



# Utilizing the SBA 7(a) Loan Guaranty Program and The Outsourcing Solution

How Community Banks Can Make Safe, Sound, Secure, and Profitable  
Commercial Loans in a Challenging Credit Climate and Uncertain Economic Environment

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# SBA 7(a) Loan Program

How Can Community Banks Increase Lending to Small Businesses and make sound, safe, secure and profitable commercial loans?



## **SBA 7(a)**

### Use Of Proceeds

- Debt Refinance and Restructure
- Permanent W/C
- Business Acquisition
- FFM&E Financing
- Owner-Occupied Real Estate Construction, Acquisition, Expansion & Debt Refinance

# Conventional Loans vs. SBA 7(a) Loans

	Conventional Loans	SBA 7(a) Loans
Interest Rate	Variable or Fixed Rate	Primary Rate based on WSJP or LIBOR
Term Maturity	<b>FFM&amp;E:</b> 5-7 Year Term <b>Real Estate:</b> 5-10 Year Term with Balloon	<b>Working Capital:</b> Up to a 10 Year Term <b>FFM&amp;E:</b> 10 Years or Useful Life <b>Real Estate:</b> Up to a 25-Year Term with no Balloon
Amortization	<b>FFM&amp;E:</b> Typically fully amortizing <b>Real Estate:</b> 15-25 years amortization	<b>FFM&amp;E &amp; Real Estate:</b> Fully amortizing (No Balloons)
Collateral	Typically fully collateralized based on discounted collateral values	Absence of full collateral coverage based on discounted collateral value is acceptable. Loan guarantee covers collateral shortfall.
Covenants	Typical for C&I and Commercial Real Estate transactions	<b>SBA:</b> Acceptable based on lender approval
Fees	Varies based on Loan Type and Competitive Factors	Agency Loan Guarantee Fee
Profitability	<b>Measured primarily by:</b> <ul style="list-style-type: none"> <li>➤ Net Interest Margin &amp; Fee Income</li> <li>➤ Deposits</li> </ul>	<b>Measured primarily by:</b> <ul style="list-style-type: none"> <li>➤ Net Interest Margin (Retained Portion of loan)</li> <li>➤ Non-Interest Fee Income (Secondary Market Sale)</li> <li>➤ Loan Servicing Income &amp; Deposits</li> </ul>

# SBA7(a) Loan Program

## Benefits to Lender

- U.S. Government Guarantee for up to 75% of Loan Amount.  
(↑Yield & ↓Risk)
- Reduced Reliance on Participations while Maximizing Fee Income. Guaranteed Portion of Loan is not subject to the Bank's Legal Lending Limit or Reserve Requirements.
- Expand Market Share / Increase Asset Quality / Reduce Loan Portfolio Credit Risk / Meet CRA Requirements.
- Increased Liquidity & Portfolio Profitability through Secondary Market Sales.
- Substantial "Non-Interest" Fee Income in Year 1 & Annual Servicing Income provides Significant Yield on Invested Funds.

# SBA 7(a) Loan Program

## Benefits to Borrower

### *SBA 7(a) Loan Program*

- Longer Term Financing:
  - Up to 10 Years for Working Capital
  - 10 Years or Useful Life for M&E
  - 25 Years for Real Estate
- No Balloon Provisions
- Reduced Equity and Collateral Requirements
- Consolidated Loan Components
  - Lower Monthly Payments
  - Improved Cash Flow

# Loan Profitability

## SBA 7(a) Loan Sale Illustration

### SBA 7(a) Loan

#### Loan Assumptions

Gross Loan Amount	\$ 1,000,000
Guaranteed Portion Sold (75%)	\$ 750,000
Non-Guaranteed Retained Portion	\$ 250,000
New York Prime	3.25%
Interest Rate Spread	2.75%
Loan Term	25 Years

#### Secondary Market Assumptions

Full Coupon Price	116.00
Less 50% over 110	113.00
<b>Gross Premium at Full Coupon</b>	<b>\$ 97,500</b>
Servicing Retained by Lender	1.00%

#### **Estimated Income Year 1 and On-Going:**

Servicing Income on Sold Portion	1.00%	on \$ 750,000	\$ 7,500
Interest Income On Retained Portion	6.00%	on \$ 250,000	\$ 15,000
Ongoing Annual Income			\$ 22,500
Premium Income First Year Only			\$ 97,500
First Year Total Income			\$ 120,000

#### **Approximate Yield on Retained Loan Balance:**

<i>First Year</i>	\$ 102,500	/	\$ 250,000	= Prime +	37.75%
<i>Ongoing Subsequent Years'</i>	\$ 27,500	/	\$ 250,000	= Prime +	7.75%

# The Outsourcing Solution

## Advantages to Community Banks

### Primary Considerations:

#### Cost Effective

Uncertain Loan Volume

Outsourcing = Fixed Fee or Variable Cost (Reduce or Eliminate Fixed Overhead)

#### Easy to Implement

- No Learning Curve
- Established Processes & Procedures on Day One

#### Industry Expertise

- Strategic Alliance = Industry Expertise on Day One
- Ensure Program Compliance = Reduced Risk to Bank

# The Outsourcing Solution

## Evaluation of Lender Service Provider

### **Lender Service Provider (LSP) Relationship Allows Lender to:**

- Acquire program knowledge and expertise vs. directly hiring and training a staff.
- Carefully manage cost to offer GGLs (Reduce or Eliminate Fixed Overhead!).
- Increase relationship profitability... Significant Non-Interest Income Potential!

### **The Lender should evaluate the LSP to ensure the LSP can:**

- Define Lender's Commercial Lending Strategy & Requirements: Loan Size, Loan Type, Industries Served, Market Area, etc.
- Evaluate LSP's:
  - Knowledge & Expertise
  - Services & Value = Cost
  - Flexibility = Must Adapt to Lender's Requirements: Clear Understanding of the Bank's Credit Culture & Policies

# Recap

## Community Bank's Use of GGL Programs

### **Advantages Offered by GGL**

- Expand the Bank's commercial loan product offerings.
- Expand and diversify the C&I loan portfolio & market share.
- Increase asset quality & reduce portfolio risk.
- Preserve liquidity & enhance profitability.

### **Obstacles**

- Technical and Specific Requirements
- Knowledge and Expertise
- Uncertain Loan Volume
- Fixed Overhead = Staffing & Training Expenses

### **Outsourcing Solution**

- Cost Effective = Reduce or Eliminate Fixed Overhead Through a Variable Cost Structure
- Industry Expertise = Reduced Compliance Risk
- Easy Implementation

# Contact Information

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