

United States House of Representatives
Committee on Small Business

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The National Council of Textile Organizations



"Increasing Access to Capital for Small Business"

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2360 Rayburn House Office Building
Washington D.C. 20515

Good afternoon Chairwoman Velazquez and members of the Committee, my name is Cass Johnson, and I am the President of the National Council of Textile Organizations (NCTO). I am pleased to appear before you today to address this very important topic and will be pleased to share with you NCTO's perspectives on how this Committee can work to increase access to capital for small businesses. NCTO is a trade association representing the entire spectrum of the textile industry which includes fiber, yarn, fabrics, and industry suppliers. The textile sector, from fiber to finished garments, employs over 600,000 workers in the United States.

Importance of Manufacturing Jobs to the Entire Economy

Given the harsh economic environment, NCTO's member companies have gone to great lengths to ensure that their operations remain strong and that they are able to provide good-paying manufacturing jobs for U.S. workers and their families. Manufacturing jobs are a critical portion of the U.S. economy and the small business sector. A recent survey of U.S. public opinion found that 71 percent of the public believes that manufacturing should be a national priority.¹ The survey also found that in relationship to six other industries, manufacturing is the number one most important industry in maintaining a strong national economy. Other industries ranked behind manufacturing in the following order: technology, energy, healthcare, financial services, retail, and communications. Given the level of importance placed on the manufacturing sector, the U.S. government should be doing its utmost to ensure the sector is viable and able to put Americans back to work.

Unfortunately, the critical benefits that the U.S. manufacturing sector contributes to our economy have gotten short shift for many years. Over five million manufacturing jobs, over one quarter of the manufacturing workforce, have been lost since 2001 and more than 1.1 million jobs have been lost during the last nine months. In the case of the textile industry, nearly 50,000 jobs have been lost since December 2008.

Manufacturing jobs are the highest paying, and highest value added jobs in our economy. And, according to economists, manufacturing jobs support far more jobs in our economy than any other. Madame Chair, rebuilding a strong U.S. manufacturing base and creating new high paying, highly skilled manufacturing jobs is clearly essential in order for the U.S. economy to recover.

Role of the Small Business Administration (SBA) in Supporting Manufacturing Jobs

This committee, in working with the Small Business Administration (SBA), can make a real impact in aiding this nation's recovery. Small and medium sized manufacturers need access to credit, working capital and loan guarantees in order to manufacture

¹ 2009 Index of the Public Views on Manufacturing, National Association of Manufacturers.

products and engage in domestic and international commerce. These financing options play a pivotal role in the manufacturing sectors ability to produce goods and export those goods to customers outside the United States. According to the SBA, Office of Advocacy, small businesses are responsible for over 97 percent of all U.S. exports.

The U.S. textile industry is the world's third largest exporter of textile products, exporting over \$16 billion in goods to other nations in 2008. However, without adequate financing options and government supported guarantees, our companies are now being shut out of some of the largest and most important export markets. During the current downturn, securing adequate credit financing and short-term loan options have become a significant problem. This problem is getting more pronounced and is now threatening many parts of our industry.

I understand that the committee recently considered a broad package of bills that aimed to provide additional access and flexibility for small businesses to secure SBA guaranteed loans. On behalf of NCTO, I applaud the committee's efforts to expand small business opportunities. However, a significant issue, the ability of small businesses to access *financing for overseas exports*, was not addressed. Currently, the SBA is able to grant export working capital loans to small businesses through the Export Working Capital Loan Program. However because of outdated restrictions on loan limits and business size, this program is rarely utilized by domestic manufacturers.

I urge the committee to consider working with the SBA to update the Export Working Capital Loan Program so that small businesses, including manufacturers, are able to tap into government supported export financing. In addition, we urge the committee to focus specific attention to small and medium manufacturers' ability to guarantee credit so that they may engage in international commerce. Before I outline our proposed modifications, I'd like to outline the current problem that the industry is having with its export operations.

Review of U.S. Textile Credit Sourcing

Historically, U.S. mills shipped primarily to domestic customers on open terms, generally 30 to 60 days. Some companies utilized domestic factors and some had open terms and credit insurance. Credit for exports has generally been handled in a variety of ways: either against Letters of Credit (L/C); open terms with credit insurance; or in many cases factors. The terms were similar to those offered to the domestic customers, but sometimes included special shipments or orders which allowed for 90 day terms.

Over time, as the industry has become more export oriented, it has become more difficult for U.S. textile manufacturers to secure financing from private lending sources. When U.S. mills sales were largely domestic in origin, U.S. mills had various means of financing with domestic banks for raw material, work in process, finished goods and

accounts receivable (A/R), and normally financing arrangements were granted annual renewal. For collateral, the lenders required real and personal property, inventory (raw and finished goods), A/R (domestic) and subordinating credit insurance policies. However, as the textile industry has come to rely more on exports, less credit is available because U.S. lenders will increasingly not accept foreign accounts receivable as collateral.

Impact of Financial Crisis and Resulting Loss of Export Credit Financing

U.S. textile mill credit problems have been dramatically increased by the financial crisis, beginning in mid to late 2008. As the recession grew more pronounced, banks began cutting credit to U.S. mills either during the term, based on covenants in existing agreements, or upon renewal. On top of the tighter restrictions, factors pulled out of agreements to offer credit to many export customers. This exposed U.S. mills to greater risk, threatening the ability of the mills to function properly. In addition, credit insurers have cut back on A/R guarantees or even canceled customers. This action caused a backlash by banks that are no longer willing to extend credit to mills that traditionally have never had issues in securing credit financing.

In contrast, Asian governments and banks reacted swiftly to ensure that export credit is not only available, but plentiful. In April, China announced a Textile Revitalization Plan that extended new credit lines and credit guarantees to small and medium sized textile companies and increased textile export subsidies by 40 percent. In August, Pakistan announced it was eliminating taxes on all textile exports and would be granting comprehensive insurance for all textile exporters which would protect against “the failure of the buyer, bank or problems faced by the buyer country.” And yesterday, India announced that all textile exporters would now get a two percent rebate on their credit costs from the Indian government.

As noted in the table below, U.S. textile exports to the Western Hemisphere preference areas and imports of apparel from these areas have been dramatically impacted. While sourcing decisions are the result of many factors, many NCTO members report that they have lost orders to the region because the cancellation of credit, insurance or guarantees in the region. Indeed, the Western Hemisphere countries have seen declines that are twice as great as their Asian competitors. Imports of apparel from Asia are down ten percent compared to a 22 percent decline for the Western Hemisphere. As the Western Hemisphere accounts for 75 percent of total U.S. exports, the 24 percent decline in U.S. textile exports is taking an enormous toll.

Reduced Export Credits Hurts U.S. Textile Exporters and Western Hemisphere Suppliers		
	CAFTA/NAFTA/ANDEAN	
	Percentage Change	Dollar Change
Apparel Imports	-22%	- \$1.9 billion
U.S. Textile Exports	-24%	-1.1 billion

The textile credit problems have been compounded by customers, domestic and foreign, who have begun to pay bills late. In particular, because of late payments from retailers, our apparel producing customers in the CAFTA region have come under severe financial stress. *This is where the SBA, working in concert with Ex-Im bank, could play a pivotal role in restoring fluidity to the textile and apparel supply chain.* The challenge that we are experiencing with Ex-Im is that it has pulled coverage because of late payments.

Foreign customers, in turn, have seen regional banks in Central America cut their credit lines in half and in some cases by even more. In part because U.S. banks have stopped extending credit to the Central American banks, U.S. mill customers are now asking U.S. mills to extend longer terms, sometimes as much as up to 150 days and to do so without Ex-Im coverage, factoring, or private credit insurance coverage. This is a burden that even large well capitalized firms would find hard to bear, much less small U.S. textile exporters.

Taking all the above into account, one can easily understand that smaller and midsize mills have been driven to the brink of failure. In addition, banks are now discounting the use of collateral to back credit terms and are now insisting on using cash flow as a basis for extending credit. For many companies, cash flow over the previous 12-months has been extremely weak, thus further reducing many textile companies ability to secure future export financing.

What small and midsize mills need now is access to capital in order to function normally and to have an adequate supply of raw material on hand in order to react quickly once orders are received. They also need credit in order to finance outstanding A/R, which have now grown because of the problem of slow payments and also because of the necessity to grant longer payment terms.

In addition to the credit needed to finance the A/R, textile companies need Ex-Im to get back to guaranteeing the A/R's for export orders since small and midsize companies are not able to carry credit risks. Ex-Im has the authority to do so today, but their choice today has been to restrict giving such guarantees.

Solutions

NCTO has been proactive in response to the credit crisis. We formed an *ad hoc* committee of member companies and representatives from the National Cotton Council and Cotton Council International to review the situation and determine what could be done to correct it. The group studied the array of programs available through the Small Business Administration (SBA), Ex-Im Bank, and the U.S. Department of Agriculture's GSM program. Several of NCTO's members have utilized these programs in the past, so there was already a broad understanding of what was available. As I mentioned earlier in my testimony, during normal economic times, the industry relies most heavily on private sector financing, with these programs filling the gaps by providing much needed credit insurance.

However, with the sharp reduction in credit from private sources, two modifications are needed immediately to the SBA export financing programs in order for U.S. textile manufacturers to continue to shipping goods overseas.

Within the SBA programs, specifically the Export Working Capital Program, there are two requirements that automatically disqualify virtually every textile company and many other small manufacturers.

Proposed Modifications to Export Working Capital Program

The first requirement is the size of the loans being guaranteed. Even for small companies, credit needs can easily exceed the \$2,000,000 cap. Overseas export orders are now much larger than they used to be and specialty products are higher value added.

We suggest creating a new loan program outside of the current 7(a) program. SBA could set three loan amounts at \$5 million, \$10 million and \$15 million that tie risk to the amount borrowed. This would limit the cost of the program. The terms of the loan would be for 12 to 18 months and use standard SBA terms for interest rates. The guarantee level would depend upon the size of the loan. SBA could offer its normal 90 percent guarantee for loans under \$5 million; the program could offer an 80 percent guarantee for loans from \$5 million to \$10 million, and 70 percent for loans ranging from \$10 million to \$15 million. For companies with multiple loans, the total borrowed could not exceed \$ 25 million.

The second requirement limiting small and medium manufacturers' ability to take advantage of SBA programs is the limit on the size of the company. As you know, SBA allots size requirements by North American Industry Classification System codes. Textiles are classified in NAICS 313, Textile Mill Productions in NAICS 314, and

Apparel in NAICS 315. The size limitations for companies in NAICS codes 31-33, which covers all manufacturers in every industry, should be raised from the current limit of 500 employees to 1,250.

Our study of SBA loan programs has revealed that the agency has already capped size standards at 1,000 or 1,500, so we do not believe this moves the SBA outside its current scope. Increasing the size limit for manufacturers would open significant new export opportunities for small and medium sized enterprises in the United States. To ensure that SBA is covering businesses with an established history, the program could require that program candidates have been in business for at least one year.

Finally, we would also strongly encourage SBA to continue its credit programs offered in conjunction with the Ex-Im Bank. Even though many of the limitations mentioned earlier are still a barrier preventing full access to these programs, we believe this has been a fruitful relationship that has benefited U.S. companies. Because of the loan limitations on SBA programs, this joint effort has expanded access to credit for some small businesses since it allows a higher overall credit limit

Conclusion

The need for credit has never been greater. We are seeing solid export opportunities in the NAFTA and CAFTA regions, but we are being forced to turn away business due to shortfalls of credit, credit guarantees, and working capital. We believe that the SBA can play an important role in opening up financing to companies and industries in need of alternative financing options. NCTO is committed to working with this committee, your Senate counterparts, and the SBA to accomplish this goal.

Chairwoman Velazquez, I'd like to thank you for the opportunity to appear before the committee and would be pleased to answer your questions.

Thank you.

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