



Real Deals

SSBCI 2.0 Product Playbook

Revenue Based Loans

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, reach and support businesses, and **permanently** strengthen their state economies?*

Opportunity

***Revenue Based Loans (RBL)** is an innovative and underutilized financial product that states should consider in their SSBCI 2.0 portfolio. RBL offers more flexible repayment, aligns incentives between founders and funders, and allows a broader range of ventures to grow early in their lifecycle — maximizing chances of success and repayment.*

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.*

Term Loan: *A capital product where a lender provides a one-time lump sum of money that is generally repaid in fixed dollar amounts over the life of the loan. The fixed amounts do not change based on the borrower's monthly revenues (examples: traditional home loans; SBA 7(a) and 504 loans).*

Revenue-Based Loans: *A loan product where a lender provides a one-time lump sum of money that is repaid from a fixed percentage of the borrower's revenue* until an agreed-upon multiple of the initial investment is met, usually between 1.5 and 3x. While this type of financing can be more costly overall, it allows flexibility, mission-alignment, and other benefits in reaching more diverse firms and entrepreneurs.*

* "revenue" can mean: EBITDA (earnings before interest, taxes, depreciation, and amortization), Free Cash Flow ("FCF"; i.e., EBITDA + CapEx), and other variations

Example Deal

Sonoran Precision Agriculture (Hypothetical)

Business Background: Founded by a first-generation college student and a business partner, the company serves independent farmers with mapping, automated fertilizer spreading, and data analytics to help maximize farms' harvest yields

Revenue Profile: As a new business supporting small farms, revenues are modest and seasonal based on the growing season, with several large recurring customers and few assets except some equipment

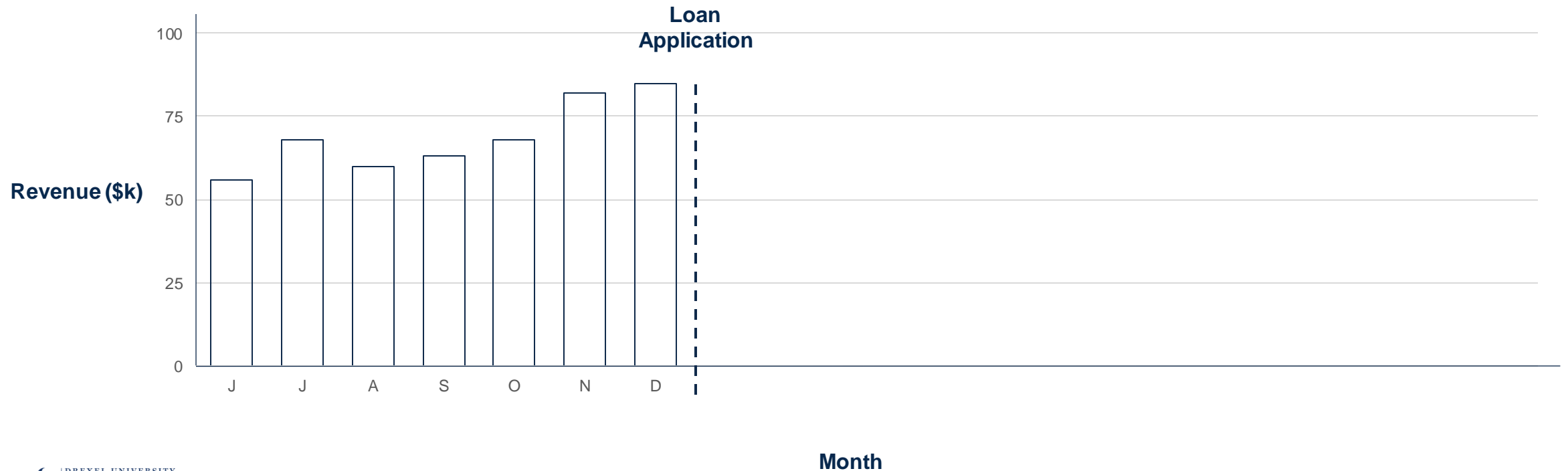


Example Deal – Loan Profile

Sonoran Precision Agriculture (Hypothetical)

Business/Loan Profile

Avg. monthly revenue: \$70,000
Collateral: None
Use of Proceeds: Hiring, software

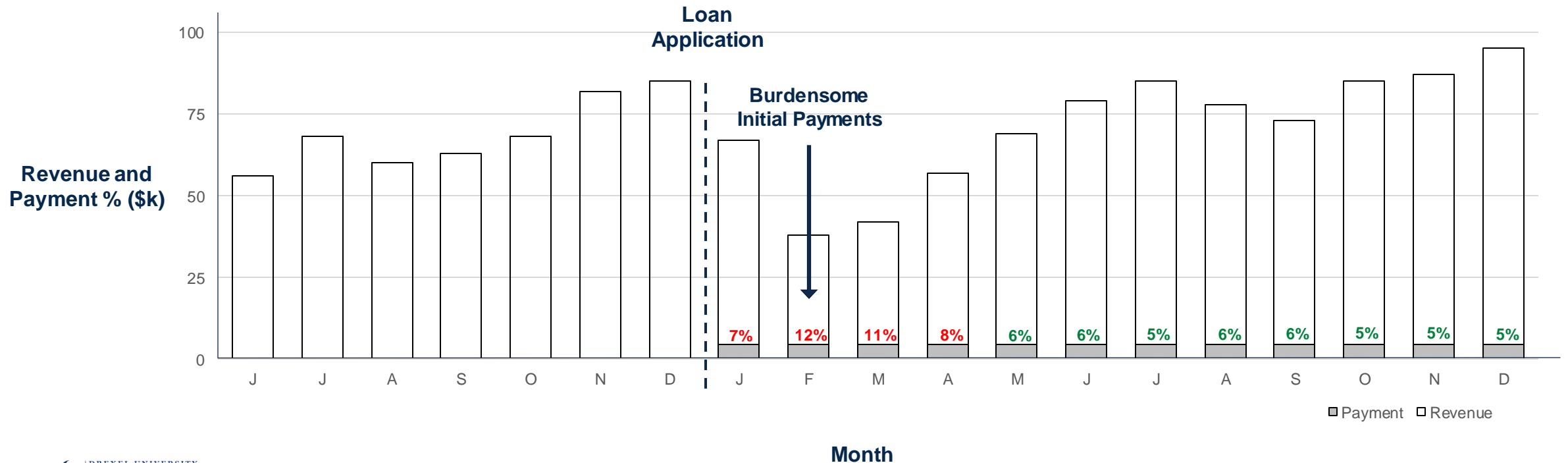


Example Deal – Term Loan

Sonoran Precision Agriculture (Hypothetical)

Traditional Term Loan

Principal: \$200,000
 Term: 5-year term
 Interest Rate: 12%
 Monthly Payment: ~\$4,450

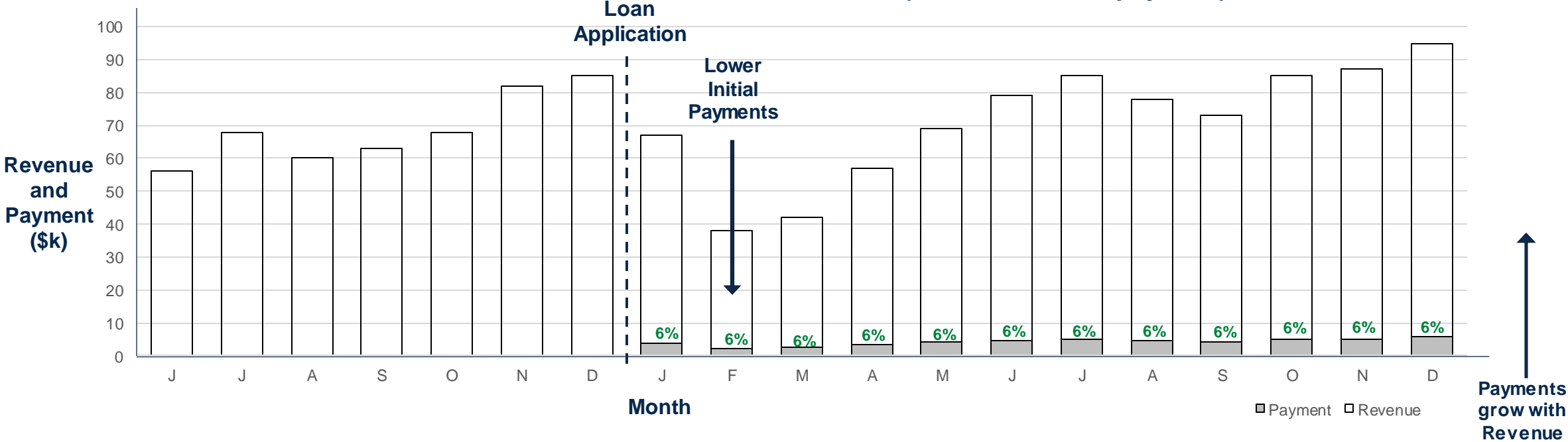


Example Deal – Revenue-Based Loan

Sonoran Precision Agriculture (Hypothetical)

Revenue-Based Loan	
Principal:	\$200,000
Term:	5-year term
% Monthly revenue:	6%
Repayment Cap:	1.5x principal

Gross Revenue By Month
(% share = loan repayment)



Side-by-Side: Term vs. Revenue-Based Loan

Sonoran Precision Agriculture

Term Loan

Principal: \$ 200,000

Total payment: \$ 266,933

First 12 months: \$ 53,386

Costs/Benefits:

- Less expensive capital overall
- Burdensome early on for borrowers
- Less flexibility for seasonality
- Collateral or personal guarantees
- Simple monthly payment calculation

Revenue-Based Loan

Principal: \$ 200,000

Total payment: \$ 300,000

First 12 months: \$ 51,300

Costs/Benefits:

- Higher total interest paid
- More affordable in early stages
- Flexibility if/when revenue decreases
- No collateral or personal guarantees
- More revenue analysis for borrower

Summary of Benefits of RBL

RBL Features	Pros	Cons	Example
No Collateral/Guarantee	<ul style="list-style-type: none"> ➤ Collateral requirements are a key hurdle underrepresented founders ➤ Protects founders against personalized, catastrophic downside risks 	<ul style="list-style-type: none"> ➤ Requires more up-front lender diligence ➤ More industry-wide training needed 	Latino food entrepreneur using ghost kitchen with few assets or savings can move from simple delivery to brick-and-mortar space
High-touch	<ul style="list-style-type: none"> ➤ Lender gets deep insight into business, can flag issues well before late payment ➤ Entrepreneurs gain significant knowledge w/ cashflow analysis 	<ul style="list-style-type: none"> ➤ Requires more staff resources from lender ➤ Servicing payment requires access to financials and relatively sophisticated software 	Entrepreneur now documents free cashflow and has more precise understanding of how much capital they can reinvest into their business and anticipate trends in future revenue
Flexible payment	<ul style="list-style-type: none"> ➤ Great for seasonality, accommodates decrease revenue with lower APR ➤ Quicker pay-off with business success and growth 	<ul style="list-style-type: none"> ➤ IRR increases with revenue growth, must create protection for borrower, usury regulations ➤ With flexibility comes (typically) higher cost of capital overall 	After the busy holiday season, repayment for entrepreneur will decrease as demand and orders recede; value of RBL payments decrease proportionally, then rise w/ summer season growth
Mission-Alignment	<ul style="list-style-type: none"> ➤ Creates incentive for lender to support business success ➤ Can recycle funds more quickly into more lending 	<ul style="list-style-type: none"> ➤ Requires sophisticated staff and continuing resources ➤ Requires mission-driven lender to uphold non-usurious standards 	Business accelerates and repayment total to quickly reach 1.5x multiple two years into five-year term, with help from capital provider

RBL-SSBCI Program Integration

Program Options with Revenue Based Loans

Four options for SSBCI-supported loans, per Treasury's SSBCI capital guidelines:

1. Capital Access Programs (CAPs)

- Loan loss reserves, w/ borrower and/or lender contributing up to 7 percent of loan amount to reserve fund, matched by state with SSBCI funds, totaling 14 percent

2. Loan Guarantee Programs (LGPs)

- State SSBCI funds guarantee between 20 and 80 percent of an enrolled loan

3. Collateral Support Programs (CSPs)

- States SSBCI funds provide cash to increase the value of borrowers' available collateral

4. Loan Participation Programs (LPPs)

- State SSBCI funds purchase a portion of loan or make direct companion loan alongside private lender

SSBCI Program Integration

Overview of Revenue-Based Products Possible with SSBCI

Product	Pros	Cons	Reach
Loan Loss Reserve (CAP)	<ul style="list-style-type: none"> ➤ Most familiar to CDFIs ➤ Most effective for reaching LMI businesses in SSBCI 1.0; extending credit to new borrowers 	<ul style="list-style-type: none"> ➤ Limited risk mitigation (14%) ➤ Borrower/Lender must pay in ➤ Low SSBCI match (1:1 max) ➤ Requires full portfolio of loans 	Moderate
Loan Guarantee (LGPs)	<ul style="list-style-type: none"> ➤ First-loss guarantee capital ➤ Covers up to 80% of loan ➤ Creates room for experimentation in building RBL best practices 	<ul style="list-style-type: none"> ➤ Less familiar to CDFIs ➤ CDFIs still need capital, does not expand existing balance sheet 	High Potential
Collateral Support (CSPs)			N/A – Not Collateralized
Loan Participation (LPPs)	<ul style="list-style-type: none"> ➤ Gets capital directly to lenders (up to 80% of fund) ➤ Expands CDFI balance sheets/lending capacity 	<ul style="list-style-type: none"> ➤ Possibly more underwriting ➤ Purchase standards may be too rigid, esp. for RBL ➤ Typically require personal guarantees (a la SSBCI 1.0) 	Lower

RBL Fund-Level Outcomes

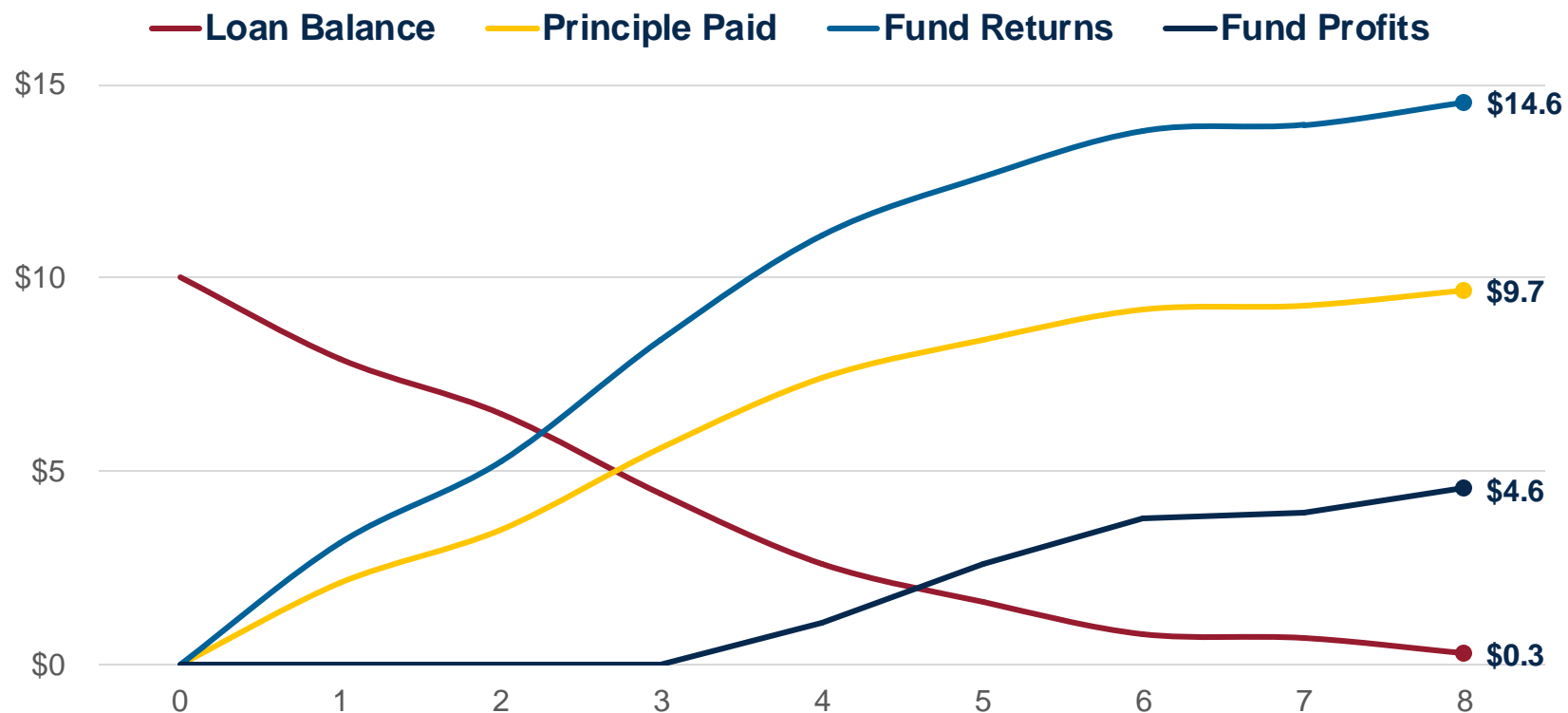
For modest estimates of an overall fund portfolio revenue growth of 1.5%

Business Performance	Proportion of Fund (\$)	Revenue Growth	Avg. Repayment Year	Effective APR	Year 8 Loans Outstanding*
Strong	15%	+20%	4	19.2%	0%
Moderate	30%	+10%	4.8	17.3%	0%
Weak	30%	+0%	5.8	15.2%	25%
Troubled	20%	-10%	8	12.5%	100%
Failed	5%	-50%	--	NA	0%
Fund Average	--	1.5%	5.6	15.9%	28%

* 28% of loans still have balance after Year 8; this represents only 3% of overall loan payments/principal

RBL Fund Returns

Mapping Repayments, Returns, and Profits over an 8-Year Timeline



Fund Profile:

- \$10 million fund
- \$200,000 avg. loan
- Assumes 3% of funds outstanding, per previous slide

Insights:

- Breakeven in Year 3
- Achieves close to 1.5x portfolio return
- Does not show reinvested funds (i.e., conservative returns estimate)

Opportunities for Patient Capital w/ RBL & SSBCI

Supportive Direct Investment:

- Cover lender/borrower portion of required SSBCI 1:1 match in CAP Loan Loss Reserves
- Expand 1:1 match on SSBCI Loan Loss Reserve (e.g., Colorado bonus in Enterprise Zones)
- Invest capital into SSBCI Guarantee Programs, growing CDFI/local lending capacity **high potential**
- Provide first-loss capital in an SSBCI Loan Participation, incentivizing private participation

Capacity-Building and Ecosystem Support:

- Fund training for RBL underwriting, loan servicing, and implementation; including supplier capital , underwriting against contracting revenue/opportunities (see our SCF deck)
- Fund development of RBL software, subscriptions, and access for local lenders

Recommendations for States

1. ***Review your Treasury application*** for possible RBL integration within your approved programs
2. ***Contact your local lenders and business service providers*** to assess current practice and capacity for RBL lending
3. ***Check out the Innovative Finance Project***, a Nowak Metro Finance Lab collaboration with Catalyze to identify and scale innovative financial products; resources include:
 - ***Sample term sheets for RBL***
 - ***Lending guidelines and best practices***
 - ***Trainings and webinars***
4. ***Reach out to the Nowak Lab*** for more information: bryan.jeffrey.fike@drexel.edu

Contact

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