Joint Economic Committee
Republicans
Senator Sam Brownback *Ranking Member*
Representative Kevin Brady *Senior House Republican*

Economic News Commentary

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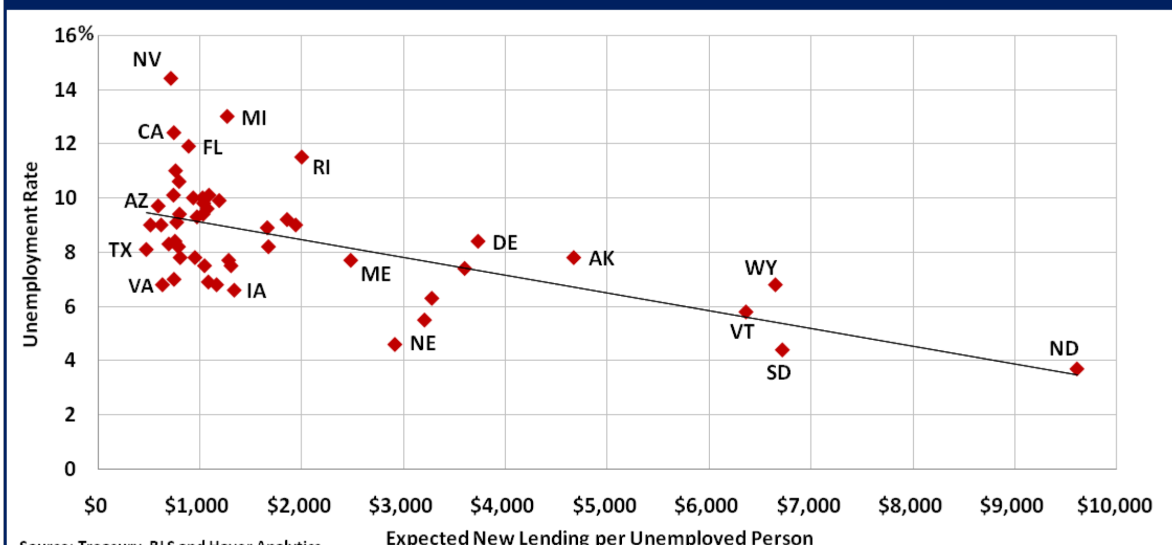
Still No Correlation between Funding and the Unemployed

On Friday, October 8th, the Treasury Department announced the State Small Business Credit Initiative (SSBCI), a new state-by-state funding allocation to support $15 billion in small business lending aimed at helping entrepreneurs obtain credit to hire new workers and expand their businesses. The funds are part of the Small Business Jobs Act that President Obama signed into law the week prior. In accordance with the SSBCI, states may apply for federal funds for programs partnering with private lenders to extend credit to small businesses. With a minimum $10:$1 in private to federal funding, the expectation is that $1.5 billion in federal funding will generate $15 billion in private lending.[1]

The formula to determine the amount of SSBCI funds a state is eligible for is based on each state's unemployment rate and its decline in employment relative to other states. However, it appears that the lending formula fails to account for the number of unemployed persons in each state.

Expected New Lending ($10:$1 Match) per Unemployed Person and the Unemployment Rate, by State



Source: Treasury, BLS and Haver Analytics

As shown by the graph above, which assumes a $10:$1 match, SSBCI provides less funding per unemployed person for small business lending to create jobs in the states with the highest unemployment rates, while states with the lowest unemployment rates receive the most funding per unemployed person. For example, North Dakota boasts the lowest unemployment rate of 3.7 percent—lower than the national average prior to the recession—and 13,700 unemployed persons, but is expected to generate $9,612 in small business lending per unemployed person. Alternatively, California bears the third highest unemployment rate at 12.4 percent, and 2,269,900 unemployed persons, but must provide only $743 in small business lending per unemployed person. Texas receives the least funding in small business lending per person and must produce only $472 of small business lending per its 987,200 unemployed persons even though Texas has a below-average unemployment rate of 8.1 percent.

Failure to account for the number of unemployed persons in each state leaves some unemployed persons in particular states significantly disadvantaged compared to unemployed persons in other states receiving higher funds per unemployed person. Unfortunately, this is not the first incidence of inequitable distribution of economic stimulus funds; the deployment of funds from the first $814 billion stimulus to the states followed a similar pattern. Instead of relieving unemployment in states that need the most relief, the funding allocations only distort the amount of funding per unemployed person.

Furthermore, these funds provide nothing more than a short-term boost to an economy rife with uncertainty. These funds do not beget long-term sustainable patterns of specialization and exchange that catalyze the success and growth of entrepreneurs and businesses. In fact, these funds merely create a moral hazard and thus distort the incentives for investing in small business, potentially leading to malinvestments and creating new drains on the economy. If the current Administration wishes to boost job and economic growth, it would achieve far better results by reducing tax burdens and removing the uncertainty of how current and impending laws will affect these individuals and businesses. Limited interference from government rather than redistribution is the condition in which entrepreneurs and businesses grow.

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[1] The SSBCI lets states either build upon existing, successful state-level small business lending programs, or if a state does not have an existing program, officials are permitted to establish one to obtain this federal funding. Examples of existing state-level programs include collateral support programs, the Capital Access Programs (CAPs) and loan guarantee programs. Collateral support programs set aside funds as additional collateral to what a borrower already possesses, providing the lender with greater confidence to extend credit. CAPs are loan portfolio assurance programs in which states match contributions to bank loan loss reserves when lenders extend credit to these qualifying businesses. Loan guarantee programs let states provide guarantees on certain small business loans to boost lender confidence. In order to be eligible for the allocated federal funding, states must provide a plan detailing how they will apply their funding allocations to the Treasury for review and authorization. For more information, see: "Treasury Announces State-by-State Funding Allocations to Support $15 Billion in Small Business Lending, Create New Jobs," U.S. Department of the Treasury, October 8, 2010, http://www.treas.gov/press/releases/tg896.htm