local small businesses.

⁸ Robb, Alicia, “Startup Financing Trends by Race: How Access to Capital Impacts Profitability” Annual Survey of Entrepreneurs Data Briefing Series. Ewing Marion Kauffman Foundation, October 2016.

⁹ “Venture Capital Demographics,” CB Insights, *available at* <https://www.cbinsights.com/blog/venture-capital-demographics-87-percent-vc-backed-founders-white-asian-teams-raise-largest-funding/>

¹⁰ Karo, Carolyn, “Phase II Summary: Lessons Learned for Advancing Minority Small Business Capital Access” Partnership for Lending in Urban Markets. Milken Institute, May 2018.

¹¹ Ibid.

3. “The lack of understanding and recognition of cultural factors is a major barrier to capital access for Black and Hispanic entrepreneurs and small business owners”¹²

The Harbor Bank of Maryland is one of 21 remaining African American Minority Depository Institutions (“MDIs”). MDIs are designated by the Federal Deposit Insurance Corporation (“FDIC”). These institutions have a long history of providing private capital and advice to minority businesses. According to a recent study, MDI branches are located in census tracts with an average of 74% minority population, as compared to 28% for all FDIC insured depository institutions.¹³ Our 80 employees are part of the fabric of this community, with the depth of access that comes from being born, schooled, churched, and accepted by its members. In fact, our Chairman and CEO, Joseph Haskins, Jr. is a graduate of this fine University, Morgan State University, where we are gathered today. A study by AEO cites three gaps which must be addressed to overcome access to capital issues: wealth gap, credit gap, and trust gap.¹⁴ Earning the trust of minority communities takes the demonstration of enduring commitment to their success, health, and inclusion. It is the one area in finance where past performance may be indicative of future results.

4. “There are policy solutions to minority barriers to capital access . . . relationships and partnerships with policy champions can be the difference between good ideas and executed outcomes”¹⁵

There are many aspects of capital access that work; however, many of these areas are continually challenged. The CDFI Fund and its programs (Bank Enterprise Award, New Markets Tax Credits, Bond Guarantee Fund, Financial Assistance/Technical Assistance Awards) work. SBA programs fostering small dollar lending and waiving fees work. The Program for Investment in Microentrepreneurs works. Their continued support by policy champions is essential. Harbor Bankshares Corporation also believes that the Opportunity Zones created by the Tax Cuts and Jobs Act of 2017 will bring catalytic market-based capital to low income communities and small businesses. While there is significant discussion around “guardrails” to somehow manage the distribution of market-based capital, our experience informs us that similar to the challenges of capital access in other capital markets, the solution to ensuring the funds get to minority small businesses is a matter of ensuring the proper intermediaries have access to opportunity fund capital. Accordingly, sound policy would make certified minority depository institutions eligible opportunity fund investments, by rights. A recent study on the MDI industry demonstrates that MDIs have the highest median percentage of small business loans to total assets (as compared to all financial institutions), but have the lowest median capital-to-asset ratio.¹⁶

¹² Ibid.

¹³ Barth, James “Minority-Owned Depository Institutions: A Market Overview” Access to Capital. Milken Institute, July 2018.

¹⁴ Gorman, 26.

¹⁵ Karo, vi.

¹⁶ Barth, 29.

5. Data challenges may yield information that is insufficiently localized to be instructive. Moreover, “there is little demographic data on groups such as women and minority small business owners and their ability to access capital”¹⁷. “Supplementing the information with community insights and local knowledge and expertise will further facilitate identifying gaps and opportunities for minority business owners.”¹⁸

Most of the organizations providing loans and investments to minority small businesses do not have research arms. They are subject to different reporting requirements than are large lenders, and they spend their time looking for opportunities, underwriting them, writing checks, and managing their portfolios. Much better efforts need to be made at getting their side of the story, both quantitatively and qualitatively. Across the country (and Baltimore is no exception), entire communities had their stories told by others for generations. It is no coincidence that these same communities have also been neglected by capital markets for generations.

I am pleased to continue this dialog with this committee to help form additional policies that support strengthening access to capital for minority-owned small businesses. Thank you for the opportunity.

¹⁷ The State of Small Business Lending: Innovation and Technology and the Implications for Innovation. 2016. Karen Gordon Mills (former SBA Administrator) and Brayden McCarthy. Harvard Business School. Working Paper.

¹⁸ Caro, vi.