# FSG-SAPF Joint Webinar:

# Government Lending Schemes:
## The Case of the U.S. Small Business Administration

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## Introduction

- Government Lending Schemes (GLS) for SMEs are successful and replicable government interventions to overcome the impediments to access to credit for relatively opaque SMEs seeking capital.
- One GLS permutation is exemplified by the case of the U.S. Small Business Administration (SBA).
- The SBA an independent government agency created in 1953 that is dedicated to aiding, counseling, assisting, and protecting the interests of small business concerns.

# Introduction

- The SBA's mission is to "maintain and strengthen the nation's economy by enabling the establishment and vitality of small businesses and by assisting in the economic recovery of communities after disasters."
- The SBA developed its performance plan and budget for achieving its mission based upon 4 strategic goals and 10 strategic objectives

# Mission Statement and Goals of the U.S. Small Business Administration

**Mission Statement**

Maintain and strengthen the nation's economy by enabling the establishment and vitality of small businesses and by assisting in the economic recovery of communities after disasters.

**Goal 1**

Support small business revenue and job growth

- 1.1 Expand access to capital
- 1.2 Help small business exporters succeed in global markets
- 1.3 Ensure federal contract and innovation set-aside goals are met and/or exceeded

**Goal 2**

Build healthy entrepreneurial ecosystems and create business friendly environments

- 2.1 Develop small businesses through technical assistance
- 2.2 Build healthy entrepreneurial ecosystems
- 2.3 Create a small business friendly environment

**Goal 3**

Restore small businesses and communities after disasters

- 3.1 Deploy disaster assistance effectively and efficiently

**Goal 4**

Strengthen SBA's ability to serve small businesses

- 4.1 Ensure effective and efficient management of Agency resources
- 4.2 Build a high-performing workforce
- 4.3 Implement enterprise-wide information system modernization and cost-effective technology

## Introduction

- The association administers several programs to support small businesses and expand employment opportunities, including:
  - (i) improving access to capital through loan guarantees and venture-capital programs;
  - (ii) technical assistance programs such as entrepreneurial education programs to assist a business in its formation and expansion;
  - (iii) increasing opportunities for government contracting by allotting 23% of total contracts to small businesses; and
  - (iv) providing direct lending to businesses and households as assistance during disasters

## Introduction

- The SBA’s flagship programs incentivize creditors and investors through credit-guarantee schemes known as the 7(a) General Business Loan-Guaranty Program and the 504 Certified Development Loan-Guaranty Program.
- However, the SBA also lends directly to businesses through its disaster relief and micro-loan programs.
- In addition, the SBA has developed its innovative Small Business Investment Company (SBIC) Program, which is a private-public partnership by which the SBA levers private funding with proceeds from debentures issued by the SBA.

## SBA’s 7(a) General Business Loan-Guaranty Program

- The SBA’s primary loan program is its 7(a) General Business Loan-Guaranty Program, which is generally used for businesses to meet various needs, such as equipment purchases, working capital, leasehold improvements, inventory, or real estate purchases.
- The standard 7(a) program provides a 75%–85% guarantee for SME loans up to $5 million.
- Lenders do not have to require collateral for loans up to $25,000; for loans greater than $350,000, lenders are required to request collateral up to the full amount of the loan

# SBA's 7(a) General Business Loan-Guaranty Program: Subsidy and Fee Structure

| | Current | FY2021 Request |
|---|---|---|
| **Subsidy Rate** | 5 basis points (bps) ($15 million in subsidy appropriation needed for $30 billion program level) | 0 bps |
| **Fee Structure** | **Upfront fee:**<br>• Loans <= $150,000: 2.0% (1.5% remitted to Small Business Administration)<br>• $150,000 < Loans <= $700,000: 3.0%<br>• Loans > $700,000: 3.50%<br>• Additional 0.25% fee for any guaranteed amount over $1 million<br>• Loan term less than 1 year: 0.25%<br>• Export Working Capital Program loans, 13–24 month maturity: 0.525%<br>• Export Working Capital Program loans, 25–36 month maturity: 0.80%<br>**Ongoing fee: 55 bps** | **Administrative fee:**<br>• $0.16 per every hundred dollars approved based on $30 billion in lending<br>**Upfront fee:**<br>• Loans <= $150,000: 2.0% (1.5% remitted to SBA)<br>• $150,000 < Loans <= $700,000: 3.0% Loans > $700,000: 3.64%<br>• Additional 0.25% fee for any guaranteed amount over $1 million<br>• Loan term less than 1 year: 0.25%<br>• Export Working Capital Program loans, 13–24 month maturity: 0.525%<br>• Export Working Capital Program loans, 25–36 month maturity: 0.80%<br>**Ongoing fee: 55 bps**<br>• Upfront fee waived for SBA Express loans to veterans |

## The Paycheck Protection Program

- In response to the Covid-19 pandemic, the U.S. government approved approximately $500 billion in forgivable loans the were offered to small businesses adversely affected by the pandemic.
- To expedite delivery of these funds, the government turned to the SBA's 7(a) loan-guarantee program, scaling it up by orders of magnitude.
- This enables the government to utilized SBA-approved lenders as the conduits for funding affected small businesses in timely manner.
- By the end of July, 2020, the SBA had approved more than 5 million PPP loans.

## FinTech and the Paycheck Protection Program

- Fintech companies played a key role in the Paycheck Protection Program.
- Fintech lenders became SBA-approved lenders and were able to quickly increase the number of very small loans being disbursed.
- Other fintech companies, such as payroll processers, worked with small-businesses to prepare the payroll paperwork necessary for obtaining PPP loans.
- Fintech loan-processing companies enabled small community banks to rapidly increase their loan volume to satisfy PPP demand.

# SBA's 504 Certified Development Company Loan-Guaranty Program

- The SBA's 504 Certified Development Company Loan-Guaranty Program was designed to provide fixed-rate, long-term financing for a firm to acquire fixed assets (including land and buildings) for modernization or expansion.
- These loans are only available from Certified Development Companies (with whom the SBA partners to provide such credit).
- Certified Development Companies are nonprofit corporations established to promote economic development in a community by making 504 loans; its loans are funded by SBA-guaranteed debentures.
- As of 2020, 260 Certified Development Companies operated in the US, each with a defined geographic area, usually the state in which the Certified Development Company is located.

## SBA’s 504 Certified Development Company Loan-Guaranty Program

- A typical 504 project includes a loan from a private-sector lender with a senior first-lien position, an SBA-backed loan from a Certified Development Company in a second-lien position, and an equity contribution from the borrower. The typical financing structure for a 504 loan is:
  - Private-sector lender: 50% (first-lien position)
  - Certified Development Company lender: 40% (second-lien position)
  - Borrower: 10% (equity contribution)

## SBA's 504 Certified Development Company Loan-Guaranty Program

- The maximum loan amount is $5 million
- Maturities can be set at 10, 20 or 25 years.
- As of Nov. 2020, loan rates were:
  - 2.23% for 10-year loans,
  - 2.36% for 20-year loans, and
  - 2.40% for 25-year loans.

# SBA's 504 Certified Development Company Loan-Guaranty Program: Subsidy and Fee Structure

| | Current Law Scenario | FY2021 Request |
|---|---|---|
| **504 certified development company** | Upfront fee: 50 basis points (bps)<br>Ongoing fee: 45.17 bps | Administrative fee:<br>• $0.24 per $100 approved based on $7.5 billion in lending<br>Upfront fee: 50 bps<br>Ongoing fee: 45.30 bps |
| **504 Refi** | Upfront fee: 50 bps<br>Ongoing fee: 48.65 bps | Administrative fee:<br>• $0.24 per every hundred dollars approved based on $1 billion in lending<br>Upfront fee: 50 bps<br>Ongoing fee: 48.75 bps |

## SBA’s Disaster Assistance Program

- The Disaster Assistance Program provides direct SBA loans to businesses of all sizes as well as households affected by natural disasters.
- The loans are to cover losses not covered by insurance of FEMA funding.
- The loans also cover business operating expenses that could have been met had the disaster not occurred.

## SBA’s Disaster Assistance Program

- The maximum loan amount is $2 million.
- The interest rate will not exceed 4% if the firm cannot obtain credit elsewhere.
- For businesses and nonprofit organizations with credit available elsewhere, the interest rate will not exceed 8%.
  - The SBA determines whether the applicant has credit available elsewhere.
- Repayment terms can be up to 30 years.
- Collateral is required only for loans > $25,000, but is required for larger loans.

## SBA’s Covid-19 Economic Injury Disaster Loan (EIDL) Program

- The SBA developed its EIDL program in response to the Covid pandemic to assist small businesses experiencing a temporary loss of revenue due to the pandemic.
- The proceeds of the loans can be used to finance working capital and/or normal operating expenses of the business.
- During 2020, the U.S. government appropriated $60 billion to fund EIDLs and an additional $20 billion to fund EIDL grants (which were forgivable).

## SBA’s Covid-19 Economic Injury Disaster Loan Program

- The maximum loan amount is $2 million.
- The interest rate is 3.75% for small businesses.
- Repayment term is set at 30 years.
- Payments are deferred for the first year.
- There are no prepayment penalties or fees.
- Collateral is required only for loans > $25,000, but is required for larger loans.

## SBA’s Microloan Program

- The Microloan Program provides direct SBA loans to help small businesses start up and expand.
- Targets start-ups with little or no credit history in underserved markets, especially minority-owned and female-owned firms, as well as those in rural areas
- Proceeds can be used to finance working capital, or machinery & equipment, but not real property.
- The maximum loan amount is $50,000; the average is $13,000.
- Maturity is up to 7 years.
- Interest rates are based on the 5-year US Treasury Bond rate; for 2019, the average loan rate was 7.5%.

## SBA’s Microloan Program

- The Microloan program provides direct loans to nonprofit lenders that, in turn, make loans to small businesses
- Microloan lenders also provide marketing, management, and technical assistance to both potential and actual borrowers.
- The SBA also provides grants to the intermediary lenders of up to 25% of the loan amounts to help offset the lender’s costs of providing business-based training, technical assistance, and coaching to the micro-borrowers.
- The combination of debt financing, technical assistance, and training helps build up the capacity of the micro-borrowers so that they can improve operations, grow their businesses, support job creation and retention, and earn a profit.

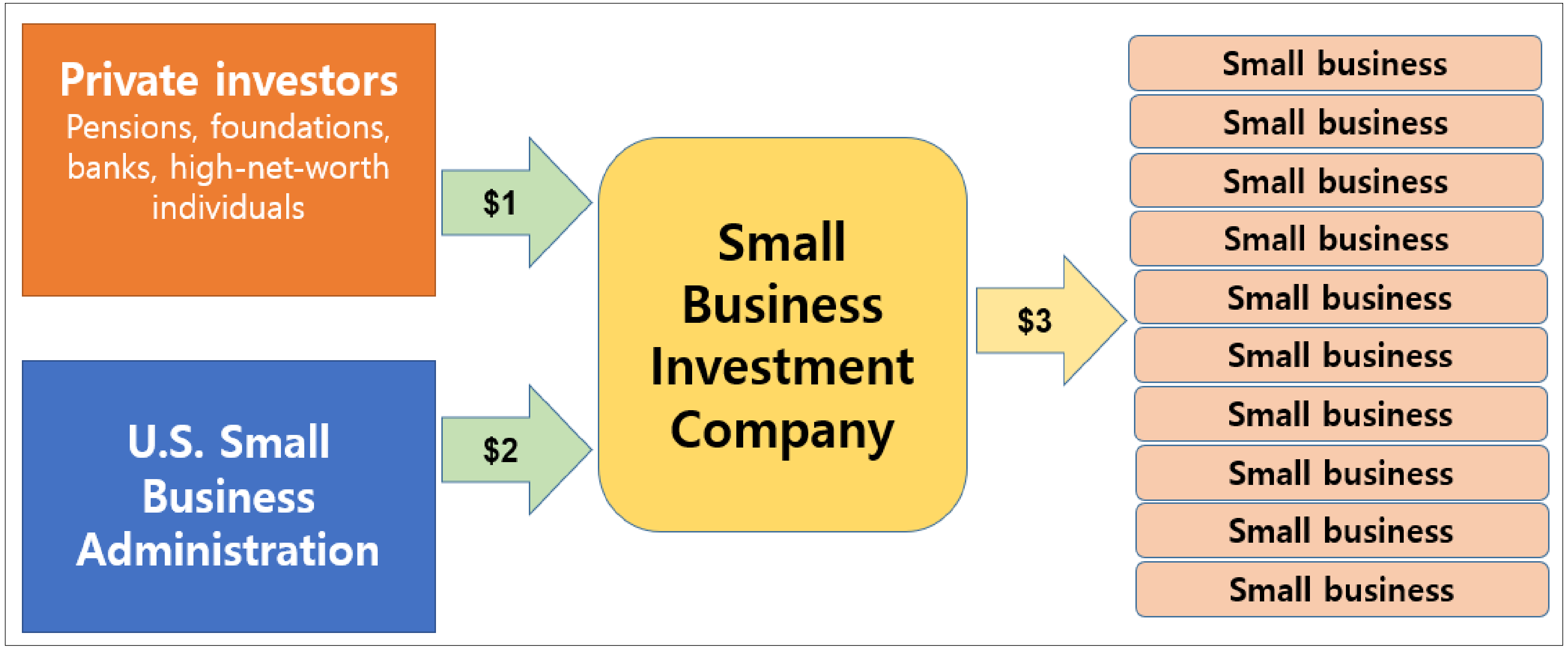
## SBA’s Small Business Investment Company (SBIC) Program

- The Small Business Investment Company (SBIC) Program is an innovative multi-billion investment program created in 1958 to bridge the gap between entrepreneurs’ need for capital and funds available from traditional sources of financing.
- The program has made billions of dollars in capital available to US small businesses representing a variety of industries across the country.
- These outcomes came about using a public-private partnership that uses the “full faith” and credit of the US government to leverage up the amount of private-sector investment capital available to small firms.

## SBA’s Small Business Investment Company (SBIC) Program

- The SBA raises capital by issuing taxpayer-backed debentures guaranteed by the SBA.
- It then combines these funds with capital raised by privately and publicly managed investment funds that raise capital from private investors, such as banks, pension funds, or wealthy individuals.
- Qualified fund managers that complete the SBA’s rigorous application process are granted a license to operate their fund as an SBIC.

# SBA's Small Business Investment Company (SBIC) Program




- For every $1 the fund raises from investors, SBA will commit up to $2 of debt, subject to a cap of $175 million.
- The SBIC then invests this combination of capital in qualifying small businesses

# SBA's Small Business Investment Company (SBIC) Program

| Key Feature | Program Summary |
| --- | --- |
| Use of Proceeds | To purchase small business equity securities, make loans to small businesses, purchase debt securities from small businesses, and provide, subject to limitations, small businesses a guarantee of their monetary obligations to creditors not associated with the Small Business Investment Company (SBIC). |
| Maximum Leverage Amount | A licensed SBIC in good standing with a demonstrated need for funds may apply to the SBA for financial assistance (called leverage) of up to 300% of its private capital. However, most SBICs are approved for a maximum of 200% of their private capital, and no fund management team may exceed the allowable maximum amount of leverage, currently $175 million per SBIC and $350 million for two or more licenses under common control. |
| Maturity | SBA-guaranteed debenture participation certificates can have a term of up to 15 years, although currently only one outstanding SBA-guaranteed debenture participation certificate has a term exceeding 10 years and all recent public offerings have specified a term of 10 years. SBA-guaranteed debentures provide for semiannual interest payments and a lump sum principal payment to investors at maturity.<br><br>SBICs are allowed to prepay SBA-guaranteed debentures without penalty. However, a SBA-guaranteed debenture must be prepaid in whole and not in part and can only be prepaid on a semiannual payment date. Also, low-to-moderate income area debentures are available in two maturities, for 5 years and 10 years (plus the stub period). |
| Maximum Interest Rates | The debenture's coupon (interest) rate is determined by market conditions and the interest rate of 10-year Treasury securities at the time of the sale. |
| Guaranty Fees | The SBA requires the SBIC to pay a 3% origination fee for each debenture issued (1% at commitment and 2% at draw), an annual fee on the leverage drawn, which is fixed at the time of the leverage commitment, and other administrative and underwriting fees, which are adjusted annually. |
| Job Creation Requirements | No job creation requirements. |
| Use of Proceeds | To purchase small business equity securities, make loans to small businesses, purchase debt securities from small businesses, and provide, subject to limitations, small businesses a guarantee of their monetary obligations to creditors not associated with the SBIC. |

# Small Business Investment Company (SBIC) Program: Performance, 2016-2020

| SBIC Program | FY 2016 | FY 2017 | FY 2018 | FY 2019 | 1H 2020 | Change from 1H 2019 |
|---|---|---|---|---|---|---|
| Financing amount ($ million) | 5,991.7 | 5,727.3 | 5,502.6 | 5,865.7 | 3,650.6 | -16% |
| Type of financing ($ million) | | | | | | |
| Straight debt | 3,791.7 | 3,720.2 | 3,543.0 | 3,594.4 | 2,263.8 | -12% |
| Debt with equity features | 1,157.1 | 859.8 | 807.3 | 792.0 | 457.0 | -25% |
| Equity only | 1,042.9 | 1,147.4 | 1,152.2 | 1,479.3 | 929.8 | -18% |
| No. of companies financed | 1,201 | 1,077 | 1,151 | 1,191 | 884 | -7% |
| Special competitive opportunity gap business | 332 | 308 | 315 | 292 | 223 | -4% |
| Business located in LMI areas | 284 | 262 | 265 | 245 | 190 | -4% |
| Woman, minority, veteran owned businesses | 61 | 68 | 66 | 59 | 50 | 9% |
| No. of jobs created or sustained | 122,382 | 112,865 | 106,021 | 111,201 | 69,253 | -16% |

# Financial Performance of the SBA's Four Major Programs (2012-2020)

## **Unpaid Principal Balances, Amounts for Four Major SBA Programs** ($ million)

| Program | FY 2012 | FY 2013 | FY 2014 | FY 2015 | FY 2016 | FY 2017 | FY 2018 | FY 2019 | FY 2020 |
|---|---|---|---|---|---|---|---|---|---|
| 7(a) Regular | 60,079 | 63,671 | 68,186 | 73,019 | 78,788 | 86,195 | 92,416 | 95,099 | 95,640 |
| 504 Regular | 26,909 | 26,850 | 27,185 | 26,470 | 25,784 | 25,493 | 25,831 | 25,771 | 25,722 |
| SBIC Debentures | 5,275 | 6,558 | 7,621 | 8,988 | 10,300 | 10,870 | 12,121 | 10,997 | 10,882 |
| Disaster | 7,176 | 7,174 | 6,766 | 6,318 | 5,996 | 6,169 | 9,001 | 9,574 | 9,342 |
| Total | 99,439 | 104,253 | 109,758 | 114,796 | 120,867 | 128,726 | 139,369 | 141,440 | 141,586 |

## Number of Loans for Four Major SBA Programs

| Program | FY 2012 | FY 2013 | FY 2014 | FY 2015 | FY 2016 | FY 2017 | FY 2018 | FY 2019 | FY 2020 |
|---|---|---|---|---|---|---|---|---|---|
| 7(a) Regular | 44,358 | 46,389 | 52,044 | 63,460 | 64,074 | 62,431 | 60,353 | 51,908 | 21,983 |
| 504 Regular | 7,047 | 7,708 | 5,885 | 5,787 | 5,893 | 5,952 | 5,693 | 5,933 | 3,456 |
| SBIC Debentures | 62 | 72 | 76 | 69 | 65 | 47 | 58 | 36 | 25 |
| Disaster | 15,330 | 46,826 | 6,244 | 11,448 | 25,235 | 27,264 | 140,249 | 42,399 | 6,063 |
| Total | 66,797 | 100,995 | 64,249 | 80,764 | 95,267 | 95,694 | 206,353 | 100,276 | 31,527 |

## Summary and Conclusions

- Access to finance is a key constraint on growing SME businesses, according to the World Bank, this even though formal SMEs account for more than 90% of all firms and more than half of employment around the world.
- This is true in emerging and developed economies, with SMEs having limited access to capital markets and facing difficulties in obtaining formal finance from lenders such as commercial banks.
- In the face of the various impediments to SME access to credit, however, policy makers can tap a few potential solutions.
- A government-sponsored entity could also provide loans to SMEs that apply for credit from traditional financial institutions, such as commercial banks, or from non-traditional sources, such as CDC and SBICs, following the example set by the SBA in the US.