WRITTEN TESTIMONY OF
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U.S. DEPARTMENT OF COMMERCE

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Committee on Small Business and Entrepreneurship

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Opening

Good Morning Madam Chair Landrieu, Ranking Member Snowe, and distinguished Members of the Committee. Thank you for inviting the Minority Business Development Agency (MBDA) here today to discuss capital access for minority businesses and the activities of MBDA.

My name is David A. Hinson and I was appointed as the National Director of the Minority Business Development Agency by Commerce Secretary Gary Locke on July, 15, 2009.

Prior to assuming this position, I was the President and CEO of Wealth Management Network, Inc., a multi-million dollar independent, financial advisory boutique. I have also held a variety of senior-level and mid-management positions at Bank of America, Morgan Stanley & Company, First Chicago Bank (now JP Morgan Chase) and the Village Foundation.

Overview

As is abundantly clear, the financial environment and recession last year has created tighter credit markets, a decline in housing values and swollen labor markets. For all businesses, especially those that are minority-owned, having access to working capital – or capital that is used to keep operations going and pay bills – has always been, and continues to mean the difference between the success or failure of that business.

Firms also need capital to fund their growth and ability to perform on contracts. And still others – primarily those in the construction field – need bonds to fulfill contractual obligations. Capital access is, in fact, one of the most important challenge business owners face on a daily basis.

Access to capital for minority-owned businesses, however, is an issue today as it was in 1969 when the Minority Business Development Agency was established. While there are some valuable lending and bonding programs available, minority-owned businesses continue to face substantial barriers and disparities with respect to accessing capital.

Last year we conducted multiple stakeholder forums with minority businesses, financiers and minority business associations to dissect the issue and explore solutions. It was from these meetings that MBDA agreed a study about capital access between minority and non-minority-owned businesses was needed.

Key Findings from the MBDA Report

In the January 2010 study commission by MBDA and co-authored by Drs. Robert Fairlie and Alicia Robb, entitled *Disparities in Capital Access between Minority and Non-Minority-Owned Businesses: The Troubling Reality of Capital Limitations faced by MBEs*, we found that limited financial, human and social resources – as well as racial discrimination – are primarily responsible for the disparities in capital.

Some particular aspects of the findings include:

1. Minority-owned firms are less likely to receive loans than non-minority owned firms.

- The denial rate for minority-owned firms with **less than $500,000 in annual revenues** is 41.9% compared to 16% for non-minority-owned firms.[1]
- The denial rate for minority-owned firms with **more than $500,000 in annual revenues** is 14.9% compared to 8.4% for non-minority-owned firms.[2]

2. When minority-owned firms do receive financing, they are provided less money regardless of the size of their firm, and at a higher interest rate.
   - The average loan size for a minority-owned firm with **less than $500,000 in annual revenues** is just over $9,000 while the average loan amount for a non-minority-owned firm of the same size is more than $20,000.[3]
   - The same holds true for **firms with annual revenues exceeding $500,000—** the average loan amount for a minority-owned firm is approximately $150,000 compared to more than $310,000 for a non-minority-owned firm.[4]
   - Additionally, loan interest rates for minority-owned firms with gross revenues less than $500,000 exceed 9% while non-minority-owned firms of the same size are often able to secure interest rates at less than 7%.[5]
3. Minority-owned firms also receive smaller equity investments than non-minority-owned firms even when controlling for firm size.
   - The average equity investment in a minority-owned firm earning more than $500,000 just exceeds $7,000; yet for a non-minority-owned firm, the average investment is more than $19,000.[6]
4. Yet, this same report finds that venture capital funds focused on investing in the minority business community are highly competitive. [7]
5. Moreover, during the 2001 recession, employment at minority-owned firms increased by 4% while employment among non-minority firms declined by 7%.[8] So had it not been for the employment growth among minority-owned firms, the job loss during this period would have been even larger.[9]

I see that Dr. Fairlie is scheduled to testify and understand he will go into more details of the MBDA report in a later panel this morning. Thus, at this time, Madam Chair, I would like to request that the MBDA report, *Disparities in Capital Access between Minority and Non-Minority-Owned Businesses: The Troubling Reality of Capital Limitations faced by MBEs*, in its entirety be entered in the hearing's official record.

And now, with the Committee's approval, I would like to move into some of the things MBDA is doing to address these challenges.

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[1] U.S. Department of Commerce, Minority Business Development Agency, *Disparities in Capital Access between Minority and Non-Minority-Owned Businesses: The Troubling Reality of Capital Limitations Faced by MBEs* (2010). The data source is the Federal Reserve System, Board of Governors, *2003 Survey of Small Business Finances.*

[2] Ibid.

[3] Ibid.

[4] Ibid.

[5] Ibid

[6] Ibid.

[7] Timothy Bates and William D. Bradford, "Venture-Capital Investment in Minority Business," *Journal of Money Credit and Banking* 40, no. 2-3 (2008): 489-504.

[8] U.S. Department of Commerce, Minority Business Development Agency, *Disparities in Capital Access between Minority and Non-Minority-Owned Businesses: The Troubling Reality of Capital Limitations Faced by MBEs* (2010). The data source is the U.S. Census Bureau's Special Tabulation on Minority-Owned Firms issued for the Minority Business Development Agency (2007).

[9] Ibid.

Overview of MBDA

As many of you know, MBDA has been in existence for over forty years. We are authorized by Executive Order 11625, as amended, and receive annual appropriations from the Commerce, Justice, and State Appropriations Subcommittee. The Agency's mission is to foster the growth and global competitiveness of U.S. businesses that are minority-owned.

We work with minority-owned firms of all sizes during all stages of their business life cycle with a special focus on firms with annual gross revenues of at least one million dollars. Our goal is to create a new generation of businesses with $100 million in annual revenue which in turn will generate higher economic activity and job creation.

MBDA funds a nationwide network of approximately 45 centers, which are operated as public/private partnerships. The centers are staffed by professional consultants who have the knowledge and practical experience necessary to operate profitable businesses.

MBDA's Performance Accomplishments

MBDA's performance is evaluated annually on the number of new jobs created, the total dollar value of contract awards and the total dollar value of financing transactions generated by the Agency. Last year, MBDA helped firms access more than $3 billion in contracts and financing, of which $800 million was specifically working capital, equity investments and bonding. Additionally, the growth of these minority firms led to the creation of more than 3,000 new jobs.

Still, there is much work ahead of us.

Consider this: A special tabulation completed by the U.S. Census Bureau on the 2002 Survey of Business Owners, showed that the growth rate in the number of minority-owned firms far outpaced that of non-minority owned businesses. Minority-owned firms employed almost 4.7 million workers with an annual payroll of $115 billion.[10] And these firms generated $661 billion in annual gross receipts.[11]

Despite this success, the potential for growth among minority-owned firms is largely untapped and unrealized.

For example, if the minority-owned business community had reached economic parity with their population representation in 2002, minority-owned businesses would have employed more than 16 million workers and generated more than $2.5 trillion in gross receipts,[12] thereby expanding the national tax base by billions of dollars. Clearly, the growth of capable and qualified

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[10] U.S. Department of Commerce, Minority Business Development Agency, *Disparities in Capital Access between Minority and Non-Minority-Owned Businesses: The Troubling Reality of Capital Limitations Faced by MBEs* (2010). The data source is the U.S. Census Bureau's Special Tabulation on Minority-Owned Firms issued for the Minority Business Development Agency (2007).

[11] Ibid.

[12] Ibid. U.S. Department of Commerce, Minority Business Development Agency, *The State of Minority Business Enterprises, An Overview of the 2002 Survey of Business Owners, Number of Firms, Gross Receipts, and Paid Employees* (2006). U.S. Department of Commerce, Minority Business Development Agency, *The State of Minority Business Enterprises*,(Fact Sheet) (2008).

minority-owned firms is necessary and will generate much needed employment, gross receipts, and add to the overall expansion of our national economy.

Denying capital to minority-owned firms constrains innovation and job creation. Working together, we can close this opportunity gap. By providing adequate capital to the minority-owned business community, we can achieve our goals of domestic prosperity and global competitiveness.

Moreover, in light of the U.S. Census' projections that the U.S. population will be majority minority by 2042,[13] investing in firms owned by minorities not only makes good business sense, but it is an investment in the future of the U.S. economy.

MBDA Initiatives

In addition to our ongoing efforts to grow the dollar volume of financing awards that we facilitate for our clients, MBDA is undertaking two specific initiatives to improve access to traditional and non-traditional sources of capital:

1. Surety Bonding Initiative

   Although minority firms represent 12 percent of all firms in construction nationwide,[14] currently fewer than one percent of all Federal construction contracts go to minority contractors. One of the leading causes of this is these contractors' inability to obtain surety bonding.

   The inherent problem is twofold: 1) consolidation of the surety industry has restricted access to performance bonds by raising underwriting standards; and 2) minority contractors continue to face discriminatory barriers and often lack the capacity, both financially and in terms of human resources, to effectively navigate through the myriad Federal, state, insurance, surety company, and private technical assistance programs available to them.

   Our goal is to help to identify over $100 million in private capital through a public/private partnership and to grow that capacity to over $1 billion in surety bonding capacity over time.

2. Minority Investment Fund Initiative

   MBDA is also focused on assisting minority-owned businesses outside the construction industry gain greater access to capital.

   MBDA is currently exploring the viability of a privately managed investment fund that would target minority-owned businesses in high-growth industries including green technology, clean energy, health care, infrastructure and broadband technology.

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[13] U.S. Census Bureau's 2000 Census projections for population (2008).

[14] MBDA industry analysis of data from the U.S. Census Bureau's Special Tabulation on Minority-Owned Firms issued for the Minority Business Development Agency (2007).

MBDA believes it is possible to spur the development of a privately managed investment fund that would attract $100 million dollars in private wealth and institutional capital and help to address some of the barriers minority owned firms face in obtaining capital from existing funds and lenders.

Conclusion

I would again like to thank you Madam Chair Landrieu, Ranking Member Snowe, and the entire Committee for allowing me to testify before you today. I respectfully request the Chair to enter my full written testimony into the official hearing record.

On a final note, Madam Chair, the Department of Commerce and MBDA are honored by this opportunity to testify before you and your distinguished colleagues. We look forward to working with you to create an environment where minority firms have an equal opportunity to participate in the marketplace. Thank you.