



April 2011

Community Affairs  
Department

## SBA's and Export-Import Bank's Working Capital Loan Guarantee Programs

### Abstract

This Insights report highlights two federal loan guarantee programs that help lenders and business borrowers finance the export of goods and services. The U.S. Small Business Administration (SBA) Export Working Capital Program (EWCP) and the Export-Import Bank of the United States (Ex-Im Bank) Working Capital Guarantee Program (WCGP)<sup>1</sup> work in a complementary fashion to guarantee loans made by commercial lenders to qualified exporters. The SBA program guarantees loans up to \$5 million; the Ex-Im Bank program has no maximum loan limit. Originating lenders benefit from loan guarantees that protect against much of the credit risk associated with export working capital lending. These products offer lenders the opportunity to develop or expand relationships with small businesses and can open the door to lenders selling a broader array of financial products to customers. Loans under these programs that meet the Community Reinvestment Act (CRA) criteria of small business loans or community development loans may be considered in an institution's CRA examination. By guaranteeing trade finance loans, the two programs help the National Export Initiative fulfill its goals to add jobs to the U.S. economy and double exports over five years.<sup>2</sup>

### I. What Are the Programs?

The SBA's EWCP and the Ex-Im Bank's WCGP work similarly and, in fact, even use the same application form. Both programs support small businesses that need working capital to finance export sales. They share a common goal: to ensure that qualified small business exporters do not lose potential sales because of a lack of working capital. Both programs rely on commercial lenders to originate and service loans backed by federal guarantees to qualifying U.S. businesses. This *Insights* report explains how the programs work and several key differences between the programs.

Each program provides 90 percent guarantees on loans made by financial institutions to exporters refinancing existing debt or providing working capital for the production and sale of export goods and services. Acceptable collateral for such loans includes raw materials, work in progress, finished goods (up to 75 percent of value), and export or foreign accounts receivable (up to 90 percent of value).

In fiscal year 2009, the SBA's EWCP guaranteed 142 loans for a total of \$130 million.<sup>3</sup> That same year, the Ex-Im Bank's WCGP authorized \$1.5 billion—with \$1.2 billion of that in loans to small

<sup>1</sup> The Ex-Im Bank and the SBA have other programs that support U.S. exports, see [www.sba.gov](http://www.sba.gov) and [www.exim.gov](http://www.exim.gov) for more information.

<sup>2</sup> For more information on the National Export Initiative, see [www.trade.gov/nei/](http://www.trade.gov/nei/).

<sup>3</sup> Data provided by SBA staff on November 1, 2010.

businesses. The Ex-Im Bank's program authorized 473 loans, including 427 that directly benefited small businesses and represented more than 90 percent of the program's total transactions.<sup>4</sup>

Both agencies have the authority and capacity to expand their trade finance support. The Ex-Im Bank's charter limits its portfolio of loans, guarantees, and insurance to \$100 billion,<sup>5</sup> and its total portfolio was \$75 billion at the end of fiscal year 2010.<sup>6</sup> As a self-sustaining agency, the Ex-Im Bank and loan commitments made by its credit programs are not subject to the availability of annual appropriations.

The SBA does not have a mandated maximum on the total portfolio of loan guarantees it can extend under its 7(a) Loan Program, which includes the EWCP.<sup>7</sup> Recent legislative changes more than doubled the program's maximum loan size and the maximum guarantee available.<sup>8</sup> Both agencies are focused on expanding their support of U.S. exports to help fulfill the goal of the National Export Initiative.

## **How Do Lenders Participate?**

The Ex-Im Bank's WCGP requires lenders to complete an Ex-Im Bank training program and meet the prerequisite number and type of loan facilities to become Delegated Authority lenders. This allows lenders to make guaranteed loans without submitting the loans for pre-approval by the Ex-Im Bank. Financial institutions may participate without having delegated authority, but Ex-Im Bank loan specialists must underwrite the loans for approval.<sup>9</sup>

The SBA's EWCP lenders can receive delegated approval authority under the Preferred Lending Program (PLP). Lenders that already have PLP status for domestic lending under the SBA's 7(a) program are eligible to apply for PLP status under the EWCP as well. PLP lenders underwrite EWCP loans and submit them to the SBA's PLP Processing Center where the loans, without review or supplemental underwriting, are assigned the loan numbers the lenders need to disburse loan proceeds to borrowers. This approval process typically takes only one or two days. When lenders use the program without having PLP status, SBA senior international trade and finance specialists underwrite the loans and submit them to the general Lender Processing Center for underwriting review, approval, and loan number. This process usually takes five to 10 days.

Both programs require lenders to complete for each transaction a "Joint Application for Export Working Capital Guarantee,"<sup>10</sup> as well as any supporting documentation required by the SBA or Ex-Im Bank programs.

The programs also require financial institutions to originate loans and to service them for the life of the loans. While the guaranteed portion of the loans, technically, can be sold on the secondary market, in practice this has not occurred due in part to the short term and nonstandardized nature of the loans. Whether loans are retained or sold, financial institutions must retain loan servicing responsibilities and the nonguaranteed portion of the loans on their books.

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<sup>4</sup> The Ex-Im Bank's 2009 Annual Report, [www.exim.gov/about/reports/ar/ar2009/index.html](http://www.exim.gov/about/reports/ar/ar2009/index.html).

<sup>5</sup> The Ex-Im Bank charter, [www.exim.gov/about/charter/index.cfm](http://www.exim.gov/about/charter/index.cfm).

<sup>6</sup> The Ex-Im Bank's 2010 Annual Report, [www.exim.gov/about/reports/ar/2010/exim\\_2010annualreport.pdf](http://www.exim.gov/about/reports/ar/2010/exim_2010annualreport.pdf).

<sup>7</sup> SBA's 7(a) Loan Program receives annual appropriations.

<sup>8</sup> The Small Business Jobs Act of 2010, enacted September 27, 2010 (Public Law 111-240), includes a broad range of initiatives that seek to increase support for small businesses and increase the number of jobs in the U.S. economy. Among other things, the act significantly increases the maximum loan size for all SBA 7(a) loans, including EWCP loans, to \$5 million. It also increases the maximum guarantee for EWCP loans to \$4.5 million, or 90 percent of the \$5 million allowable maximum.

<sup>9</sup> The Ex-Im Bank's WCGP forms, [www.exim.gov/tools/appsforms/workcap.cfm](http://www.exim.gov/tools/appsforms/workcap.cfm).

<sup>10</sup> The joint application form, [www.sba.gov/sbaforms/sba84-1.pdf](http://www.sba.gov/sbaforms/sba84-1.pdf).

## **II. Why Should Financial Institutions Be Interested in These Programs?**

### ***Market Conditions***

Historically, government guaranteed loan programs have been important tools for providing loans to customers who do not meet conventional underwriting criteria. Loans to small business exporters, especially new customers and those entering the international marketplace or expanding their export activities to new markets, often fit this description. As small businesses work to recover from the recent economic downturn by expanding into new markets, the SBA's EWCP and Ex-Im Bank's WCGP may be useful tools for reaching new customers.

### ***Expand Relationships With Existing Customers***

The OCC's conversations with participating lenders suggest it is not uncommon for financial institutions to have relationships with small business borrowers and not realize that these customers are also exporters. Consequently, the company's banker may not have known that the company might be eligible for government-guaranteed working capital loans available from the SBA and Ex-Im Bank programs. This is particularly true for indirect export businesses that do not ship products overseas directly. These exporters may sell products to other U.S.-based businesses that resell products overseas or use the products as inputs for other products sold overseas. As long as the products financed are ultimately exported, the SBA's EWCP and Ex-Im Bank's WCGP can provide financing. These programs help financial institutions expand relationships with existing customers and help borrowers expand their businesses.

### ***New Business Development Opportunities***

The 90 percent government guarantees provided by the SBA and Ex-Im Bank programs allow lenders to use as loan collateral raw materials, work in progress, and finished goods used in the production of an export. The programs may allow financial institutions to have relationships with new customers that might not be immediately bankable absent the guarantees.

Additionally, financial institutions report customers using loans obtained through the SBA and Ex-Im Bank programs often expand and maintain banking relationships with these lenders. Borrowers also may require working capital loans for domestic production, construction loans, payroll accounts, credit cards, and other personal banking relationships.

### ***Profitability***

The federal guarantee offered by these programs may boost profitability for participating financial institutions while minimizing credit risk. Loans and fees for these programs are negotiable between the borrower and the lender. Neither the EWCP nor the WCGP have mandated caps on interest rates or fees on loans.

### ***Mitigating Risk***

The SBA's EWCP and the Ex-Im Bank's WCGP each provide a 90 percent federal guarantee on working capital loans for the production and sale of export goods. When a loan defaults, a lender must follow the programs' detailed procedures to make a claim on the guarantee.<sup>11</sup> Generally, a lender is expected to liquidate any available collateral pledged for the loan (as is the case with SBA loans), but under the WCGP the lender may elect to assign to the Ex-Im Bank all of its rights, title, and interests in the loan and have Ex-Im Bank liquidate the collateral. To the extent that the guarantee claim is approved, which is generally the outcome if a lender follows the programs' requirements in making and servicing the loan, any remaining unpaid principal and interest on the guaranteed portion of the loan will be remitted to the lender on a pro-rata (typically 90 percent) basis.

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<sup>11</sup> Guidelines for the Ex-Im Bank's WCGP are in the WCGP Manual, [www.exim.gov/pub/pdf/ebd-w-15.pdf](http://www.exim.gov/pub/pdf/ebd-w-15.pdf). The SBA's EWCP guidelines are in the "Lender and Development Company Loan Programs" SOP 50-10(5), [www.sba.gov/about-sba-services/7481](http://www.sba.gov/about-sba-services/7481).

### ***Legal Lending Limits***

Some community and midsize financial institutions with smaller legal lending limits may find the SBA's EWCP and Ex-Im Bank's WCGP helpful in expanding commercial lending. In accordance with 12 CFR 32, the federally guaranteed portion of the guaranteed loan does not count toward the institution's legal lending limit to one borrower. By utilizing these programs, lenders may make larger loans to individual customers than they might otherwise be able to provide. The amount applied against the institution's legal lending limit is the unguaranteed portion of the loan.

### ***Capital Requirements***

The federal guarantees lower a lender's risk-weighting for capital reserve requirements. In either program, the capital risk weight is "preferred"—much lower than for unguaranteed loans.<sup>12</sup>

### ***Community Reinvestment Act***

Loans made through the Ex-Im Bank and SBA programs have the potential to receive CRA consideration as either a loan to a small business or a community development loan, provided they meet the geographic requirements of the CRA regulation. For example, the CRA examination for institutions evaluated under the large bank test includes a review of small business loans that meet the definition of "loans to small business" on the Consolidated Report of Condition and Income.<sup>13</sup> Loans of over \$1 million in amount may qualify as community development loans if they meet the CRA definition of community development.

In contrast, institutions evaluated under the small and intermediate small bank tests receive CRA consideration for business loans of any amount that finance small businesses, which are loans to businesses with gross annual revenues of \$1 million or less. Intermediate small banks may opt to have business loans of any amount that meet the definition of community development considered as either business loans under the lending test or community development loans under the community development test.

For all banks, providing technical assistance on financial matters to small businesses qualifies as a community development service. For example, banks may provide assistance to small businesses in preparing loan application packages for submission to local, state, or federal government agencies.

For additional information and guidance on CRA, refer to the regulations and the Interagency Questions and Answers on CRA.<sup>14</sup>

## **III. How Do the Programs Work?**

The programs are designed to support exporters faced with a significant time period between when sale contracts are executed, deliveries are made, and payments are received. The guaranteed loans are akin to working capital loans for domestic borrowers. Examples include exporters selling manufactured goods or exporters selling services that take a significant period of time to deliver. Working capital loans help exporters cover their production costs until they receive payments, especially in situations when it is not possible or advantageous for exporters to cover these costs with internal resources.

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<sup>12</sup> The SBA and the Ex-Im Bank guarantees to the lender are "conditional" based on the lender following certain requirements established by the programs. Thus, the guaranteed portion of a loan receives a 20 percent capital risk weighting and the unguaranteed portion receives a 100 percent risk weight. For more information on capital reserve requirements for guaranteed loans per 12 CFR 3, see Appendix A to Part 3—Risk-Based Capital Guidelines, accessed November 19, 2010, <http://ecfr.gpoaccess.gov/cgi/t/text/text-idx?c=ecfr&sid=e801422230c9c4484be778c7eb36094d&rgn=div5&view=text&de=12:1.0.1.1.3&idno=12#12:1.0.1.1.3.5.4.9.1>.

<sup>13</sup> Loans to small business are defined as those with original amounts of \$1 million or less and that are reported as "loans secured by nonfarm or nonresidential real estate" or "commercial and industrial loans" in Part I of the Call Report.

<sup>14</sup> Interagency Questions and Answers on CRA, [www.occ.gov/news-issuances/federal-register/75fr11642.pdf](http://www.occ.gov/news-issuances/federal-register/75fr11642.pdf).

Small business exporters, particularly those starting new lines of business or working with new customers, may have difficulty accessing working capital loans sufficient to meet their needs. Lenders may be understandably cautious about approving loans where repayment is based on future payments by foreign companies. For this reason, the federal guarantee that protects lenders is particularly beneficial for export working capital lending.

Appendix A shows a table that lists the key aspects and costs of the SBA's EWCP and the Ex-Im Bank's WCGP. Both programs are based on working capital loans for exporters, which can be revolving lines of credit or single transactions. Loan terms are generally for one year, although under the EWCP program loans may be renewed annually for up to three years and under the WCGP the term of the loan may be up to three years if certain conditions are met.<sup>15</sup> Loans are generally held in the portfolios of originating lenders as currently there is no secondary market for these loans.

Appendix B details a hypothetical loan made under the Ex-Im Bank's WCGP (the process would be practically identical under the SBA's EWCP). Appendix C compares the fee structure for a hypothetical loan by each program.

The following are key differences between the Ex-Im Bank's WCGP and the SBA's EWCP:

- WCGP has no cap on the size of the loan or guarantee; EWCP has a maximum loan of \$5 million and a maximum guarantee of \$4.5 million.
- WCGP has somewhat higher fees for lenders and borrowers than EWCP (see Appendix C for details).
- WCGP requires that financed exports contain U.S. content greater than 50 percent. The program generally cannot finance the export of military defense items or exports to a military buyer. The EWCP does not have these limitations, but buyers of military products must be properly licensed.
- Both programs offer streamlined procedures for preferred lenders—that is, DA<sup>16</sup> for WCGP and PLP<sup>17</sup> for EWCP. The delegated authority program is the primary channel for WCGP loans while the PLP program is less frequently utilized for EWCP. The SBA is encouraging more lenders to participate in the PLP program.

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<sup>15</sup> A WCGP revolving loan facility may be committed for a term of up to three years, provided (1) the lender is also committing to provide the borrower with a domestic revolving credit facility for the same term, and (2) it is common practice for the lender to extend loans with such terms.

<sup>16</sup> To become a delegated authority lender under the Ex-Im Bank's WCGP, typically a lender must at all times employ at least two authorized officers who have completed the Ex-Im Bank Delegated Authority Training Course (a three-day course), or any Ex-Im Bank-approved alternate training course, and have successfully transacted at least two Ex-Im-WCGP loans. Requirements vary for "Community-Level Lenders" (with assets under \$500 million, serving a single market area, and meeting other requirements), and there are different tiers of delegated authority status, ranging from "Basic" to "Super." All delegated authority lenders are authorized to approve loans and receive an Ex-Im Bank Guarantee without submitting individual applications to Ex-Im Bank for approval. But as lenders progress through the delegated authority tiers, they are able to approve increasingly larger loans and maintain increasingly larger portfolios of Ex-Im-WCGP loans. See the Ex-Im Bank's WCGP Manual for more details.

<sup>17</sup> A lender with PLP status for domestic SBA 7(a) loans can apply for PLP status under the Ex-Im Bank's EWCP as well. SBA offers PLP status on EWCP loans to a PLP lender through a request filed by the lender's international unit for expansion of its domestic lending institution's PLP authority. There is no explicit training requirement for a PLP lending officer. A lender's eligibility is assessed with regard to: (1) the ability to effectively process, close, service, and liquidate SBA-guaranteed loans; (2) the ability to develop and analyze complete loan application packages; and (3) a satisfactory performance history with SBA. In addition, the SBA considers whether a lender shows a substantial commitment to SBA's mission and a spirit of cooperation with SBA PLP. Also, a lender is authorized to make SBA guaranteed loans, subject only to a brief eligibility review and assignment of a loan number by SBA. Lenders are expected to handle servicing and liquidation of all of their SBA loans with limited involvement by SBA. For more information, please refer to the "Lender and Development Company Loan Programs" SOP 50-10(50), [www.sba.gov/about-sba-services/7481](http://www.sba.gov/about-sba-services/7481).

## IV. What Are the Key Risks and Regulatory Issues With the Programs?

Although these loan guarantee programs significantly reduce credit risk by guaranteeing up to 90 percent of a loan, the lender remains exposed to credit risk on the nonguaranteed portion. Lenders must exercise appropriate due diligence and maintain appropriate controls and ongoing monitoring to protect against this credit risk and the operational risks associated with the administration of these programs. Financial institutions should underwrite loans made under these programs using sound underwriting procedures. Lenders using the Ex-Im Bank's WCGP may use their own credit review and financial analysis documentation or follow the agency's Delegated Authority Credit Memorandum Format when underwriting loans.<sup>18</sup> PLP lenders in the SBA's EWCP may use the Delegated Authority Credit Memorandum Format. The SBA loan processing center performs the credit underwriting for participating lenders that do not have SBA delegated authority.

Financial institutions must comply with the operational requirements of the SBA and Ex-Im Bank programs to ensure that guarantees will be honored in the event of defaults. Failure to comply with program rules can result in guarantee claims being partially or fully denied. For example, claims must be filed within the prescribed time period (e.g., 120 days following default for the Ex-Im Bank's WCGP). Ultimately, the quality of the lender's management of operational risk (adherence to Ex-Im Bank and SBA operational requirements) and legal compliance risk associated with these lending programs may have a direct impact on the integrity of the loan guarantees and therefore on the lender's credit risk profile.

Bankers also need to take steps to apply the appropriate policies and procedures to comply with requirements established under the export control and economic sanctions programs administered and enforced by the Office of Foreign Asset Control (OFAC) of the U.S. Department of the Treasury and the Bureau of Industry and Security (BIS) of the U.S. Department of Commerce.<sup>19</sup> Compliance with OFAC regulations, which are intended to enforce U.S. economic and trade sanctions against targeted foreign entities, individuals and countries, is routinely required of all banks in their normal course of business. Knowledge of the Export Administration Regulations (EAR) published by the BIS and their implications for initiating and processing international trade transactions is especially applicable for lenders seeking to conduct such transactions on behalf of their customers. The EAR are the vehicle through which the U.S. laws related to the control of exports, re-exports, and other related activities are enforced.

Some lenders are apprehensive about whether their loan guarantee claims will be honored if loans go into default.<sup>20</sup> Under the Ex-Im Bank's WCGP and the SBA's EWCP, lenders can minimize this risk by carefully following procedures for documenting and servicing loans. With the SBA's EWCP, this risk is further reduced because the SBA pre-approves loans before the loans are funded. Figure 1 lists the most common mistakes identified by the programs.

Although both programs offer technical assistance to support new participants, lenders should be aware that servicing loans under these programs requires more effort than servicing working capital loans that are not government guaranteed.

## V. Who Uses These Programs?

Generally, trade finance is dominated by large financial institutions, although a number of small and midsized financial institutions also are active in the programs. Participants include supervised depository institutions as well as nondepository institutions. Most guaranteed loans are made to small businesses.

<sup>18</sup> The Ex-Im Bank's Delegated Authority Credit Memorandum Format, accessed November 19, 2010, [www.exim.gov/pub/pdf/ebd-w-20.pdf](http://www.exim.gov/pub/pdf/ebd-w-20.pdf).

<sup>19</sup> "Trade Finance Activities—Overview" section of the *Bank Secrecy Act/Anti-Money Laundering Examination Manual*, [www.ffiec.gov/bsa\\_aml\\_infobase/documents/BSA\\_AML\\_Man\\_2010.pdf](http://www.ffiec.gov/bsa_aml_infobase/documents/BSA_AML_Man_2010.pdf).

<sup>20</sup> The share of guaranteed loans for which guarantee claims were filed were under 1 percent in recent years for the SBA-EWCP and just over 2 percent for the Ex-Im-WCGP. For the Ex-Im Bank's WCGP, only one guarantee claim was denied out of the 37 claims filed between the beginning of fiscal year 2007 and the end of fiscal year 2009. None of the 22 SBA's EWCP guarantee claims were denied during this period.

**Figure 1: Common Mistakes by Lenders Making EWCP and WCGP Loans**

- Disbursements exceed collateral.
- Material changes in loan without notification.
- Missing the guarantee claim-filing deadlines (120 days for Ex-Im Bank's WCGP).
- Failure to notify SBA or Ex-Im Bank of events of default or other loan status changes.
- Failure to adhere to terms of loan authorization.
- Other failures in adhering to relevant requirements in the SBA's EWCP Standard Operating Procedures or the Ex-Im Bank's WCGP Master Guarantee Agreement.

The Ex-Im Bank's WCGP lending is accomplished primarily through lenders with delegated authority, a direct result of the program being set up to use delegated authority lenders. On the other hand, most lending through the SBA's EWCP is by lenders who do not have the SBA's PLP status. The SBA is working to increase the share of participating lenders with PLP status. This would decrease the workload for the SBA, while expediting the guarantee approval process for these lenders.

## **VI. How Does the Cost and Pricing Structure Work?**

The SBA's EWCP and Ex-Im Bank's WCGP work in similar ways. Each program allows lenders to negotiate interest rates and fees with borrowers without limitation. The programs assess fees on borrowers and the lenders. Appendix A shows the main parameters for each program. Appendix C shows costs for a hypothetical loan by each program. Table 1 on page 8 shows fees.

The Ex-Im Bank's WCGP charges an upfront facility fee to a borrower. For a delegated authority lender, the Ex-Im Bank shares most of this fee with the lender. For loans up to \$2 million with terms up to six months, the facility fee is 0.75 percent, of which the lender retains 0.5 percent. For loans up to \$2 million with terms between six months and a year, the facility fee is 1.5 percent, of which the lender retains 1.25 percent. For loans greater than \$2 million, the facility fee for the portion over \$2 million is shared equally between the lender and Ex-Im Bank.

The Ex-Im Bank's WCGP facility fee can be reduced to 1 percent for exporters meeting certain criteria:

- Export sales structured under letters of credit<sup>21</sup> and/or backed by export credit insurance.<sup>22</sup>
- Exporter's financial ratios must meet or exceed the industry median quartile.<sup>23</sup>

The Ex-Im Bank's WCGP also charges borrowers an upfront \$100 application processing fee, due at final commitment.

The SBA's EWCP charges borrowers an upfront 0.25 percent guarantee fee and an ongoing service fee throughout the loan term. The service fee is assessed against the outstanding balance each month. The service fee is determined by the SBA annually to cover its projected costs. For loans approved during fiscal year 2011, the service fee is 55 basis points (an annual rate, assessed monthly).<sup>24</sup>

<sup>21</sup> In trade finance, a letter of credit addresses the risk of a buyer's nonpayment and is issued by the buyer's lender to the seller of exported goods on behalf of the buyer. Typically, once a seller presents a letter of credit, goods are shipped and received in accordance with the sales agreement, and the buyer's lender makes payment to the seller.

<sup>22</sup> Ex-Im Bank's export credit insurance covers the risk of a buyer's nonpayment for commercial risks (e.g., bankruptcy) and certain political risks (e.g., war or the inconvertibility of currency). This product can replace cash-in-advance, letters of credit, and other more costly products designed to reduce risk of buyer nonpayment.

<sup>23</sup> The WCGP Manual lists seven financial ratios. Exporters must meet or exceed the industry median quartile on at least four of the ratios.

<sup>24</sup> SBA Information Notice, Control No. 5000-1172, accessed December 15, 2010, [www.wbdc.org/uploads/Small%20Business%20Act%20Notice.pdf](http://www.wbdc.org/uploads/Small%20Business%20Act%20Notice.pdf).

Table 1 summarizes the fees assessed on lenders by each program. Fees can be, and typically are, passed on to borrowers. Lenders may assess additional fees on borrowers.

**Table 1: Fee Structures of SBA's EWCP and Ex-Im Bank's WCGP**

| Fee                                    | SBA's EWCP   | Ex-Im Bank's WCGP   |
|--|--|---|
| Facility fee (0 to 6 month terms)      | None.  | For loans up to \$2 million, flat fee of 0.75%, with 0.5% retained by lender.<br><br>For loans greater than \$2 million, the facility fee for the portion over \$2 million is shared equally.                     |
| Facility fee (6 month to 1 year terms) | None.  | For loans up to \$2 million, flat fee of 1.5% per annum, with 1.25% retained by the lender. For loans greater than \$2 million, the facility fee for the portion over \$2 million is shared equally. <sup>a</sup> |
| Application fee                        | None.  | \$100.  |
| Guarantee fee (borrower)               | 0.25%  | None.   |
| Service fee (lender)                   | Determined annually. (FY 2011 set at 0.55% annual rate, assessed monthly.) | None.   |
| Interest rates                         | Negotiated between borrower and lender.                                    | Negotiated between borrower and lender.   |

Source: SBA and Ex-Im Bank

<sup>a</sup>Facility fees can be reduced for low-risk borrowers and the share of fees retained by lenders is reduced for larger loans. For more details, see Appendix A or the Ex-Im Bank's WCGP Manual, [www.exim.gov/pub/pdf/ebd-w-15.pdf](http://www.exim.gov/pub/pdf/ebd-w-15.pdf).

## VII. What Barriers Have Constrained the Growth of the Programs?

### *Banks Not Aware of Current Borrowers' Export Activities*

Many lenders do not know the extent to which their small business borrowers export. And many small business exporters could draw on working capital lines to expand their current operations with loans from the SBA's EWCP and Ex-Im Bank's WCGP. Additionally, lenders may be unaware that their small business borrowers may be indirect exporters. Both programs guarantee working capital for direct and indirect exports.<sup>25</sup> As banks gain familiarity with these programs, they may become more aware of their borrowers' export operations.

### *SBA Programs Face Cap on Loan Guarantees*

The SBA's EWCP is additionally constrained because guaranteed loans under this program contribute to the overall guarantee cap for the SBA's guaranteed loans for any one borrower. Until enactment of the Small Business Jobs Act of 2010 (Public Law 111-240), this cap was set at \$1.5 million. Many small businesses reached this cap with their domestic SBA-guaranteed borrowing. This effectively prevented them from participating in the SBA's EWCP. In response, many lenders originated loans guaranteed by the Ex-Im Bank's WCGP for these borrowers.

Under the Small Business Jobs Act, the guarantee cap for the SBA's EWCP was permanently raised to \$4.5 million. More than doubling the previous cap should expand the opportunity for borrowers and lenders to use the SBA's EWCP. Ultimately, many of these borrowers will graduate to either the Ex-Im Bank's WCGP or non-guaranteed products, which the SBA would consider a success.

<sup>25</sup> An indirect export is a good that is produced in the United States, sold to another company in the United States, and then sold as an export or incorporated as a component of another good sold as an export. For the purposes of these programs, the good being financed must ultimately be sold to a foreign buyer to be considered an export, but the specific transaction being financed need not be international.



### ***Concern About Lengthy Processing Times***

Some lenders have cited concerns that the SBA, in particular, takes an excessive amount of time to review and approve loan applications. These concerns seem to stem from the performance of other SBA programs and processing from years past; however, recent improvements in SBA processes have reduced approval times overall. Furthermore, the SBA's EWCP is distinct from other SBA programs. Lenders originating loans using SBA underwriting can expect approval decisions within nine days. Lenders participating in the Preferred Lender Program typically receive approvals within three days.<sup>26</sup>

Processing times are typically not a concern for the Ex-Im Bank's program because the majority of its loans are originated by delegated authority lenders. As a result, lenders can approve loans and disburse funds under their delegated authority without having to wait for approval from the Ex-Im Bank.

### ***Concern About Guarantee Claims***

Some lenders are apprehensive that their guarantee claims will not be honored if loans go into default. With the SBA's EWCP and the Ex-Im Bank's WCGP, however, claim denials have been low. The SBA and Ex-Im Bank report that claim denials are unlikely if lenders follow procedures for documenting and servicing loans. Because the SBA pre-approves EWCP loans before the loans can be funded, these risks are additionally reduced.

The Ex-Im Bank's WCGP reports that only one guarantee claim was denied out of 37 claims filed from the beginning of fiscal year 2007 to the end of fiscal year 2009.<sup>27</sup> The SBA's EWCP reports that no guarantee claims were denied out of 22 claims filed during that same period.<sup>28</sup>

## **VIII. Conclusion**

The SBA's EWCP and Ex-Im Bank's WCGP are designed for lenders interested in helping businesses—particularly small businesses in the case of the SBA program—initiate and expand export activities. When properly administered, the programs can be important tools for lenders and borrowers involved in export financing. This is especially true for businesses that might otherwise be unable to find working capital credit and for lenders wishing to reduce credit risk. SBA and Ex-Im Bank administrators believe that the programs are currently underutilized by lenders, in part because many business customers participate in exporting or indirect exporting without the knowledge of their lenders. The programs may help financial institutions to better serve existing and new customers, while increasing their own profitability. Additionally, many of the SBA's EWCP and Ex-Im Bank's WCGP loans to small businesses may be included in an institution's CRA evaluation.

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<sup>26</sup> SBA processing times provided by SBA staff on December 16, 2010.

<sup>27</sup> The Ex-Im Bank's WCGP guarantee payment data provided by Ex-Im-Bank staff on October 13, 2010.

<sup>28</sup> Guarantee payment data provided by SBA staff on December 16, 2010.

## Appendix A: Comparison of SBA's EWCP and Ex-Im Bank's WCGP

|                        | SBA (Normal Processing and Preferred Lender Program)   | Ex-Im Bank (Delegated Authority)   |
|------------------------|--|--|
| Type                   | Single order or revolving line of credit, but allows for advances against purchase orders.   | Single order or revolving line of credit.  |
| Maturity               | One to three years.  | Up to three years.   |
| Guaranty               | 90%.   | 90%.   |
| Eligible borrowers     | Sole proprietorships, partnerships, and corporations.<br><br>One year in business (can be waived based on management experience).<br><br>Must be a small business as defined by SBA.   | Sole proprietorships, partnerships, and corporations.<br><br>One year in business (can be waived based on management experience).  |
| Financial requirements | Ex-Im Bank minimums do not apply.  | Must have positive net worth. Must meet industry lower quartile for four out of seven key ratios.  |
| Eligible products      | No minimum U.S. content requirement.<br><br>Defense customers and defense products are allowed with proper licensing.  | Must be greater than 50% U.S. content.<br><br>No defense products or defense customers.  |
| Use of proceeds        | To acquire inventory and pay for production costs.<br><br>To purchase goods for resale.<br><br>Delivery of services.<br><br>To support Stand-by Letters of Credit with reduced (25%) collateral <sup>a</sup> (may be reduced to 10%).            | Same.  |
| Collateral             | First priority security interest in export inventory and accounts receivable.<br><br>Personal and corporate guarantees.<br><br>Assignment of Letters of Credit or Foreign Credit Insurance (if applicable).                                      | Same.  |
| Loan amount            | Borrower limits: \$4.5 million maximum guaranty and \$5 million maximum loan amount.<br><br>Lender limits: None.   | Six levels of delegated authority for lenders ranging from \$1 million to \$10 million per exporter and from \$10 million to \$150 million aggregate per lender.   |
| Application fee        | None.  | \$100.   |
| Other fees             | Guaranty fee: 0.25% (of the guaranteed amount) for a 12-month loan.<br><br>Service fee: 55 basis points charged to lender as with all SBA 7(a) loans (based on monthly balance).<br><br>Lender may charge additional fees as deemed appropriate. | Facility fee (upfront):<br>Up to six months: flat fee of 0.75% (lender retains 0.5%).<br><br>More than six and up to 12 months: 1.50% annual, pro-rated for terms less than 12 months (lender retains 1.25% as a baseline <sup>b</sup> ).<br><br>For loans greater than \$2 million the Facility Fee for the portion over \$2 million is shared equally. |
| Field examinations     | None required.   | Required for loans of \$1 million or more; semi-annual at borrower's cost.   |
| Interest rates         | Negotiable with lender.  | Negotiable with lender.  |

Source: SBA and Ex-Im Bank

<sup>a</sup> A stand-by letter of credit is used to guarantee payment to a borrower's suppliers. The borrower's bank issues the letter of credit to the supplier's bank and the supplier is paid once receipt of the good or service is documented.

<sup>b</sup> Facility fees can be reduced for lower risk loans (to 0.5 percent for loans up to six months and 1 percent per annum for loans longer than six months), as defined in the Ex-Im Bank's WCGP Program Manual, [www.exim.gov/pub/pdf/ebd-w-15.pdf](http://www.exim.gov/pub/pdf/ebd-w-15.pdf). Fee sharing terms vary by loan amount, with lenders retaining the percentage listed for loans up to \$2 million; the percentage retained by lenders generally declines for the share of larger loans that exceeds this \$2-million benchmark. See the Program Manual for details.

## Appendix B: Example of Export Working Capital Loan Guarantee Transaction

CleanWater, a fictitious company, manufactures water filtration equipment for sale primarily to municipalities in the United States and foreign countries. Although this company would likely need working capital loans to support its business—whether the customer is located in the United States or overseas—financial institutions may be more willing to approve a transaction-specific working capital line for a domestic deal. Lenders would be more comfortable with the likelihood of repayment from a domestic municipality that has access to a stable tax base and revenue from federal programs (e.g., Community Development Block Grants). Underwriting a loan to a company for which the source of repayment is future payments from a municipality in an emerging market country (e.g., Malaysia, Egypt, or Hungary) might be more problematic for a lender.

CleanWater has manufactured and distributed its product in the United States for more than 15 years. Because the company's track record is strong, there is little risk that the company will not make good on its contractual obligations with regard to the sales contract. The company wants to expand its lending into foreign markets and has an interested buyer in the Philippines. The Philippines government is interested in putting in a new water filtration plant in Sagada, a municipality in the northwestern part of the country.

The buyer seeks to purchase and install a suite of filtration equipment with a retail price of \$5 million. CleanWater would produce this equipment through a network of domestic manufacturers with which it has long-standing relationships. The costs of production and installation will be \$4 million, with payments due to suppliers throughout the eight-month production period. Delivery and installation of the final goods are due to Sagada nine months after signing the sales contract. The Philippine government will pay \$2 million upon signing the sales contract, with the \$3 million balance due within 60 days of installation of the finished product. Both the initial and final payments will be funded out of a loan to the Philippine government from the World Bank.

CleanWater needs to finance \$2 million in working capital to cover its costs of production, over and above the \$2 million that the buyer will pay upon signing the sales contract. The company approaches ABC National Bank, an Ex-Im Bank delegated authority lender under the WCGP.

The terms of the loan negotiated between ABC National Bank and CleanWater include

- Interest rate will be the Wall Street Journal Prime Rate plus 1.5 percent, adjusted daily.
- Payments will be interest-only, payable monthly, with principle due at final payment on contract, which is scheduled at the end of month 11.
- Payment will come through a lock-box account maintained by ABC National Bank for this purpose.
- Ex-Im Bank charges ABC National Bank an up-front facility fee of 1.5 percent of the Ex-Im Bank's WCGP credit line (\$30,000), which is passed through as an up-front fee to CleanWater.

CleanWater will work with three suppliers to execute the contract, as follows:

- Supplier A will complete its work at a cost to CleanWater of \$1 million at the end of month three. This will trigger the release of \$500,000 in working capital, with Supplier A's product serving as collateral.<sup>29</sup>
- Supplier B will complete its work at a cost to CleanWater of \$1 million at the end of month five. This will trigger the release of an additional \$500,000 in working capital, with Supplier B's product serving as collateral.

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<sup>29</sup> Maximum collateral for finished goods or works in progress is 75 percent, so the 50 percent leverage leaves room for adjustment.

- Supplier C will complete its work at a cost to CleanWater of \$1 million at the end of month seven. This will trigger the release of the final \$1 million in working capital, collateralized by the products from Supplier A, B, and C.<sup>30</sup>

The proceeds from the Ex-Im Bank's WCGP loan and the initial \$2 million payment will cover all production and installation costs for ClearWater for this project, which will be completed by the end of month nine.

The final payment from the Philippine government will be due 60 days later, at the end of month 11. This \$3 million will cover repayment of the Ex-Im Bank's WCGP loan (\$2 million), as well as returning a profit to ClearWater.

Buyer payments will come from a long-term World Bank loan to the Philippine government. This secure source of funding provides assurance to the lender and the Ex-Im Bank that there is little likelihood of buyer default.

See table 2 for a timeline of cash flows associated with this loan.

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<sup>30</sup> The production cost to ClearWater for products from Suppliers A, B, and C is \$3 million, which could support a WCGP loan of up to \$2.25 million. The total drawdown here of \$2 million is within program guidelines.

**Table 2: CleanWater Cash Flow Projections**

With a \$2 million working capital loan from Ex-Im Bank's WCGP, CleanWater maintains a positive cash position for nearly a year despite the outlay of \$3.92 million to procure and install a water filtration system for the Philippine government. In month 11, CleanWater receives the buyer's final \$3 million payment and repays the \$2 million WCGP loan.

| Cash Flow by Month           | 0           | 1           | 2           | 3             | 4           | 5             | 6           | 7             | 8           | 9           | 10          | 11            | 12        |
|------------------------------|-------------|-------------|-------------|---------------|-------------|---------------|-------------|---------------|-------------|-------------|-------------|---------------|-----------|
| Payments to suppliers        |             |             |             | (\$1,000,000) |             | (\$1,000,000) |             | (\$1,000,000) |             |             |             |               |           |
| Interest payments            | \$0         | \$0         | \$0         | (\$1,979)     | (\$1,979)   | (\$3,958)     | (\$3,958)   | (\$7,917)     | (\$7,917)   | (\$7,917)   | (\$7,917)   | (\$7,917)     | \$0       |
| Facility fee due WCGP        | (\$30,000)  |             |             |               |             |               |             |               |             |             |             |               |           |
| Internal costs of production |             | (\$100,000) | (\$100,000) | (\$100,000)   | (\$100,000) | (\$100,000)   | (\$100,000) | (\$100,000)   | (\$100,000) | (\$100,000) | (\$10,000)  | (\$10,000)    | \$0       |
| Principal repayment          |             |             |             |               |             |               |             |               |             |             |             | (\$2,000,000) |           |
| Buyer payment                | \$2,000,000 |             |             |               |             |               |             |               |             |             |             | \$3,000,000   |           |
| Loan drawdown                |             |             |             | \$500,000     |             | \$500,000     |             | \$1,000,000   |             |             |             |               |           |
| Net cash position            | \$1,970,000 | \$1,870,000 | \$1,770,000 | \$1,188,021   | \$1,066,042 | \$462,083     | \$358,125   | \$250,208     | \$142,292   | \$34,375    | \$16,458    | \$998,542     | \$998,542 |
| Outstanding loan principal   |             |             |             | \$500,000     | \$500,000   | \$1,000,000   | \$1,000,000 | \$2,000,000   | \$2,000,000 | \$2,000,000 | \$2,000,000 | \$2,000,000   | \$0       |

## Appendix C: Example Costs for a Loan Under SBA’s EWCP and Ex-Im’s WCGP

ABC Inc. seeks a \$1 million working capital loan from First National Bank to support a large contract for its growing export business. The loan will be for one year and will be paid off with the customer payment upon receipt of goods. The full loan amount will be drawn down at closing (and will be outstanding for the full year). The following table illustrates the fees under EWCP and WCGP.

|                           | <b>SBA’s EWCP</b><br>(Normal Processing and Preferred Lender Program)   | <b>Ex-Im Bank’s WCGP</b><br>(Delegated Authority)   |
|---------------------------|---|---|
| Total loan amount         | \$1 million   | \$1 million   |
| Guaranteed amount         | \$900,000   | \$900,000   |
| Interest rates            | Negotiable with lender.   | Negotiable with lender.   |
| Bank fees to borrower     | Negotiable with lender.   | Negotiable with lender.   |
| Application fee to agency | None.   | \$100   |
| Other fees                | \$2,250 guarantee fee paid to SBA by borrower.<br><br>\$4,950 paid by lender (\$412.50 per month, assuming the full balance is drawn and held for the entire year). | \$15,000 from borrower to agency as an upfront facility fee, lender retains \$12,500. This fee can be reduced for very low risk borrowers. <sup>a</sup> |
| Field examinations        | None required.  | Required for loan amounts of \$1 million or more; semi-annual at borrower’s cost.   |

<sup>a</sup> See information on page 8.

Kristopher Rengert was the primary author of this report. Also contributing were William Reeves, Ted Wartell, and Barry Wides. Copyediting assistance was provided by Lily Chin, Janet Fix, and Joyce Jones. Community Developments *Insights* reports differ from OCC advisory letters, bulletins, and regulations in that they do not reflect OCC policy and should not be considered as definitive regulatory or supervisory guidance. Some of the information used in the preparation of this paper was obtained from publicly available sources that are considered reliable. However, the use of this information does not constitute an endorsement of its accuracy by the OCC.