Real Deals
SSBCI 2.0 Product Playbook
Bonding + Supply Chain Finance

Drexel’s Nowak Metro Finance Lab & Kauffman Foundation
Executive Summary

Background
The State Small Business Credit Initiative (SSBCI 2.0) is a federal program authorized by the 2021 American Rescue Plan that gives $10 billion to states to create programs that invest in — and help grow — small businesses. Each state is tasked with designing the programs and products that reach a broad range of diverse entrepreneurs from this unprecedentedly large program.

Challenge
How do states structure capital, administer programs, and build the partnerships necessary to successfully leverage this federal investment to create jobs, support businesses, and permanently strengthen their state economies?

Opportunity
Supply Chain Finance (SCF) is an innovative and underutilized approach that states should consider in their SSBCI 2.0 portfolio. SCF ties financing to the promise of future cash flows (e.g., contracts, invoices), providing critical working capital to small supplier (e.g., B2B, B2G) businesses.
About the Nowak Metro Finance Lab

The Nowak Metro Finance Lab is a research lab based at Drexel University to help local governments identify and implement public finance strategies to support strong and inclusive cities and states. The Lab’s current and founding director is Bruce Katz, co-author of The New Localism and The Metropolitan Revolution: How Cities and Metros are Fixing Our Broken Politics and Fragile Economy.

The Lab has partnered with the Ewing Marion Kauffman Foundation to provide free research and support to states as they implement the $10 billion State Small Business Credit Initiative, with the goals of:

1) Strengthening and building local small-business capital ecosystems;
2) Reaching underserved entrepreneurs without access to capital; and
3) Driving catalytic innovation in metropolitan regions and states.
Definitions

**Capital Product:** An agreement wherein one entity or firm invests money into another; examples included loans, equity investments, and other means of extending credit and capital to businesses.

**Supply Chain Finance (SCF):** A capital product that helps businesses access working capital by borrowing against existing customer orders, such as receivables for future work or invoices for goods or services already delivered/rendered.\(^1\)

**Surety Bond:** A form of insurance intended to indicate firms’ ability to undertake and perform work specified in a contract and protect the procurer against non-performance, often required for construction and government-purchased work; typically underwrites against firms’ cash reserves, limiting access.

**Bid Bond:** A subset of Surety Bonds that indicates a firm is able and qualified to perform work, and will perform the work, as specified in a bid if accepted by the procurer.

**Performance and Payment Bonds:** Once a bid is awarded, the Performance Bond gives surety that the contractor will perform and complete the work as specified; the Payment Bond guarantees pay to all entities, most commonly subcontractors and suppliers; both Bonds are subsets of Surety Bonds.

\(^1\) Aunnie Patton Power’s *Adventure Finance* (2021) helped guide these definitions
Typical Bond Structure & Agreement
Limits Access for Small and Underrepresented Firms

**Policy Objective:**
Public agency aims to expand S/WMBE participation in procurement.

**Policy Challenge:**
Bonding capacity primarily depends on cashflow, a limiting factor for S/WMBEs.

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1. Requires bond
2a. Surety fee
2b. Underwrites bond
3. Performs work

- **Procurer:** i.e., public agency
- **Supplier:** S/WMBE firm
- **Surety Company:** bond issuer guarantees supplier’s work

If applicable:
Pays out in event of non-performance

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**Ex:** NY State Bond Guarantee Assistance Program

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Nowak Metro Finance Lab
Lindy Institute for Urban Innovation
SSBCI Bond Guarantee Program Structure
Guarantees Up to 80% of Bonds to Expand Access

**Policy Objective:**
Public agency aims to expand S/WMBE participation in procurement.

**Policy Challenge:**
Bonding capacity primarily depends on cashflow and liquid assets, a limiting factor for S/WMBEs.

**Policy Tool:**
SSBCI-supported bond assistance program guarantees up to 80% of project cost, lowering risk to surety and making bond more accessible to S/WMBE contractors.

**Ex:** NY State Bond Guarantee Assistance Program
Sample Deal: SSBCI Bond Guarantee Program
Sample Deal + Fund Structure

1. Bid Bond:
- S/WMBE is looking to begin contracting
- Firm has $10,000 in current assets
- 10x assets industry standard for bond capacity

$100,000 capacity

10x Assets

$10,000

Firm ineligible w/- SSBCI Guarantee

Firm becomes eligible w/ SSBCI Guarantee

$150,000 capacity

2. Performance/Payment Bond:
- S/WMBE wins $125,000 contract
- Needs Performance Bond

$125,000 contract

30% / $37,500 SSBCI Bond Guarantee

$100,000 = Previous Bonding Capacity

$25,000 Remaining Bid Bond Capacity

$10M SSBCI Guarantee Pool

Bid, Performance, & Payment Bonds @ Surety Companies
Supply Chain Finance in Action
Funds Administrator Model w/ Invoice Payment

**Need:** government can take as long as 90 days after work is completed to pay contractor invoices

**Opportunity:** new federal infrastructure dollars could boost local, diverse firms if correctly channeled

**Solution:** create capital products and vehicles to front payment for contractor invoices and other SCF mechanisms to smooth small business cashflow

**Ex:** LA’s Contractor Development and Bonding Program

**SCF works best at scale:** financier gets surety doing all contracts for city/region, keeps % cut low with volume

**Revenue-Based Integration:** can also be structured as full payment with revenue-based repayment (i.e., repaid when government pays contractor); See our Revenue-Based Lending deck for more
Supply Chain Finance in Action
SSBCI Integration

Loan Guarantee Program: SSBCI Guarantees Financier against losses

Capital Access Program: SSBCI creates loan loss reserve for financier, up to 14%

Loan Participation Program: SSBCI buys into existing/new Funds Administrator w/ new capital

Collateral Support Program: SSBCI deposits enhance surety, allow for earlier payment of receivables, not just invoices

SSBCI benefits: financiers have additional support + reserves to test SCF/Funds Administrator model
Supply Chain Finance in Action
Line of Credit Model, as % of Contract

Product: Working Capital Loan/LOC for 20% of contract value
Benefit: Firm now has cashflow/working capital to meet project costs

Key Innovation: concurrent bond and LOC approval integrating bonding and financing functions reduces costs + risk
Supply Chain Finance in Action
Significant Ecosystem Benefits across Parties

To Government: many more tools and much larger reach in reaching and growing local, S/WMBE firms

To Local S/WMBEs: contracts and predictable revenue now available, offering significant growth opportunities, expanding access and equity

To Capital/Surety Providers: more lending/insurance capability + market reach w/ SSBCI enhancements; extensive cost savings and risk-mitigation w/ integrated bonding + lending functions; and now an incentive to provide pre and during-contract TA

Removes Silos, Expands Access, Grows Underrepresented Firms
## Pros/Cons for SSBCI Programs

### By Bonding and SCF Integration

<table>
<thead>
<tr>
<th>Product</th>
<th>Pros</th>
<th>Cons</th>
<th>Reach/ Ideal Business</th>
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<tbody>
<tr>
<td><strong>Loan Guarantee Program (Bonding + SCF)</strong></td>
<td>- Pools guarantees</td>
<td>- Does not address capital or firm assets shortfall</td>
<td>High: Lender/surety can get significant first-loss coverage; Business has some assets, needs modest capital</td>
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<td>- Enables large number of transactions</td>
<td>- Relatively less credit extended per transaction</td>
<td>Limited: Minimal loan coverage, but works for small firms on edge (many S/WMBE; easiest to implement w/local lenders/CDFIs</td>
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<td>- Up to 80 percent covered, first-loss capital</td>
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<td>Moderate: Balance sheet expansion for lender; business often already has assets, some access to credit</td>
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<td><strong>CAP Loan Loss Reserve (Bonding + SCF)</strong></td>
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<td>- Limited risk mitigation (14%)</td>
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<td>- Borrower/lender must pay in</td>
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<td>- Low SSBCI match (1:1 max)</td>
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<tr>
<td><strong>Loan Participation Program (SCF)</strong></td>
<td>- Gets capital directly to lenders (up to 80% of fund)</td>
<td>- Possibly more underwriting</td>
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<td>- Expands CDFI balance sheets + capital to lend</td>
<td>- Typically required personal guarantees</td>
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<tr>
<td><strong>Collateral Support Program (Bonding + SCF)</strong></td>
<td>- More financing per transaction</td>
<td>- Cannot pool SSBCI funds for more transactions</td>
<td>High: Effectively addresses asset shortfall for both bonds and lending; business growing into first/larger contract</td>
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<td>- Easy utilization for community lenders</td>
<td>- Thus enables fewer new transactions overall</td>
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<td>- Deposit could also be considered equity in firm</td>
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*SSBCI capital could participate in theory in a bonding portfolio, meeting capital at risk requirement; we are yet to see or investigate this integration*
SSBCI + Patient Capital Integration
Product 1a: Enhanced Bond Guarantees
Patient Capital with SSBCI Fund Structures

Bonding Fund Structure 1 – SSBCI Guarantee

SSBCI Guarantee

SSBCI Guarantee Pool

Guaranteeing Portion of Bid, Performance, & Payment Bonds @ Surety Companies

Bonding Fund Structure 2 – SSBCI Collateral Support

SSBCI Collateral Support

SSBCI Collateral Fund

Depositing Collateral to Enhancing Bid, Performance, & Payment Bonding Capacity w/ Surety Companies

Opportunities for Philanthropic + Patient Capital
Structure 1 – Guarantee Program

$170,000 capacity

$100,000 capacity

Now 17x Assets

30% SSBCI Guarantee

10x Assets

$10,000

$10,000

10% Patient Guarantee

Additional Bonding Capacity

$100,000

$170,000

$10,000
Product 1b: Bond Collateral Deposits
Patient Capital with SSBCI Fund Structure

**Bonding Fund Structure 1 – SSBCI Guarantee**

- **SSBCI Guarantee**
- **SSBCI Guarantee Pool**
- Guaranteeing Portion of Bid, Performance, & Payment Bonds @ Surety Companies

**Bonding Fund Structure 2 – SSBCI Collateral Support**

- **SSBCI Collateral Support**
- **SSBCI Collateral Fund**
- Depositing Collateral to Enhancing Bid, Performance, & Payment Bonding Capacity w/ Surety Companies

**Opportunities for Philanthropic + Patient Capital**

Structure 2 – Collateral Support

- *Deposit could be considered equity in business; see our Alternative Equity deck*

- $100,000 capacity
- Further Bonding Capacity
- $10,000 assets
- 10x assets
- Deposit $10,000

**Role for patient capital:** 1) further enhance bonding and/or 2) fill asset shortfalls

- Patient Capital Deposit
- $200,000 capacity
- $10,000 at 10x
- $100,000 at 10x
Product 2a: Enhanced SCF Funds Administrator
Patient Capital with SSBCI Fund Structure

Role for Patient Capital w/ Funds Administrator:

- Fund pre-contract TA for bonding support
- Buy down interest/fee payments
- Fund during-contract programmatic support
- Fund pilots w/ first-in/first-loss structure (LGP, CAP, LPP, CSP) for Funds Administrator
Product 2a: Enhanced SCF Working Line of Credit
Patient Capital with SSBCI Fund Structure

Individual Product

Total Project Cost
Total Capital Needed over Course of Project

X% Working Capital Line of Credit
Other Capital: senior debt, future project revenues

Current Assets

SSBCI Credit Enhancement Products

1) SSBCI Loan Guarantee

Total Loan Amount
SSBCI Guaranteed Portion
Additional Credit Enabled

2) SSBCI Loan Participation

Total Loan Amount
SSBCI Purchased Portion
Additional Credit Enabled
Product 2b: SSBCI Supply Chain Finance
Fund Structure(s) + Patient Capital

Individual Product

- Total Project Cost
- Total Capital Needed over Course of Project
- Working Capital
- Line of Credit
- Other Capital: senior debt, future project revenues
- Current Assets

SSBCI Credit Enhancement Products

3) SSBCI Collateral Support*
- Total Loan Amount
  - SSBCI Deposit
    - Lender + Borrower
    - Contribution to Reserve Fund
  - Additional Credit Enabled

4) SSBCI Loan Loss Reserve
- Total Loan Amount
  - Lender + Borrower
    - Contribution to Reserve Fund
  - Additional Credit Enabled

*Collateral Support would likely happen at front end as bonding support, with the firm then approved for the line of credit with bond approval.
Summary of Patient Capital Opportunities

**Supportive Direct Investment:**

- Offer additional guarantees and collateral support for SSBCI bonding products
- Provide first-in/first-loss credit enhancements for SCF, across SSBCI programs
- Target and test specific funds and models with a regional focus to lower capital cost w/ scale

**Capacity-Building and Ecosystem Support:**

- Fund Pre-Contract TA + programmatic support to build more diverse contractor pipeline
- Fund During-Contract TA and Funds Administrator support to defray staffing costs and thereby lower cost of capital
Recommendations for States

1. **Review your Treasury application** for possible Bonding + SCF integration within your approved programs

2. **Contact your local lenders and surety companies** to assess current practice and capacity for SCF lending and bonding support programs

3. **Check out the Innovative Finance Project**, a Nowak Metro Finance Lab collaboration with Catalyze to identify and scale innovative financial products; resources include:
   - SCF case studies and examples
   - Lending guidelines and best practices
   - Trainings and webinars

4. **Reach out to the Nowak Lab** for more information: bryan.jeffrey.fike@drexel.edu
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