One Sign Of Recovery: Businesses Are Borrowing Again

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Martin Foil's company sells yarn that winds up in clothes from the Gap, Ralph Lauren and American Apparel, and business is growing. He's buying new machines and hopes to hire as many as 200 workers this year.

When he decided to expand into a shuttered yarn factory in North Carolina, he borrowed $11 million recently from Wells Fargo to buy it.

"It was a Hanes factory that was closed for a couple of years and had some good equipment — we knew we could crank up that place," said Foil, who also used the loan to buy equipment and another factory in South Carolina. "We have the advantage of being stronger at a time when others aren't."

Now that demand is up and business is finally improving for many companies, they're doing what they always do at the beginning of an expansion — calling the bank and asking for a loan.

And in a stark contrast to the depths of the financial crisis, the banks are saying yes.

In the last three months of 2010, U.S. Bancorp wrote $8 billion in new business loans, the most in two years. JPMorgan Chase added 400 midsize companies as clients. And bank loans overall grew for the first time in two years, according to the Federal Reserve.

"Companies are talking about growth in ways they haven't for three years," says Perry Pelos, head of Wells Fargo's commercial banking.

Loans are one of the best gauges of economic growth. Small and midsize businesses that form the backbone of the U.S. economy take them out to pay for business needs — unlike big corporations, which go to the bond markets for low-cost debt.

Borrowing by smaller companies is being watched especially closely because it may indicate those companies are preparing to hire. So far, the economic recovery hasn't been accompanied by job growth. Small companies created about three of every five new jobs over the past two decades.

Those companies took a pummeling during the recession. Bankruptcies skyrocketed and led to massive job cuts. Firms employing fewer than nine people accounted for more than half the jobs lost in the first quarter of 2010, just after the recession technically ended, according to the Labor Department.

Many small businesses blame banks for making matters worse by pulling back credit dramatically after the financial crisis.

Vu Thai, president of Efficient Lighting of Buena Park, Calif., wanted more space to house his energy-efficient light bulbs and fixtures at the end of 2008. "Nobody would lend to us," Thai says.

But demand for Thai's bulbs increased, and he snagged Home Depot as a customer last year, sending sales up 10 percent. In December, Thai secured a $100,000 loan to install racks and other equipment in his new warehouse. He bought the space with another loan of $1.6 million taken jointly from Bank of America and a government program for small businesses.

In another hopeful sign, about 75 percent of the loans taken out in the last three months were to pay for mergers and acquisitions. That shows that companies that can afford it are buying up weaker competitors as they prepare for growth in the months ahead.

"After surviving a brutal recession, companies are starting to look around them for opportunities to get stronger," says Laura Whitley, an executive at Bank of America's global commercial banking business.

Still, while many companies have opened up lines of credit, many aren't using them yet, reflecting their hesitation. About 25 percent of small businesses applied to renew a credit line in 2010, while only 13 percent tried to get a business loan, according to the National Federation of Independent Business.

U.S. Bancorp CEO Richard Davis says he's watching closely to see how many companies dip into their lines of credit for cash. He said in a recent conference call that nearly half of the bank's customers, a record, don't use their lines of credit at all.

The companies that were the first to apply for a line of credit were those that hunkered down the most during the recession because of massive sales declines, but were now suddenly experiencing sales growth.

For instance, manufacturers of plastic containers and packages saw sales increase about 5 percent in 2010 after a 16 percent decline in 2009. They nearly doubled their credit lines, to about 2.8 percent of their assets, according to SageWorks, a firm that analyzes financial trends at private companies. .

One such company is Pyrotek of Spokane, Wash., whose primary customers are car parts manufacturers. Pyrotek, which makes materials to handle aluminum at high temperatures, saw sales plummet 40 percent at the depths of the recession, and it cut staff.

The company's chief operating officer, Don Ting, says car sales finally grew last year. His customers started ordering more after a year-long hiatus, and Ting hired back most of his employees. He recently increased his available credit with Wells Fargo by more than $10 million.

"We're not losing money anymore, nor are we back to 2008," he says, "but we are in a better place."