



*Community
Development
Financial
Institutions*

A Publication of the CDFI Data Project



This report is a product of the CDFI Data Project (CDP)—an industry collaborative that produces data about community development financial institutions (CDFIs).

The goal of the CDP is to ensure access to and use of data to improve practice and attract resources to the CDFI field. *Community Development Financial Institutions: Providing Capital, Building Communities, Creating Impact* analyzes fiscal year 2005 data collected through the CDP from 496 CDFIs.

Written by the CDP Publication Committee

Aspen Institute

**Community Development Venture
Capital Alliance**

National Community Investment Fund

**National Federation of Community
Development Credit Unions**

Opportunity Finance Network

The writers would like to thank the CDP Advisory Committee for its assistance and editorial guidance in this publication.

CDFI Data Project Advisory Committee

Mark Pinsky, Chair

Opportunity Finance Network

Kerwin Tesdell, Vice Chair

Community Development
Venture Capital Alliance

Elaine Edgcomb

Aspen Institute

Amy McKenna Luz

Association for Enterprise Opportunity

Jennifer Vasiloff

Coalition of Community Development
Financial Institutions

Andrea Levere

CFED

Saurabh Narain

National Community Investment Fund

Clifford Rosenthal

National Federation of Community
Development Credit Unions

This publication and the research that was done was funded by the Annie E. Casey Foundation, the Ford Foundation, the John D. and Catherine T. MacArthur Foundation, HSBC Bank USA, Wachovia Foundation, and the W. K. Kellogg Foundation. We thank them for their support but acknowledge that the findings and conclusions presented in this report are those of the author(s) alone, and do not necessarily reflect the opinions of these organizations.

Providing Capital Building Communities Creating Impact

“Studies undertaken by the CDFI Data Project show that for 2004, charge-off rates for CDFI portfolios were similar to those for the banking industry as a whole. These studies and market data suggest that banks and other private organizations may become an increasingly significant source of competition for CDFIs. That is good news, not bad news...”

– Federal Reserve Chairman Ben Bernanke

Contents

Executive Summary	2-3
CDFI Industry Overview	4-5
Size and Scope of CDFI Field	6-8
Focus on Diversity	9
Focus on Rural CDFIs	10
Focus on Revitalizing Rural Communities	11
CDFI Outcomes, Impacts, and Clients	12-13
CDFI Products, Services, and Performance	14-18
Appendix A: Methodology	19
Appendix B: Glossary of Terms	20

Complementing this publication are individual brochures that provide more in-depth analysis of the following institution types: community development banks, community development credit unions, community development loan funds, community development venture capital funds, and microenterprise funds.

The CDFI industry continues to grow, innovate, and change, while retaining its focus on strong financing performance and increasing impact in emerging domestic markets throughout the United States. This study, which includes fiscal year (FY) 2005 data from 496 CDFIs, one of the largest data sets ever collected on the CDFI industry, demonstrates the following:

CDFIs invested \$4.3 billion in FY 2005 to create economic opportunity in the form of new high-quality jobs, affordable housing units, community facilities, and financial services to low-income people.

In FY 2005, CDFIs:

- financed and assisted 9,074 businesses, which created or maintained 39,151 jobs;
- facilitated the construction or renovation of 55,242 units of affordable housing;
- built or renovated 613 community facilities in economically disadvantaged communities; and
- provided 11,401 alternatives to payday loans and helped 138,045 low-income individuals open their first bank account.¹

CDFIs serve niche domestic markets throughout the United States that are not adequately served by conventional financial markets. CDFI customers are 52% female, 58% minority, and 68% low income—all much higher proportions than in mainstream financial institutions. Such customers typically have been turned down by conventional financial institutions because they do not have sufficient collateral or capacity and resources to borrow from banks.

CDFIs finance transactions in low-income communities in a prudent and effective way. CDFIs are adept at managing risks through a combination of solid capital structures and loan loss reserves, close monitoring of portfolios, and technical assistance. In 2005, CDFIs in this study had a net charge-off ratio of 0.44%, which outperforms the net charge-off ratio of 0.60%² for all financial institutions. Delinquency

ratios are also relatively low. Banks and loan funds had delinquency rates greater than 90 days of 1.5% and 2.4%, respectively, and credit unions, which measure delinquency by a different metric, had a delinquency rate greater than 60 days of 1.7%.

CDFIs continue to grow and change in response to changes in the market. The 496 CDFIs in this study held \$20.8 billion in assets and \$14.1 billion in financing outstanding. For the 224 CDFIs for which we have six years of data, financing outstanding grew at a compound annual growth rate (CAGR) of 17% per year. CDFIs are growing at a time of decreasing subsidy available from government sources and financial institutions. CDFIs are finding new ways of using market-rate or near-market-rate capital; using off-balance-sheet financing transactions to grow their financing and impact; and increasing earned income and the use of partnerships to improve business models and sustainability.

Financial leaders, such as Federal Reserve Chairman Ben Bernanke, have taken note of the success of the CDFI industry and the CDP. Bernanke said at the Opportunity Finance Network conference in November 2006, “Studies undertaken by the CDFI Data Project show that for 2004, charge-off rates for CDFI portfolios were similar to those for the banking industry as a whole. These studies and market data suggest that banks and other private organizations may become an increasingly significant source of competition for CDFIs. That is good news, not bad news. Indeed, the surest sign of a CDFI’s success is that private investors see viable investment opportunities in the neighborhoods in which the CDFI has been operating.”

¹ The numbers would be 6,152 payday loan alternatives and 15,259 unbanked customers helped based on the community development credit unions (CDCUs) that responded to the survey. The National Federation of Community Development Credit Unions estimated these figures to be 11,401 payday loan alternatives and 138,045 new accounts to unbanked customers in FY 2005 for the entire universe of CDCUs.

² Federal Deposit Insurance Corporation, December 2005.

FY 2005 CDFI Data Project Data

Figure 1: Summary of FY 2005 CDP Data

	All	Bank	Credit union	Loan fund	Venture fund
Number of CDFIs	496	51	280	150	15
Total Assets	\$20,782,033,752	\$11,105,541,165	\$5,688,162,756	\$3,813,059,321	\$175,270,510
Average Assets	\$41,899,262	\$217,755,709	\$20,314,867	\$25,420,395	\$11,684,701
Total FTEs	7,624 n = 320	3,436 n = 51	1,673 n = 115	2,434 n = 140	82 n = 14
Total Direct Financing Outstanding	\$14,026,013,396	\$7,233,417,171	\$4,232,457,207	\$2,432,213,037	\$127,925,981
Average Direct Financing Outstanding	\$28,860,110	\$141,831,709	\$15,115,919	\$17,372,950	\$8,528,399
% of Direct Financing Outstanding (\$) (a)	n = 272	n = 5	n = 116	n = 136	n = 15
Business	13%	13%	4%	18%	97%
Community Service	9%	19%	0%	13%	2%
Consumer	24%	1%	61%	0%	0%
Housing	48%	57%	30%	62%	0%
Micro	2%	0%	1%	3%	1%
Other	5%	11%	4%	3%	0%
% of Direct Financing Outstanding (#) (a)	n = 266	n = 5	n = 116	n = 130	n = 15
Business	2%	7%	0%	12%	69%
Community Service	2%	51%	0%	5%	3%
Consumer	70%	11%	81%	2%	0%
Housing	12%	24%	7%	54%	0%
Micro	3%	1%	1%	26%	28%
Other	11%	6%	12%	2%	0%
Net Charge-Off Ratio	0.4%	0.2%	0.8%	0.6%	NA
Delinquency Rate > 90 Days	NA	1.5%	NA	2.4%	NA
Delinquency Rate > 2 Months	NA	NA	1.7%	NA	NA
Total Capital (b)	\$19,932,491,499	\$10,909,839,952	\$5,645,479,956	\$3,153,971,812	\$223,199,779
Average Capital	\$40,186,475	\$213,918,430	\$20,162,428	\$21,026,479	\$14,879,985
% of Debt Capital from: (c) (d)	n = 268	NA	n = 113	n = 140	n = 5
Banks, Thrifts, and Credit Unions	21%	NA	5%	48%	30%
Corporations	1%	NA	1%	2%	0%
Federal Government	4%	NA	0%	9%	25%
Foundations	6%	NA	1%	14%	38%
Individuals	55%	NA	85%	2%	0%
National Intermediaries	2%	NA	1%	3%	3%
Nondepository Financial Institutions	3%	NA	0%	8%	3%
Other	4%	NA	6%	2%	0%
Religious Institutions	3%	NA	1%	5%	1%
State Government	2%	NA	1%	5%	0%

Notes: (a) The number of institutions (n) and breakout data are for the CDFIs that provided the breakout data for each category.

(b) Total capital for venture capital funds includes capital committed (and not drawn down).

(c) Debt capital includes borrowed funds, EQ2, secondary capital and shares, and deposits. Debt capital breakout does not include credit union borrowings.

(d) One outlier is excluded from debt capital breakouts.

CDFI Industry Overview

CDFIs are specialized financial institutions that create economic opportunity for individuals and small businesses, quality affordable housing, and essential community services throughout the United States. Currently, approximately 1,000 CDFIs operate in low-wealth communities in all 50 states, the District of Columbia, and Puerto Rico. CDFIs provide affordable banking services to individuals and finance small businesses, affordable housing, and community services that, in turn, help stabilize neighborhoods and alleviate poverty. In addition, CDFIs provide credit counseling to consumers and technical assistance to small business owners and housing developers to help them use their financing effectively.

CDFI customers include a range of individuals and organizations:

- **Small business owners**, who bring quality employment opportunities and needed services to economically disadvantaged communities
- **Affordable housing developers**, who construct and rehabilitate homes that are affordable to low-income families
- **Community service providers**, which provide childcare, health care, education, training, arts, and social services in underserved communities
- **Individuals** who require affordable banking services, including basic checking and savings accounts, responsible alternatives to predatory financial companies, mortgages, and other kinds of loans

Why Are CDFIs Needed?

A growing gap exists between the financial services available to the economic mainstream and those offered to low-income people and communities. CDFIs help bridge that gap by bringing capital and financial services to the latter, affording them access to capital to start and expand businesses, build and purchase homes, and develop needed community facilities.

As mainstream lenders have increasingly consolidated, grown in size, and streamlined their operations, their connections to local communities have diminished. Millions of families today either have no relationship with mainstream lenders or depend on fringe financial institutions. This exacerbates long-standing difficulties that low-income families, and the nonprofit institutions that serve them, have had in accessing credit and financial services.

In the absence of conventional financial service providers, high-cost check-cashing services and payday lenders have moved into low-income communities. These institutions prey on unsophisticated borrowers, draining wealth from distressed neighborhoods and contributing to the growing economic inequality in the United States. Payday lenders offer quick cash but charge exorbitant interest rates. Check-cashing companies are increasingly becoming the financial service institutions of choice for low-income people, creating a dual system for delivery of financial services. CDFIs offer responsible alternatives to these predatory lenders, providing necessary products and services at a fraction of the cost to consumers.

In addition, mainstream financial institutions do not sufficiently meet the capital needs of nonprofit organizations that provide critical community services and of small businesses that employ people and provide services in emerging domestic markets. Such organizations often have neither enough collateral to meet conventional banking standards nor the capacity and resources to borrow from banks. CDFIs are able to use their flexible capital products, coupled with critical technical assistance, to serve these markets while also managing their risks.

CDFIs respond to market needs for affordable housing, small business development and job creation, creation of community facilities, financial literacy, and consumer education. They also provide safe and fair mechanisms for low-income customers to do such simple things as open a checking account or obtain a mortgage.

CDFI activities fit into two broad categories. First, all CDFIs provide *financial services*, including such activities as loans, equity investments, deposits, and consumer financial products. Second, virtually all CDFIs provide *nonfinancial services*. For some organizations, these services represent fairly modest complements to their larger financial service activities; for others, they represent the majority of the organization's work. Such activities include entrepreneurial education, organizational development, homeownership counseling, savings programs, and financial literacy training.

The Four Sectors of the CDFI Industry

As with mainstream lenders, a variety of institutions has evolved to serve the broad range of needs in emerging domestic markets. Although these institutions share a common vision of expanding economic opportunity and improving the quality of life for low-income people and communities, the four CDFI sectors—banks, credit unions, loan funds, and venture capital (VC) funds—are characterized by different business models and legal structures.

- **Community development banks** provide capital to rebuild economically distressed communities through targeted lending and investing. They are for-profit corporations with community representation on their boards of directors. Depending on their individual charters, such banks are regulated by some combination of the Federal Deposit Insurance Corporation (FDIC), the Federal Reserve, the Office of the Comptroller of the Currency, the Office of Thrift Supervision, and state banking agencies. Their deposits are insured by FDIC.
- **Community development credit unions (CDCUs)** promote ownership of assets and savings and provide affordable credit and retail financial services to low-income people, often with special outreach to minority communities. They are nonprofit financial cooperatives owned by their members. Credit unions are regulated by the National Credit Union Administration (NCUA), an independent federal agency, by state agencies, or by both. In most institutions, deposits are also insured by NCUA.
- **Community development loan funds (CDLFs)** provide financing and development services to businesses, organizations, and individuals in low-income communities. There are four main types of loan funds; defined by the clients they serve: microenterprise, small business, housing, and community service organizations. Increasingly, loan funds are serving more than one type of client in a single institution. CDLFs tend to be nonprofit and governed by boards of directors with community representation.
- **Community development venture capital (CDVC) funds** provide equity and debt-with-equity features for small and medium-sized businesses in distressed communities. They can be either for-profit or nonprofit and include community representation.

Within certain constraints, CDFIs choose the legal structure that maximizes value and resources to the people and communities they serve. The different corporate structures allow for different capitalization products, financing products, and regulations.

Community development banks are all for-profit entities, whereas CDCUs are nonprofit cooperatives with members (and customers) as shareholders. Nearly all of the depositories—credit unions and banks—are regulated by state or federal agencies (or both) and use insured deposits and shares to capitalize their organizations.

The vast majority of CDLFs (96%) are nonprofit. The CDVC field is the most varied, with 67% structured as for-profit, 27% as nonprofit, and the remaining as quasi-government. The for-profit category includes limited liability companies (LLCs), limited partnerships (LPs), and C corporations among its corporate structures. The loan funds and venture funds are unregulated institutions.

Timeline of CDFIs

The roots of the CDFI industry go back to the early 1900s. Some of the first CDFIs were depository institutions that collected savings from the communities they served in order to make capital for loans available to those communities. Credit unions and banks dominated the field until the 1960s and 1970s, when community development corporations and CDLFs emerged to make capital available for small businesses and affordable housing developers.

In the past three years, the industry has appeared to be slowing down in terms of the growth of new CDFIs, while consolidating and growing existing CDFIs. From 2003 to 2005, 15 new CDFIs were established (from our sample), compared with 36 established in the prior three years (2000, 2001, and 2002). In addition, the industry is just beginning to experience its first mergers, including some high-profile ones in loan funds, banks, and credit unions. We expect that trend to continue in the next few years.

The four institution types have distinct histories and growth trajectories (see Figure 2). Community development banks and credit unions are the most mature sectors, with institutions dating back to the turn of the 20th century. They have had slow and steady growth for the past several decades. Loan funds are much newer, with 72% of this sector established in the 1980s and 1990s. Venture capital funds are newer still: only one VC fund in this study began financing before 1995. In the 1990s, the CDFI industry grew significantly: 32% of the CDFIs in our sample were established after 1990.

The CDFI Fund

The main factor that contributed significantly to the CDFI growth of the 1990s was the creation and subsequent growth of the CDFI Fund. In 1994, the federal government established the CDFI Fund as a new program within the U.S. Department of Treasury. The CDFI Fund is now one of the largest single sources of funding for CDFIs and the largest source of hard-to-get equity capital. It plays an important role in attracting and securing private dollars for CDFIs by requiring them to match their award with nonfederal funds. The Fund reports that \$1 of its investment leverages \$27 of private-sector investments. The CDFI Fund operates four principal programs: the CDFI Program, the Bank Enterprise Award (BEA) Program, the New Markets Tax Credit Program, and the Native American CDFI Assistance (NACA) Program.

In FY 2005 alone, CDFIs leveraged each appropriated financial assistance (FA) dollar from the CDFI Fund with \$27 in private and other non-CDFI Fund dollars, in effect using \$51 million in FA disbursements to leverage \$1.4 billion private and non-CDFI Fund dollars. Since 1995, its first year of funding, the Fund made more than \$820 million in awards to CDFIs and financial institutions through the CDFI and BEA Programs. It has also awarded allocations of New Markets Tax Credits, which will attract private-sector investments totaling \$12.1 billion, including \$600 million for the Gulf Opportunity Zone. Although the CDFI Fund's funding has decreased under the Bush administration, it remains a critical resource for CDFIs.

Community Reinvestment Act

In addition to the CDFI Fund, the federal government strengthened provisions and enforcement of the Community Reinvestment Act (CRA) during the 1990s.³ In particular, the 1995 CRA regulations, which classified loans and investments in CDFIs as qualifying CRA activity, increased those activities. These regulations have led to the growth of banks as a critical source of capital for CDFIs.

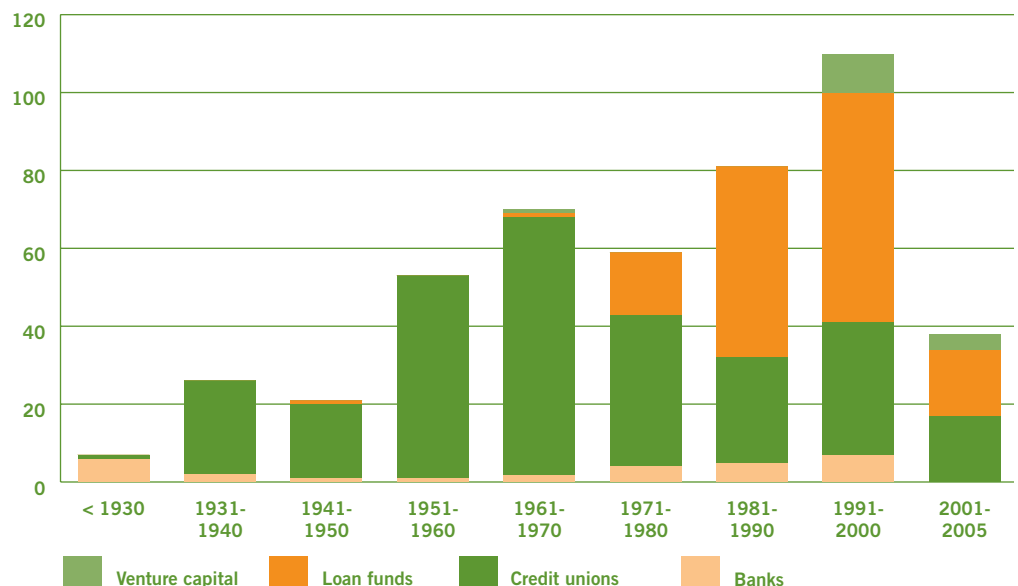
Native American CDFIs

A range of CDFIs has also emerged to serve the needs of Native American populations in the past couple of years. Serving these communities entails unique challenges because of the concentration of poverty, reservation-based economies, and tribal governance. Despite the challenges, there are currently 38 Native American-certified CDFIs, a number that is growing each year. Of those CDFIs, 26 are loan funds, six are banks, five are credit unions, and one is an intermediary. There are also many emerging native CDFIs that are not yet certified. Unlike the growth of the CDFI industry, in which the first CDFIs were depositories, the Native American CDFI sector began with mostly loan funds, followed by the growth of native credit unions.

The CDFI Fund has helped this field grow by providing targeted funding for Native American communities. The CDFI Fund has provided \$19.5 million to 95 organizations for Native American initiatives, including development of and financing and technical assistance for Native American CDFIs.

³ The Community Reinvestment Act of 1977 places responsibilities on depository institutions to lend to, invest in, and serve all of the communities in which they receive deposits from customers.

Figure 2: Number of CDFIs by Decade



Note: Year is year of charter for credit unions and year the institution started financing for other sectors.

Size and Scope of the CDFI Field

The FY 2005 CDP data set represents 496 CDFIs of the approximately 1,000 CDFIs operating in the United States.

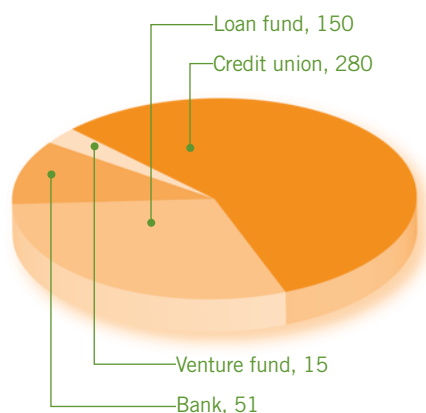
The CDP estimates that there are approximately 100 community development banks, 290 CDCUs, 500 CDLFs, and 80 CDVC funds. The CDP sample (Figure 3) represents a significant percentage of each CDFI sector.⁴

Asset Size of CDFIs

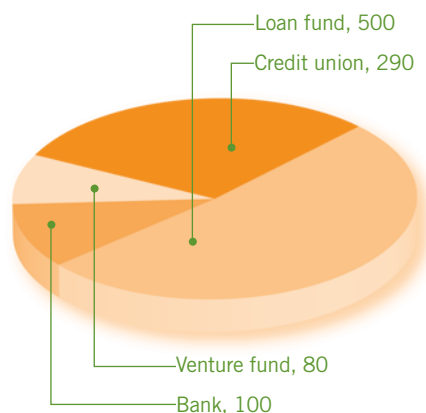
The CDFIs in this study managed \$20.8 billion in assets at the end of FY 2005 (see Figure 4 for a breakout by institution type). Although that number represents a significant amount of capital for emerging domestic communities, it is still quite modest compared with the mainstream financial sector. As of December 31, 2005, U.S. financial institutions alone controlled more than \$10.8 trillion in assets.⁵ Thus, although the growth of the CDFI industry over the past decade is significant in relative terms, it remains a specialized, niche player in the wider financial services industry.

Institution size varies substantially across and within the four sectors. The CDCU sector represents a large number of small organizations—the inverse of the banking sector. For example, 51 community development banks together hold almost double the assets (\$11.1 billion) of the 280 credit unions (\$5.7 billion). The median bank holds approximately \$122 million in assets, while the median credit union holds only \$2.4 million. Loan funds represent 18% of our sample (or \$3.8 billion), with a median size of \$7.7 million. VC funds also tend to be small institutions relative to banks. Specializing in the niche products of equity and near equity, they managed less than 1%

Figure 3: CDP Sample by Sector



Estimated Number of CDFIs in the United States by Sector



Note: Total number estimates are from CDFI trade associations and intermediaries.

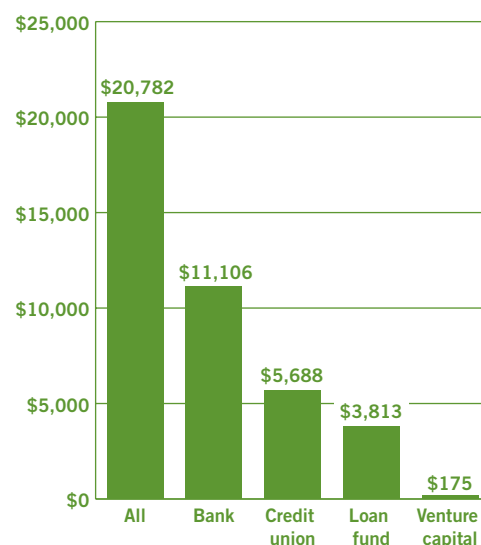
of total assets reported, with a median asset size of \$6.7 million.

Distribution of Assets

A small number of CDFIs also holds a substantial portion of the field's total assets. The largest five CDFIs control 28% of the sample's assets, and the largest 10 control 38% (see Figure 5). The largest five CDFIs include institutions in three of the four sectors: three banks, one loan fund, and one credit union.

Although most organizations (64%) in the field have less than \$10 million in assets and 40% have less than \$5 million in assets, overall industry results are skewed by a handful of very large institutions. Of the 50 CDFIs with more than \$100 million of assets, seven are loan funds, 11 are credit unions, and 32 are banks.

Figure 4: Total Assets (in millions)



Median Assets (in millions)

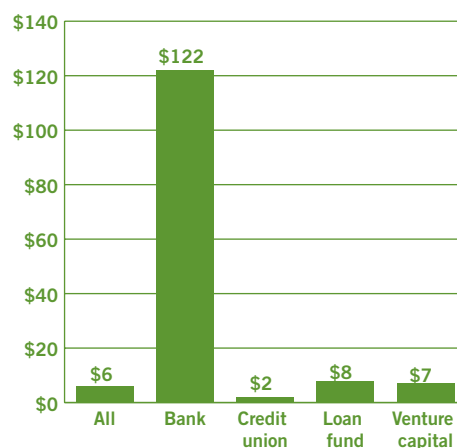
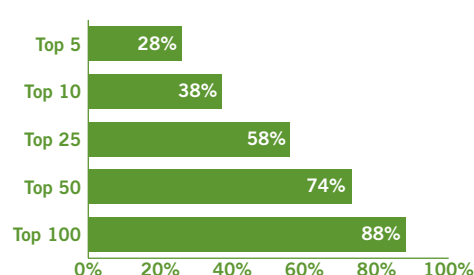


Figure 5: Concentration of Assets



Capitalization

CDFIs managed more than \$19.9 billion of capital at the end of FY 2005. CDFIs receive 21% of their debt capital from banks, thrifts, and credit unions, and 55% from individuals. Credit unions receive a majority (85%) of their debt capital from individuals, whereas loan funds receive a majority (48%) of their debt capital from banks, thrifts, and credit unions.⁶

⁴ There are 100 community development banks in the National Community Investment Fund's (NCIF's) network. NCIF estimates the total number of community development banking institutions (CDBIs) in the country as approximately 500. These banks had 60% or more of their branches located in a low-income community. NCIF made the assumption that banks located in low-income census tracts (as defined by the CDFI Fund) will serve at least a portion of the residents and businesses in those communities.

⁵ As of December 31, 2005, according to the FDIC.

⁶ One loan fund is excluded from debt capital breakouts.

When Dolores Tucker and her fellow tenants learned that their apartment building was to be sold, they decided to purchase the building as a cooperative.

Unitarian Universalist Affordable Housing Corporation (UUAHC) gave them an earnest money loan of \$7,000 and partnered with Eagle Bank to provide a last-minute bridge loan until the association could receive long-term financing from the District of Columbia.

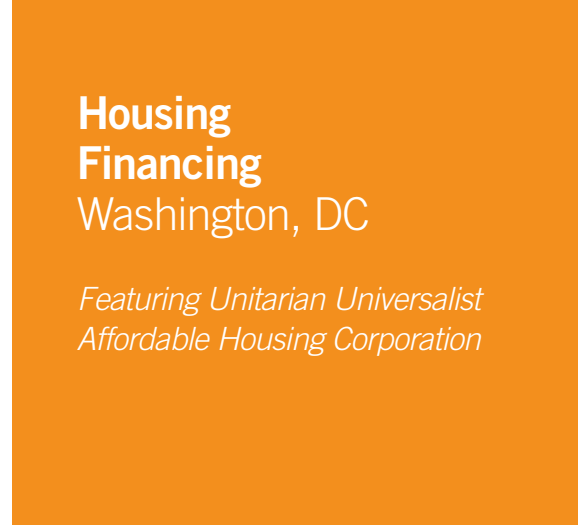
“It’s an unbelievable feeling. I’m doing all the things I used to do to take care of my building, but now it’s for me.”

Dolores Tucker
President,
Friendly Neighbor Tenant Association

The Unitarian Universalist Affordable Housing Corporation (UUAHC) was founded in 1989 as a loan fund capitalized by investments from individuals, churches and institutions to improve the lives and neighborhoods of low- and moderate-income people in

the Washington metropolitan region. Loans have supported the work of a wide range of affordable housing developers including nonprofit, for profit and tenant associations. UUAHC’s recent growth and lending activity attracted the attention of another CDFI serving the Washington metropolitan region—the Washington Area Housing Trust Fund. After months of discussions and due diligence, both boards have unanimously voted to merge. This merger will create the largest locally controlled CDFI in the Washington metropolitan region with an initial capitalization of close to \$20 million.

To right: Dolores Tucker of the Friendly Neighbors Tenant Association



Housing Financing Washington, DC

Featuring Unitarian Universalist Affordable Housing Corporation



Focus on CDFI and Bank Partnerships

Banks have consistently been a provider of capital to CDFIs, as well as being critical partners for CDFIs in enhancing their ability to serve emerging domestic markets. Banks view CDFIs as key partners to increase their market penetration in low-income communities, to allow them to finance a greater number of deals, and to help fulfill their CRA requirements. Bank-CDFI partnerships range from informal to highly structured relationships. Some examples of the ways banks partner with CDFIs include the following:

- **Investing directly in CDFIs to expand the capital base of CDFIs** (i.e. grants, loans, subordinate debt, equity equivalent, equity investments): In our sample, bank, thrift, and credit union debt investments in CDFIs was \$965 million at the end of 2005, representing 21% of CDFI debt capital.⁷
- **Referring to CDFIs deals that banks cannot finance:** Some of these clients return to become bank customers after they develop a credit history.

- **Co-lending, participation lending, and selling loans to financial institutions**
- **Developing products together** (e.g., the Citibank/Opportunity Finance Network partnership, which co-developed the Equity Equivalent Investment in 1997): At the end of 2005, \$123 million of EQ2s is on the balance sheet of the CDFIs in the sample.
- **Working jointly on policy initiatives that provide additional capital to industry** (e.g., the New Markets Tax Credit).

Statistics on Bank Investments in CDFIs

- Of the 269 CDFIs that reported a breakout of debt capital in 2005, 69% had investments from financial institutions
- Banks are investing in small and large CDFIs, representing a similar percentage for small and large CDFIs. In 2005, banks represented 21% of debt capital for CDFIs with more than \$6 million in capital and for CDFIs with less than \$6 million in capital.
- Banks are investing in rural and urban CDFIs, representing a larger percentage of debt capital for urban CDFIs (24% for urban vs. 12% for rural).

⁷ One outlier is excluded from debt capital breakouts.

Figure 6: Debt Investments by Financial Institutions by CDFI Type*

	Bank Investments	% of Debt from Banks
Credit union	\$118,517,160	5%
Loan fund	\$687,223,912	48%
Venture capital fund (a)	\$11,441,896	30%

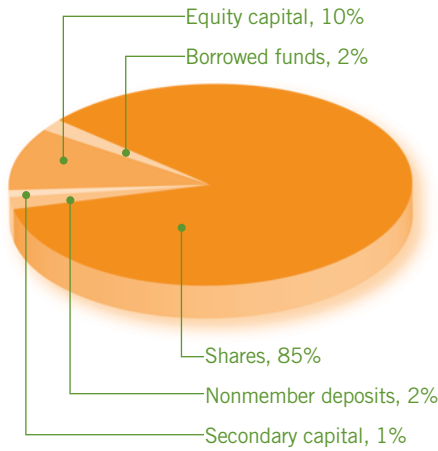
Notes:

(a) In addition to debt capital, VC funds have received a substantial amount of equity investments from financial institutions.

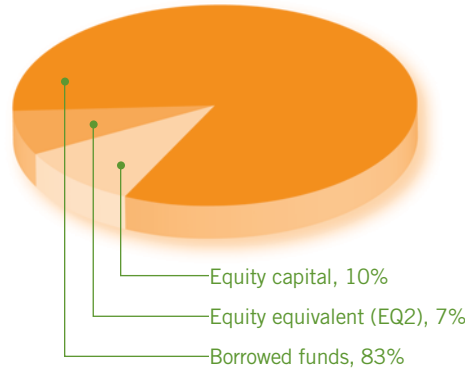
* Banks did not provide a breakout of borrowed funds.

Figure 7: CDFI Capital Structure

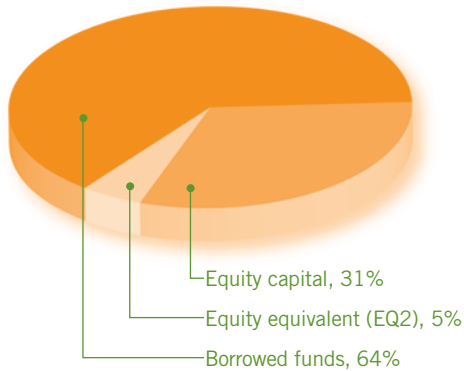
Credit Unions



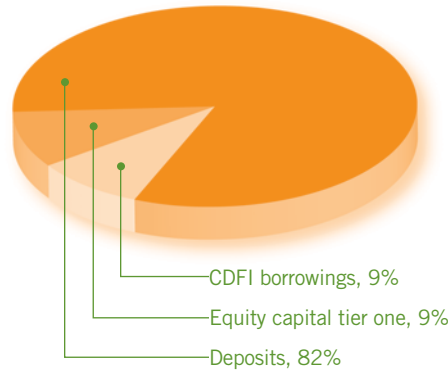
Venture Funds



Loan Funds



Banks



The different types of CDFIs have very different capital structures. Loan funds receive the greatest percentage of capital in the form of borrowed funds (64%), venture funds in the form of equity capital (83%), credit unions in the form of shares (86%), and banks in the form of member deposits (82%). (See Figure 7.)

Markets Served

CDFIs tend to concentrate in certain areas of the country. The Northeast, the Upper Midwest, Texas, and California each have a high concentration of CDFIs, with New York, California, Texas, Pennsylvania, and Illinois having the greatest number of CDFIs. CDFI financing activity also concentrates in these areas because of the high number of CDFIs there. Five states—Texas, North Carolina, California, New York, and Michigan—are home to the CDFIs that did 59% of total financing activity in FY 2005.⁸ CDFIs in our study are located in 49 states, the District of Columbia, and Puerto Rico.

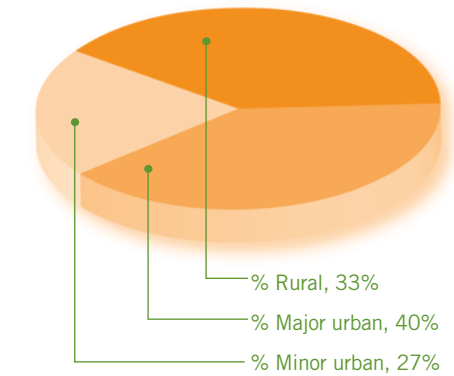
CDFIs serve a mix of rural and urban markets across the country, with 40% of CDFI clients being from major urban areas,⁹ 33% from rural areas, and 27% from minor urban areas

(see Figure 8).¹⁰ All of the CDFI types have similar patterns of geographical coverage, with rural CDFIs the most alike across CDFI types with all CDFI types serving between 29% and 35%. Banks serve the highest percentage (49%) of clients in major urban areas.

The FY 2005 data set included 275 CDFIs that reported the breakout of the geographic area they served. Ninety-one reported serving primarily a rural market,¹¹ and 184 reported serving primarily an urban area (See Figure 9). The data set also includes 37 CDFIs that serve a 100% rural market and 50 CDFIs that serve a 95% rural market. The CDFIs that serve a 100% rural market included 19 loan funds, 17 credit unions, and one VC fund.

Geographical markets served by CDFI types vary significantly, ranging from a city or town to a national service area (see Figure 10). In general, credit unions tend to serve smaller geographical markets, including cities, towns, and metropolitan areas, because their customers are typically in close proximity to the credit union, often going to the actual credit union branch for services. Venture funds, on the other hand, cover larger geographical

Figure 8: Rural and Urban Distribution of CDFIs

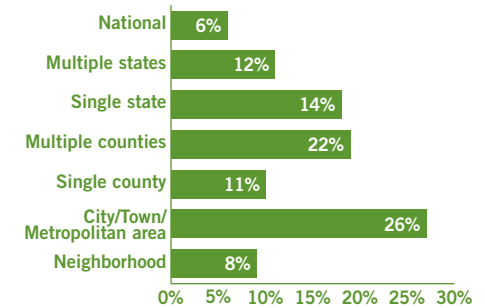


Note: n = 275.

Figure 9: Primary Area Served

	All	Rural	Urban
All	275	91	184
Banks	10	3	7
Credit unions	115	37	78
Loan funds	136	47	89
Venture capital funds	14	4	10

Figure 10: Geographic Markets Served



areas. Eighty percent serve a state, multistate, or national service area because their specialized equity products require a larger market area to operate efficiently. Loan funds vary in their markets served, with 55% serving either a single state or multiple counties. FY 2005 was the first time no loan funds serviced a single neighborhood, as even the smallest loan funds are expanding their area served. Many loan funds began by serving a smaller area but have since developed niche products and have expanded to a larger service area.

⁸ Although 49 CDFIs in our study serve a multistate or national population, all of their financing is captured in the state where the CDFI is located.

⁹ Major urban area is defined as a metropolitan statistical area greater than 1 million residents.

¹⁰ Minor urban area is defined as a metropolitan statistical area less than 1 million residents.

¹¹ CDFIs that cover 50% rural and 50% urban areas are considered to serve a primarily rural area.

Focus On Diversity

Figure 11: Summary of Staff, Board, and Client Diversity Data

		Female		Minority	
		n	(%)	n	(%)
FTEs	All	276	69%	271	45%
	Banks	9	65%	9	63%
	Credit unions	115	78%	115	63%
	Loan funds	138	65%	123	28%
	Venture funds	14	51%	14	28%
	Rural	88	72%	85	20%
	Urban	176	68%	167	58%
	> 50% female clients	125	76%	120	57%
	> 50% minority clients	138	71%	135	73%
	> 95% low-income clients	31	80%	31	50%
	< \$2 million capital	78	70%	72	59%
	> \$2 million and < \$10 million	105	70%	96	45%
	> \$10 million and < \$50 million	67	68%	67	33%
> \$50 million	27	69%	26	38%	
Primary lending sector FTEs	Business	89	61%	80	31%
	Housing	69	68%	77	39%
	Community service	10	70%	10	22%
	Personal development	84	79%	84	68%
Board	All	285	39%	270	41%
	Banks	9	21%	9	74%
	Credit unions	115	43%	115	58%
	Loan funds	146	38%	131	26%
	Venture funds	15	33%	15	21%
	Rural	87	38%	84	24%
	Urban	181	40%	173	50%
	> 50% female clients	126	46%	121	53%
	> 50% minority clients	143	40%	139	66%
> 95% low-income clients	31	49%	31	48%	
Primary lending sector board members	Business	92	36%	85	27%
	Housing	78	39%	78	33%
	Community service	10	46%	10	20%
	Personal development	84	44%	84	63%

Figure 12: Staff Diversity

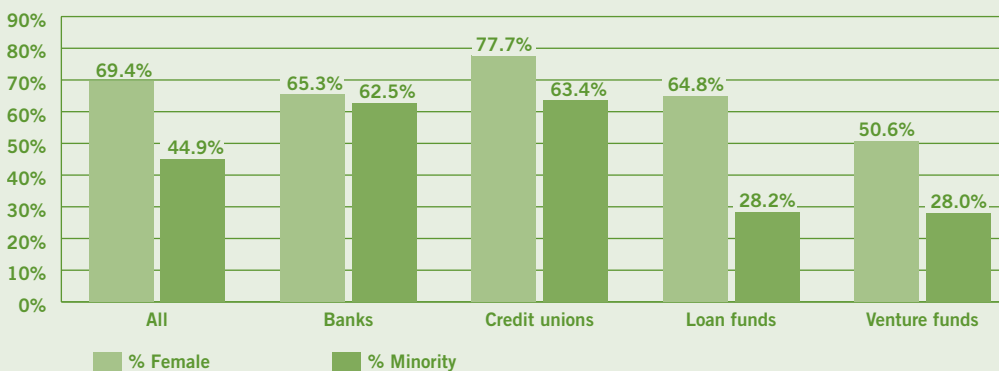
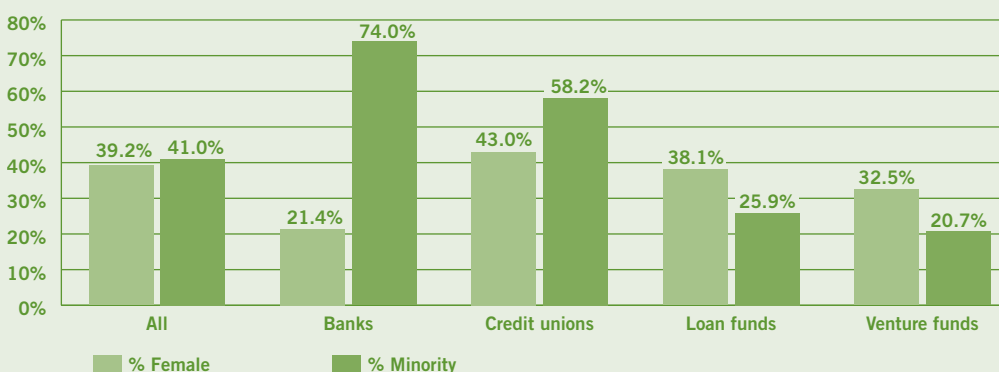


Figure 13: Board Diversity



Substantial diversity exists within the staff and boards of CDFIs. The average percentage of female workers is 69%, ranging from 78% at credit unions to 51% at venture funds. There is little difference between percentages of female employees among CDFIs with capital between \$10 million and \$50 million averaging at 68% and CDFIs with between \$2 million and \$5 million in capital averaging at 70%. CDFIs have an average of 45% minority staff, ranging from 63% at credit unions to 28% at loan funds and venture funds. (See Figure 12.) The size of a CDFI does have an impact on the percentage of minority staff; the smallest CDFIs with capital less than \$2 million average the highest percentage of minority staff, at 59%. The mix of rural versus urban also has a large impact: rural CDFIs have 20% minority staff, while urban CDFIs have 58%. CDFIs that do lending for personal development, primarily credit unions, have the highest percentage of minority and female staff—68% and 79%, respectively.

CDFIs also have highly diverse boards. Board members come from financial institutions, law firms, government agencies, local businesses, housing developers, and the communities that the CDFIs serve. CDFI boards are made up of 39% female and 41% minority members, on average (see Figure 13). CDFIs that do community service lending have the highest percentage of female board members (46%), while CDFIs that do personal development lending have the highest percentage of minority board members (63%).

Focus on Rural CDFIs

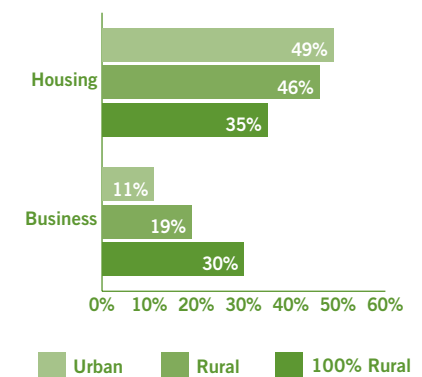
CDFIs that operate in a rural environment face several unique challenges and opportunities related to their strategy, operations, and capitalization. Some highlights include the following (see also Figure 14):

- Rural CDFIs tend to be smaller and to make smaller loans. Rural CDFIs averaged loans outstanding of \$14,541,283—much smaller than urban CDFIs, which average \$26,088,411. CDFIs that serve 100% rural markets averaged loans outstanding of \$8,331,843.
- Rural communities have many more business CDFIs than housing CDFIs, most likely reflecting the lower access to conventional business development capital in rural areas. The percentage of direct financing outstanding for business is much greater for rural CDFIs (19%), increasing to 31% for CDFIs that serve greater than 95% rural areas. Of the twelve CDFIs that serve greater than a 95% rural market, eleven provide only business financing, and one provides only housing financing.
- Rural CDFIs received a greater amount of their capital from government. The rural CDFIs in our sample received 14% of their debt capital from federal and state governments, while urban CDFIs received only 4% of their debt capital from government sources. In contrast, rural CDFIs received 9% of their debt capital from banks, thrifts, and federal credit unions, whereas urban-based CDFIs received 24% of their debt

capital from such institutions. One reason for this is that far fewer lenders and more segmented markets exist in rural areas, resulting in reduced competition among lenders. Another reason is that the federal government has several programs specifically geared for rural communities, the largest being the Intermediary Relending Program of the U.S. Department of Agriculture (USDA).

- Rural CDFIs are forging partnerships to achieve their missions and greater efficiency. It is becoming increasingly important for CDFIs in rural areas to work with local governments, universities, banks, businesses, and other CDFIs to support entrepreneurship and other community development activities.

Figure 14: Financing Outstanding by Housing and Business Sectors



	All	Rural	Urban	100% Rural
Number of CDFIs	275	91	184	37
Total Assets	\$8,862,119,751	\$2,154,205,468	\$6,707,914,283	\$458,953,836
Average Assets	\$32,225,890	\$23,672,588	\$36,456,056	\$12,404,158
Average Total Direct Financing Outstanding per CDFI	\$22,977,037	\$14,541,283	\$26,088,411	\$8,331,843
Average Size of Direct Financing Outstanding	\$89,405	\$54,509	\$106,650	\$33,734
% of Debt Capital from: (a) (b)	n = 254	n = 84	n = 170	n = 37
Banks, Thrifts, and Credit Unions	21%	9%	24%	9%
Corporations	1%	2%	1%	3%
Federal Government	4%	10%	2%	8%
Foundations	6%	9%	5%	13%
Individuals	57%	56%	57%	55%
National Intermediaries	2%	3%	1%	3%
Nondepository Financial Institutions	3%	1%	4%	1%
Other	3%	4%	2%	2%
Religious Institutions	2%	3%	2%	2%
State Government	2%	4%	2%	4%

(a) Debt Capital includes borrowed funds, EQ2, secondary capital; shares and deposits; Debt Capital breakout does not include Credit Union borrowings.

(b) Two outliers are excluded from debt capital breakouts.



Focus on Revitalizing Rural Communities

Featuring Southern Bancorp

*To left and below: Students of the KIPP
Delta College Preparatory School*

For almost 20 years, **Southern Bancorp** (Southern) has operated a family of banks and development companies that work in concert with one another to promote development in rural Arkansas and the Delta region of Arkansas and Mississippi. Southern is made up of several CDFIs including a community development loan fund housed in Southern Financial Partners as well as three community development banks: Delta Southern Bank, Elk Horn Bank and First Bank of the Delta. With \$537 million in assets, 40 locations in rural Arkansas and Mississippi and over 250 employees, Southern Bancorp is the largest rural development banking organization in the United States.

Southern is currently engaged in a long-term project to create a cluster of revitalized communities in the Delta that can support development within a 50 mile radius and, through the conflux of areas of influence, change the region as a whole. The first site for the Delta Bridge Project is Phillips County, Arkansas. Phillips County represents a staggering economic development challenge, with a poverty rate of 30%, a population decline of 49% since 1960, a recent history of industries closing or moving, and a history of racial division and social dissension.

Southern's strategy is to revitalize communities in the Delta and the region as a whole. Southern has worked with a broad cross-section of Phillips County residents and organizations to create a strategic plan for revitalizing the community which provides a blueprint for community action. The implementation stage is led by the community itself, with Southern providing an array of development services, targeted investments, and technical assistance. Southern has partnered and gained the support of the local partners including, nonprofits, faith-based organizations,

academic organizations, and the governor of Arkansas as well as other public servants in this project. They also have partnered with the Walton Family Foundation and the USDA to provide money for the projects. The Delta Bridge Project is already showing tremendous results in Phillips County, including a 40 million gallon per year biodiesel facility, a \$2 million sweet potato processing facility, a \$4.5 million health and wellness center, a 20-unit affordable housing development, and a Boys & Girls Club. In all, Southern has invested over \$9 million in Phillips County through the Delta Bridge Project and has leveraged this investment to bring in another \$43 million in outside resources. A more intangible indicator of progress, but one that is crucial, has been a renewed sense of optimism and civic engagement in Phillips County.

KIPP Delta College Preparatory School:

Southern Financial Partners and First Bank of the Delta teamed up with the United States Department of Agriculture to provide financing and grants to help start the KIPP charter school in Helena-West Helena, Arkansas. The 95 percent African American middle school has been astonishingly successful—the first cohort of students has gone from a mean 20th to 90th percentile on standardized tests in four years. Southern is now working with KIPP on a \$25 million campaign to build a new high school campus and, eventually, to expand the program to cover grades K-12. Southern's support for the KIPP school has included a \$1.2 million loan, a \$40,000 grant to hire a director of development, a \$250,000 grant to develop a comprehensive expansion plan and to purchase land for the new campus, and most recently a \$400,000 grant to provide temporary classroom space for grades 10 and 11.



CDFI Outcomes, Impacts, and Clients

These results include helping borrowers open their first formal bank account, improving financial literacy or entrepreneurial skills, opening bank or credit union branches in markets not typically served by financial institutions, and providing much-needed technical assistance.

CDFI Client Characteristics

CDFIs are successful in reaching customer groups that others overlook—low-income families, minorities, and women, in particular. Sixty-nine percent of CDFI clients are low income, 58% are minorities, and 52% are women (see Figure 15). Credit unions, with their focus on financial services to low-income individuals, had the highest percentage of low-income clients (73%). Credit unions also had the highest percentage of minority and female clients, showing their reach and accessibility for everyone (see Figure 15). CDFIs with a focus on community service lending serve the largest percentage of female and low-income borrowers (66% and 81%, respectively), while CDFIs that focus on personal development lending serve the highest minority percentage (76%).

CDFI Sectors Served and Outcomes

CDFIs provide financial and nonfinancial services to a variety of sectors and clients.¹² Although there is substantial variation among and between sectors, CDFI activities fall into six main categories: microenterprise, small and medium-sized business, community services, housing, consumer, and other (see Figure 16 for a breakout by sector). CDFIs that finance these different strategies are looking for different outcomes and impacts.

Microenterprise

- \$100 million outstanding at fiscal year-end (FYE) 2005
- 10,308 transactions at FYE 2005
- 5,813 microenterprises financed in FY 2005

Microenterprise development includes financing to businesses that have five or fewer employees and a maximum loan or invest-

CDFIs reach many individuals and communities that other institutions overlook. CDFIs strive for—and achieve—social and economic benefits that align with their institutional missions. The results of the industry’s financing and other products go well beyond easily measurable impacts.

Figure 15: Customer Profile by Institution Type

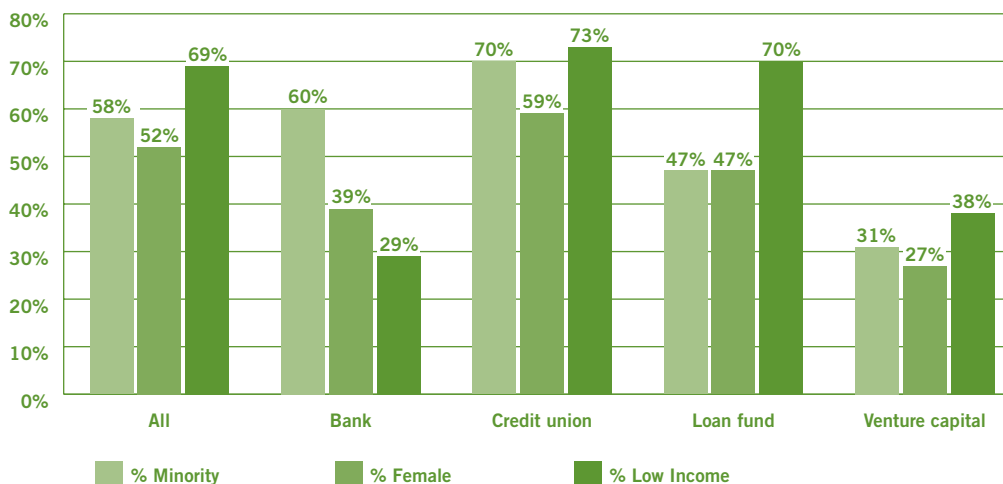
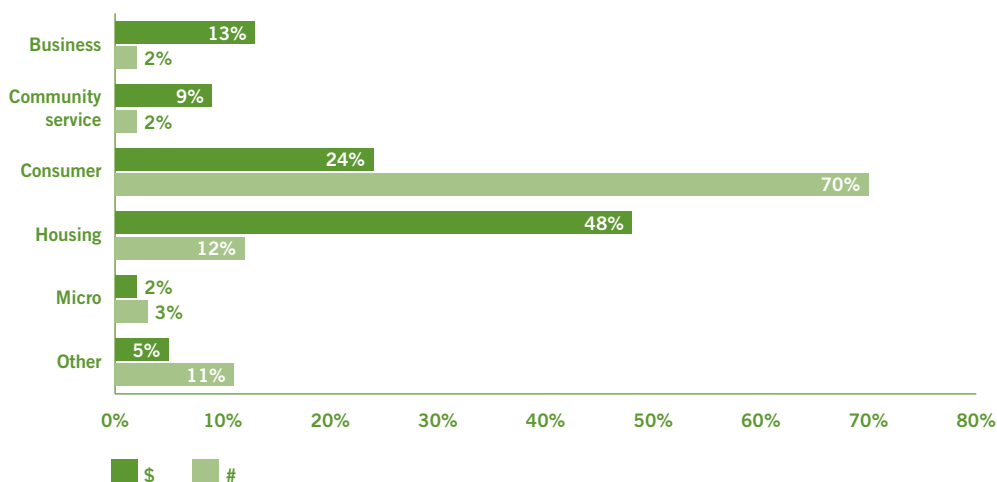


Figure 16: Financing Outstanding by Sector



ment of \$35,000. This financing is typically for the start up or expansion of a business, working capital, or equipment purchase. Clients are typically low- or moderate-income individuals in the very early stages of small business development. They have a skill or idea that they want to turn into a business, but they may lack the capital or the technical and management expertise. Most CDFIs that assist microenterprises provide substantial technical assistance, such as entrepreneurial training, business coaching, and networking opportunities. Microenterprise loans help provide self-employment opportunities for

entrepreneurs, many of whom would not have the opportunity without this financing.

One hundred institutions in our sample reported microenterprise financing in FY 2005. Of these institutions, 72 were loan funds, 26 were credit unions, one was a venture capital fund, and one was a bank. Microenterprise financing is characterized by a high number of transactions and relatively

¹² Several CDFIs cannot break out their financing outstanding into these sectors; therefore, the total figures in each sector underrepresent the total financing activity among sectors.

small dollar amounts of loans. For the loan fund sector in FY 2005, microenterprise financing accounted for only 3% of financing in dollars outstanding but 26% in terms of the number of loans.

Small and Medium-Sized Businesses

- \$739 million outstanding at FYE 2005
- 5,663 transactions outstanding at FYE 2005
- 2,048 businesses financed in FY 2005
- 39,151 jobs created and maintained in FY 2005 (includes activity from microenterprise financing)

Small and medium-sized business development includes loans and equity investments to businesses that have more than five employees or that have financing needs greater than \$35,000. CDFIs consider the benefits of financing, such as how many jobs will be created, what kind of salaries and benefits are offered, whether the business is located in and provides services to a disinvested location, and what the environmental impact of the business will be.

In our sample, 130 CDFIs provided business financing, including all 15 VC funds. Business financing represents virtually all (97%) of the dollar amount of venture fund financing outstanding and smaller percentages of credit union and loan fund financing.

The CDFIs in our study that financed both microenterprise and small and medium-sized businesses created and maintained more than 39,151 jobs.¹³

Housing

- \$2.6 billion outstanding at FYE 2005
- 36,438 transactions outstanding at FYE 2005
- 55,242 housing units assisted in FY 2005
- 15,109 mortgages closed in FY 2005

Housing financing among CDFIs includes two primary subcategories: financing to housing developers and direct mortgage lending to low-income individuals.

CDFIs make loans to housing developers for predevelopment, acquisition, construction, renovation, working capital, and mortgages. These loans support the development of rental housing, service-enriched housing, transitional housing, and residential housing. With a rapidly shrinking supply of affordable housing to low-income families in both the rental and ownership markets, this effort addresses a critical need in many communities. CDFIs facilitated the construction or renovation of 55,242 units¹⁴ of affordable housing in 2005, with 94% of the activity

from CDLFs. These affordable housing units typically provide for monthly payments that run less than 30% of a household's monthly income and enable low-income individuals to own or rent quality housing while preserving sufficient income to pay for other critical products and services.

CDFIs also provide loans to low-income families who cannot qualify for a mortgage from the mainstream financial sector. One hundred and forty-one CDFIs reported providing 15,109 mortgages to home buyers in 2005. They are typically first-time home buyers who also need significant help working through the process. Many CDFIs providing direct mortgage financing also offer homeownership counseling or other services. CDFIs provide this mortgage financing as an affordable product to home buyers and act as an alternative to predatory lenders in the community.

Housing financing is the largest sector, accounting for \$2.6 billion, or 48% of the sample's total dollar amount of financing outstanding broken out by sector. Banks, credit unions, and loan funds all provide substantial amounts of housing financing. Of the top 10 CDFIs to report financing outstanding for housing, four were loan funds, three were credit unions, and three were banks. Credit unions primarily provide mortgage loans to individuals, and loan funds primarily provide loans to housing developers, although there are a growing number of loan funds providing mortgage products as well.

Community Services

- \$485 million outstanding at FYE 2005
- 5,391 transactions outstanding at FYE 2005
- 613 community service organizations financed in FY 2005
- 24,396 new and existing childcare slots assisted in FY 2005
- 32,303 new and existing educational slots assisted in FY 2005

CDFIs supply financing to community services—human and social service agencies, advocacy organizations, cultural facilities, religious organizations, health care providers, childcare centers, and education providers—that offer critical and much-needed services to low-income people and communities. Many community service providers have one or more niche markets in which they operate. This expertise enables them to provide critical advice on issues affecting the particular industry. The borrowers, which are primarily nonprofits, often require some form of technical assistance, such as cash flow forecasting or securing other funds.

Sixty-two CDFIs in our sample provided community service financing, with a majority (52) being loan funds. Community service financing accounted for 9% of all CDFI financing outstanding in FY 2005. In 2005, CDFIs financed 613 community facilities and assisted 32,303 education slots and 24,396 childcare slots in urban and rural areas across the country. CDFIs have an impact on a greater number of education slots each year because of the increased lending to charter schools across the country. Many CDFIs are using the CDFI Fund's New Markets Tax Credit Program to finance charter schools and other community facilities.

Personal Development

- \$1.3 billion outstanding at FYE 2005
- 208,130 transactions outstanding at FY 2005
- 6,152 payday loan alternatives in FY 2005

Consumer financial services are for individuals; they include all personal loans for health, education, emergency, debt-consolidation, transportation, and other consumer purposes. CDFIs also provide nonfinancial services, such as financial literacy training or programs that encourage savings. In many low-income communities, these services are provided not by mainstream lenders but by institutions that specialize in check cashing, payday lending, and wire transfers at exorbitant and predatory rates.

Almost all of the credit unions (97%), as well as nine other CDFIs that were able to break out their financing outstanding, provided personal development, or consumer, financing. Similar to microenterprise financing, consumer financing is characterized by a high number of transactions and relatively small dollar amounts of loans. The consumer financing sector accounts for 70% of all CDFI transactions in our sample but only 24% of the dollar amount of transactions. The median loan size of \$4,526 is substantially lower than that in any of the other financing sectors and is less than half of the median microenterprise loan. Many of these loans are to people who have not previously had a relationship with a financial institution and who do not have a credit history.

¹³ This figure is significantly underreported. It does not capture all self-employment activity of microentrepreneurs, job data from the 170 credit unions for which we have only call report data (see Appendix A), and those CDFIs that do not track this information.

¹⁴ Because CDCUs generally do not track housing units (and these data were not reported from those that did not complete the CDCU survey), housing units are substantially underreported for credit unions.

CDFI Products, Services, and Performance

CDFIs deliver a range of products to meet the needs of their communities, including financing products, retail and depository services (such as savings and checking accounts and individual retirement accounts), training and technical assistance, advocacy and research, and other services that benefit the communities they serve.

Most CDFIs have strong market knowledge and long-term relationships with clients, which help them develop the right mix of products for their markets.

FY 2005 Financing Totals

At the end of 2005, the CDFIs in our study had 536,721 financial investments outstanding (loans, equity, guarantees), totaling \$14.1 billion. Financing outstanding among individual CDFIs ranged widely, with an average of \$29 million. Again, the larger institutions account for a disproportionate share of financing. Ten CDFIs account for more than 41% of total financing outstanding, and 20 CDFIs account for 54% of total financing.

CDFIs generated \$4.3 billion of new financing activity in 2005: \$3.7 billion of direct financing and \$619 million in indirect financing. Direct financing includes loans, equity investments, and debt-with-equity features closed during the year. Indirect financing is made by other financial institu-

tions, in which CDFI intervention (i.e., loan purchase¹⁵ or guarantee) allows the financial institutions to finance additional community development loans and investments. The loans purchased by CDFIs has continued to grow over the years as more CDFIs have begun buying and selling loans.

In addition, many more CDFIs are using their core expertise in underwriting and servicing to provide those services to third-party organizations. Such loans do not flow through the financial statements of the CDFIs but instead provide an important service that allows banks, foundations, government entities, and other entities to invest more in community development projects. In FY 2005, 32 community development loan funds provided loan servicing on portfolios totaling 11,510 loans and \$341 million. Eleven CDFIs provided underwriting for third parties, totaling almost \$83 million, which enabled the CDFIs to finance larger deals and to leverage their expertise and market knowledge.

Figure 17: FY 2005 Financing Totals

		# Respondents
Total financing outstanding in FY 2005 (\$)	14,101,555,439	485
Total financing outstanding in FY 2005 (#)	536,721	429
Total financing closed in FY 2005 (\$)	4,330,109,693	430
Total financing closed in FY 2005 (#)	257,340	427

Note: Total financing outstanding includes loans, investments, and guarantees outstanding; total financing closed includes direct investments (loans and investments) and indirect investments (guarantees and loans purchased).

¹⁵ Loan purchases are not a common activity for most CDFIs. The majority of the purchases are through a single CDFI, which purchases nonconforming home mortgages as a strategy to expand the scope of mortgage lending by mainstream financial institutions to low- and moderate-income borrowers.

Financing Products Offered

CDFIs use four primary types of financing products to serve their communities: loans, equity investments, debt-with-equity features, and guarantees (see Figure 18).

Loans

Loans are far and away the most used tool by CDFIs, representing \$13.9 billion, or 99% of all financing outstanding. Loans represent virtually all financing from loan funds, credit unions, and banks. The only exception is VC funds, which are designed primarily for equity and near-equity investments.

CDFI loans include short-term (fewer than six months) and long-term (up to 30 years) loans, amortizing and balloon loans, and small (less than \$500) and large (more than \$1 million) loans. Loan size varies greatly by the type of CDFI, mainly according to the sectors and clients the CDFI serves (see Figure 19). CDCUs primarily provide small loans to members; as such, the average loan size at credit unions is significantly smaller than at other CDFI types. VC funds have a larger average loan size, as they typically provide larger loans, coupled with investments, to high-growth-potential businesses that have substantial needs for working capital, equipment, or acquisition financing.

As indicated in Figures 19 and 20, the median loan and investment sizes for CDFIs have been increasing over time. As CDFIs have increased their capital, resources, and capacity, they have been able to provide larger loans, in addition to the usual smaller loans, to businesses and individuals. The largest increase has been in the community services sector, increasing from \$76,000 in 2002 to \$127,000 in 2005. This increase results, in part, from several CDFIs that are involved in financing large charter school deals.

Equity Investments

Equity investments are an important tool for CDFIs that finance high growth-potential businesses that offer financial and social returns for low-income people and communities. Equity investments are made in for-profit companies that give the CDFI an ownership interest in the company in exchange for the capital. With an equity investment, the CDFI shares both the risk and the potential financial gain that the business experiences. The relatively recent emergence of equity as a tool is reflected in the comparatively modest

numbers shown for this type of investing. Most such investment activity is concentrated in the VC sector: the \$68 million in 215 equity transactions outstanding represents less than 1% of the overall CDFI financing but 41% of VC financing for the 15 venture funds in the CDP sample. Fifty-four percent of the equity investments made by the CDFIs in the CDP sample were originated by VC funds. Fourteen loan funds made the remaining 46% of equity investments. Some of these loan funds have VC programs within the same corporate structure as the lending entity.¹⁶ Credit unions and banks do not use equity financing. The median investment size outstanding at venture funds was more than \$383,000, and the median at loan funds was less than \$122,000. In FY 2005, 14 CDFIs closed on \$7.4 million in new equity transactions.¹⁷

Debt-with-Equity-Features

Debt-with-equity (dequity) features are loans that allow the CDFI to receive additional payments based on the performance of the borrower's company. Debt-with-equity features include convertible debt, as well as debt with

warrants, participation agreements, royalties, or any other feature that links the investment's rate of return to the performance of the company that received the investment. Eight VC funds (or 53%) and 10 loan funds (7%) use near-equity products. VC funds have always used these products in combination with equity to finance business growth. More recently, loan funds have begun using these products to offer an alternative to debt when the borrower requires more patient capital. In FY 2005, eight CDFIs closed on \$3.0 million in debt-with-equity features. A few CDFIs have started debt-with-equity features lending in the past few years. However, several CDFIs, particularly loan funds, have discontinued or reduced their debt-with-equity programs.

Debt-with-equity features represented only 0.2% of loan fund financing but 7% of VC fund financing. Eighteen CDFIs had debt-with-equity outstanding, representing a range of less than 1% to 36% of their financing outstanding, depending on whether it was a core product or an occasional instrument supplementing other loan and investment products.

Figure 18: Financing Outstanding by Financial Product Type

	Millions of Dollars	Percentage
Loans	\$13,945	98.9%
Debt with equity-like features	\$13	0.1%
Equity	\$68	0.5%
Guarantees	\$76	0.5%

Figure 19: Median Loan and Investment Size by Institution Type, 2002 and 2005

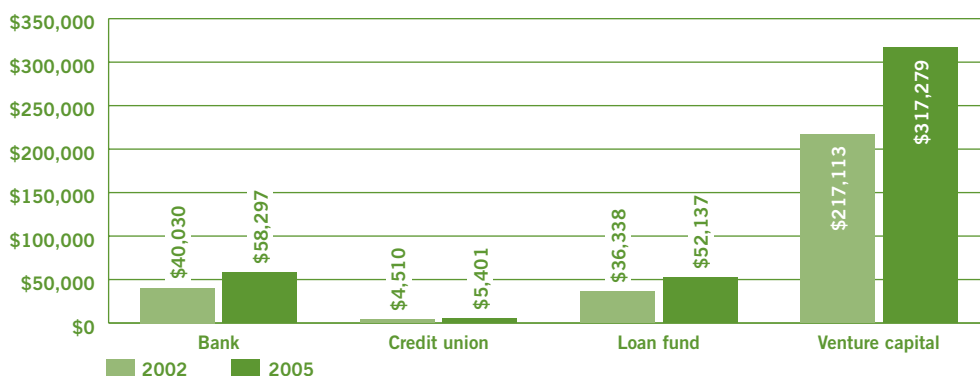
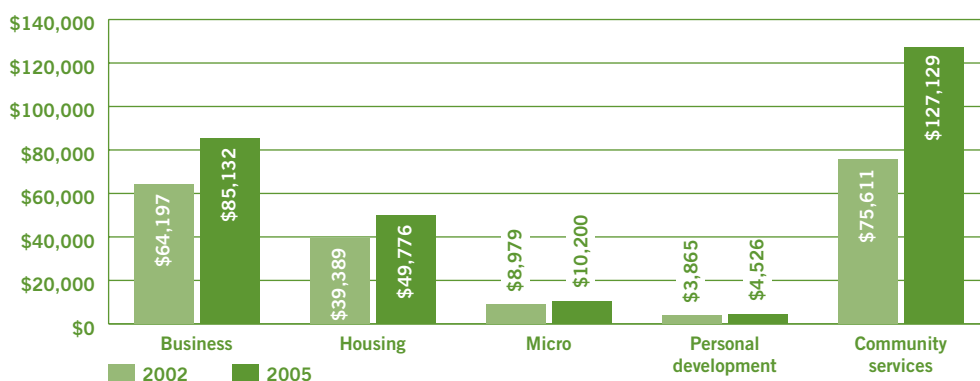


Figure 20: Median Loan and Investment Size by Sector, 2002 and 2005



¹⁶ Some CDFIs are classified as loan funds and have programs within their organizations that do VC investing. Some CDFIs are listed as VC funds and do a substantial amount of lending. Therefore, the VC fund and loan fund categories may underrepresent the lending and investing activity within that given sector.

¹⁷ The venture funds that responded to the CDP survey represent less than a quarter of the overall CDVC industry, as estimated by the Community Development Venture Capital Alliance, the industry's trade association.

Note: The CDP collects data on average loan size per CDFI. The median loan size represents the middle (or typical) loan size of the CDFIs in that sector.

Small Business Financing Duluth, MN

Featuring Northeast Entrepreneur Fund



Like many in the Mid-West the Willoughby household was economically insecure due to a declining industrial sector. Working with the Northeast Entrepreneur Fund, Carol Willoughby was able to add management skills to her background in commercial art, and this allowed her to develop two businesses. One makes hand painted signs for a few hundred customers in the Duluth area. A second spin-off business makes vinyl window appliques that are distributed through over 600 retailers across the United States. What started as a supplemental source of income to help make ends meet, the businesses now are the primary source of income for the Willoughby's, and together they employ an additional two full-time and three part-time staff.

The Northeast Entrepreneur Fund (NEEF) is a community development financial institution (CDFI) that provides loans and guidance to start-up and existing small businesses in northeastern Minnesota and northwestern Wisconsin. Believing that small and micro-businesses are crucial elements of community-based economic growth, NEEF works to foster entrepreneurial spirit and self-employment opportunities. NEEF helps people with planning, expansion, strategy and goal development.

To left: Small business owner Carol Willoughby with Mary Mathews, Northeast Entrepreneur Fund President.

Guarantees

Guarantees include letters of credit or guarantees provided to enhance the creditworthiness of a borrower receiving a loan from a third-party lender. CDFIs in our sample had \$76 million in guarantees at the end of 2005. Guarantees and letters of credit come in different structures, but all enable other financial institutions to participate in more community development lending activity, because a loan or a portion of the loan that the financial institution makes is guaranteed to be repaid by the CDFI in the event of default. Some are tied to a specific program (e.g., Small Business Administration or the State of California Trust Fund), and some are part of a CDFI's general product mix. Guarantees also help keep interest rates reasonable, as the financial institution is not taking as great a risk because of the guarantee. Two CDFIs represent a large majority—nearly 83%—of the guarantees outstanding. In total, 21 CDFIs used guarantees, including 19 loan funds and two VC funds.

Portfolio Performance

For the industry as a whole, portfolio performance has been strong and consistent during the past few years. Figure 21 demonstrates delinquencies and loan losses at banks, credit unions, and loan funds. CDCUs measure

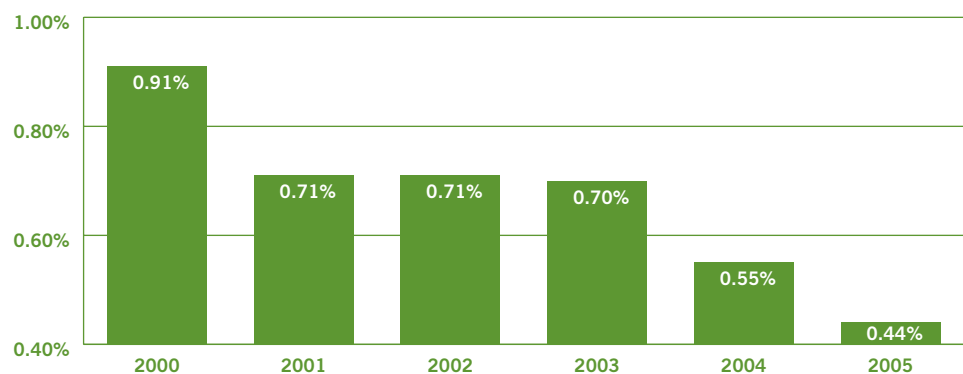
delinquency rates by different metrics than do loan funds and banks. Delinquency and loan losses are not reported for VC funds, as they measure portfolio performance by the overall return on the fund. Overall, net loan loss rates¹⁸ for these groups of CDFIs was 0.44%, ranging from a total of 0.2% in the bank sector to 0.8% in the credit union sector; this outperforms the net loan loss ratio of 0.6% at

conventional financial institutions in 2005. While there is substantial variation among CDFIs, only 15 CDFIs, or 3% of the 463 banks, credit unions, and loan funds that reported these data, had net loan loss rates greater than 10%. Figure 22 demonstrates how the loss rate for the overall industry has been slowly declining during the past few years.

Figure 21: Delinquency and Loan Loss Rates

	Banks	Credit unions	Loan funds
2005 net loan loss ratio	0.2%	0.8%	0.6%
Delinquency ratio > 90 days	1.5%	NA	2.4%
Delinquency ratio > 2 months	NA	1.7%	NA

Figure 22: Net Loan Loss Rates, 2000-2005



¹⁸ Net loan loss rate is the net charge-offs during FY 2005/total loans outstanding at FYE 2005.

CDFI delinquency rates are somewhat higher than their net charge-off rates. CDFIs are able to manage these delinquencies through technical assistance and frequent contact and monitoring of their borrowers. CDFIs also keep adequate loan loss reserves and equity bases to further protect their investors.

Financial Services

Banks and credit unions mobilize savings and provide access to credit. Data on deposit and transaction products were collected from 104 credit unions and eight banks for FY 2005. These institutions offered a broad range of products, such as savings accounts, checking accounts, certificates of deposit, and IRAs, as well as client services, such as automated teller machine (ATM) access, check cashing, bill payment, and direct deposit. They have also crafted products unique to the field, such as individual development accounts (IDAs), which use a mix of financial education, peer support, and matching funds to promote savings among low-income customers that can be used to invest in homeownership, small business development, or education.

Among credit unions and banks, direct deposit is the most widely offered service, followed by wire transfers and electronic funds

transfer (see Figure 23). Alternatives to payday loans—exorbitantly high-interest short-term loans secured by the borrower’s next paycheck—are also reported by 29% of the banks and credit unions. Although many customers view these depositories as being just like any other financial institution, the difference lies in the customer base and the communities that the organizations seek to serve.

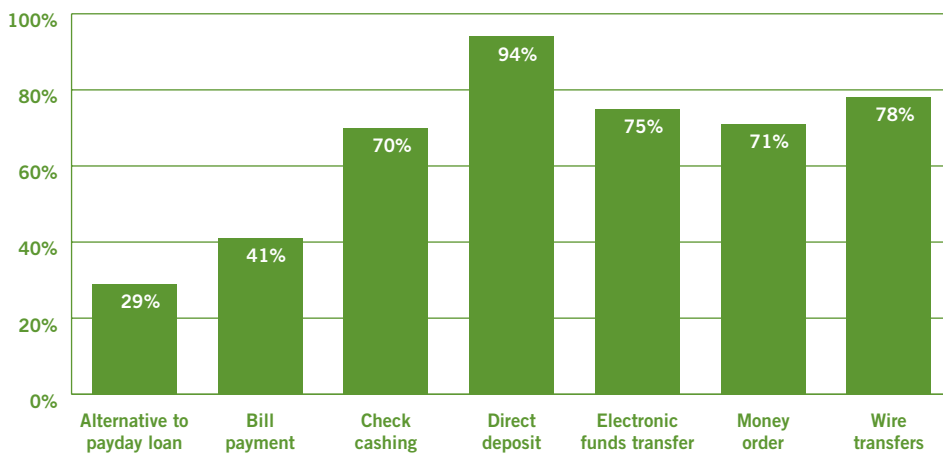
Training and Technical Assistance Services

In addition to providing access to capital and retail financial services, CDFIs are distinct from mainstream lenders because they provide training, technical assistance, and other assistance to help increase their customers’ capacity and access to financing. The type and amount of training and technical assistance a CDFI offers depend on the needs in its market, whether those needs include packaging funding for an affordable housing developer, business plan training for an entrepreneur, or credit counseling for an individual. CDFIs provided approximately 9,600 organizations and more than 181,000 individuals with group-based training and one-on-one technical assistance.

Focus on New Markets Tax Credit (NMTC) Investing

CDFIs are taking advantage of the NMTC program to invest growing dollars in low-income communities. This innovative \$15 billion program administered by the federal CDFI Fund provides a tax incentive for private investors to invest capital through intermediaries into low-income communities. The 15 CDFIs that reported this data financed more than \$509 million in 95 NMTC deals, representing an average deal size of nearly \$5.4 million. The NMTC program benefits investors, CDFIs, and the projects by providing investors with market-rate (or near-market-rate) returns on investments, borrowers with favorable financing for high-impact deals in emerging markets, and CDFIs with capital to finance larger projects and with income generated through fees to sustain financing operations and to support their capital base. A key benefit of the program is that a variety of deals can be financed, including commercial real estate, businesses, and community facilities, such as charter schools, childcare centers, and health care facilities. For the CDFIs that reported this data, NMTC deals in 2005 financed commercial real estate (40%), business (11%), community facilities (31%), housing (5%), and other (14%).

Figure 23: Financial Products and Services at Depositories



Note: Alternatives to payday loans includes only credit unions reporting.

Figure 24: Training and Technical Assistance

	People or Organizations	CDFIs reporting
People receiving group-based training	85,690	144
People receiving one-on-one technical assistance	95,569	175
Organizations receiving training	9,596	109

Manufactured Housing Financing North Hero, Vermont

Featuring Opportunities
Credit Union



Carolyn and Jim Barber came to **Opportunities Credit Union** (Opportunities) in 2004 for financial counseling after several challenging life events.

Jim became disabled, forcing him to close his business. As a result, many of their bills lapsed, and he was forced to declare bankruptcy.

Their goal was to purchase a manufactured home in North Hero, Vermont, which they were renting from Carolyn's parents. Determined to overcome their financial challenges, they came to Opportunities looking for a manufactured home loan. After two years of counseling and a lot of determination, the Barbers completed their action plan, improved their credit and qualified to purchase their home.

Opportunities works closely with financial institutions and non-profits to secure grants to help modest-income Vermonters reach their goal of homeownership. Opportunities informed Carolyn and

Jim of three different grants available to help with down payments and closing costs for their manufactured home. They applied for and received three grants, totaling \$35,000 from Federal Home Loan Bank of Boston, the American Dream Downpayment Initiative by the Vermont Housing and Conservation Board, and the Vermont Community Development Program.

Opportunities is an affordable housing lender in Vermont. Opportunities creates options for members of modest income to reach their goal of homeownership when they have been left behind by traditional financial institutions. Their financing supports the increasing demand for affordable housing in Vermont, and is making dreams come true for lower-income Vermont families.

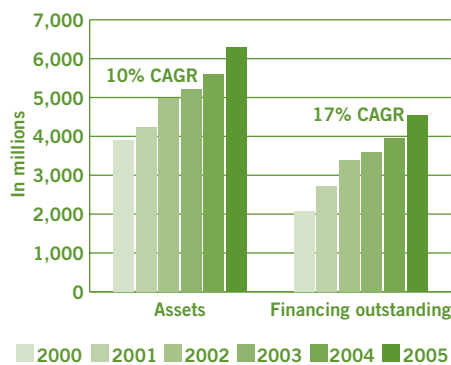
To left: Carolyn and Jim Barber in front of their home.

CDFI Growth from 2000 to 2005

CDFIs experienced growth in the past five years. For the CDFIs for which we have six years of data (224 CDFIs), their assets grew at a CAGR¹⁹ of 10% between 2000 and 2005; financing outstanding for the sample grew by 17% (see Figure 25).

CAGRs at individual CDFIs varied significantly. Twenty-eight percent of the sample experienced CAGRs in financing outstanding from 2000 to 2005 of greater than 25% (see Figure 26). Fifteen percent of the sample experienced declines in the financing outstanding. This results from having repayments in their portfolio during the five-year period greater than the amount of new financing closed.

Figure 25: Growth from 2000 to 2005



Note: Chart includes 224 CDFIs for which we have six years of data.

Figure 26: Growth Distribution of Financing Outstanding



Note: Chart includes 224 CDFIs for which we have six years of data.

¹⁹ CAGR is the rate of increase over a period of time that would exist if the rate of return were exactly the same each and every year.

Appendix A: Methodology

As partners in the CDP, five national trade associations and intermediaries—Aspen Institute, Community Development Venture Capital Alliance (CDVCA), National Federation of Community Development Credit Unions (NFCDU), Opportunity Finance Network, and National Community Investment Fund (NCIF)—worked together as the Data Collection and Cleaning Committee to collect data across the four types of CDFIs.

Each data collector was responsible for collecting CDP data from its member or constituent CDFIs. Opportunity Finance Network acted as project manager, consolidating all of the data collected.

The Data Collection and Cleaning Committee defined common data points and definitions across the various institution types and developed data-cleaning protocols that all data collectors were required to follow. Opportunity Finance Network, as data consolidator, also applied financial formulas during data consolidation to perform further quality assurance. Each trade association was responsible for designing its own survey instruments for distribution to its constituent CDFIs. The instruments were based on consensus language that defined cross-sector CDP data points, as well as on language appropriate for individual CDFI sectors.

Overall, the CDP sent out 626 surveys for FY 2005 and compiled data for 496 CDFIs, a response rate of 79%—a decrease of 6% from 517 CDFIs in FY 2004. This data set represents one of the largest and most comprehensive samples of the CDFI data to date in the field. Nonetheless, it represents only a subset of CDFI industry.

Each CDFI reported information based on its own fiscal year, which may be different from the calendar year and may vary from institution to institution.

Not all questions were relevant to all CDFIs and thus were not answered by every institution. In addition, some CDFIs were unable to answer some of the survey questions. As a result, the number of responses to individual questions may frequently be less than the total study size and is noted accordingly.

Use of Public Data for Credit Depositories

The CDP sent surveys to 280 CDCUs for FY 2005. The survey requested data on organizational characteristics, financial position, products and services, and community development outputs as of the end of FY 2005.

A total of 116 credit unions (42%) sent back completed questionnaires. For 164 nonresponding credit unions, financial data were obtained from regulatory “call reports” prepared by all federally insured U.S. credit unions. Data on nonfinancial fields were unavailable for nonrespondents.

Consequently, when a survey question sought the same information provided on the call report, those data were obtained for all 280 CDCUs. Thus, it was possible to include an aggregated tally for the whole CDCU movement (as defined by this study) for those data points. For those survey questions, the sample size was all 280 credit unions. For requested data unique to the survey (and thus not available for nonrespondents), this report presents only the numbers drawn from the respondents. The sample size in such cases is limited to the 116 institutions that responded.

The CDP sent surveys to 55 community development banks for FY 2005. The survey requested data on organizational characteristics, financial position, products and services, and community development outputs as of the end of FY 2005. A total of 13 sent back completed surveys. For the 32 nonresponding community development banks, publicly available data was obtained from the FDIC Web site for a limited number of data points.

Appendix B: Glossary of Terms

Staffing and Governance

full-time equivalents (FTEs): Includes full- and part-time employees of the organization and volunteers who fill regular staff positions. Excludes temporary staff and professional services conducted outside of the office by third parties, such as accounting, bookkeeping, and legal counsel. One FTE is at least a 35-hour workweek.

specialized staff (FTEs): Staff dedicated to one or more specific functions.

> **lending/investing:** Includes all FTEs performing the following functions: portfolio management, loan/investment underwriting and outreach, and loan/investment administration.

> **training and technical assistance:** Includes all FTEs providing training and technical assistance. Training refers to a forum such as a workshop, while technical assistance is customized to an individual or specific organization.

> **financial services:** Includes all FTEs providing services such as savings products, checking accounts, and other services (e.g., wire transfers). Includes all work performed by tellers.

Capital Available for Financing

capital under management (venture capital, VC):

Traditional VC funds, organized as limited lifespan funds, are described in terms of their *capital under management*, not their *total assets*, as are banks, credit unions, and loan funds. Capital under management is the total amount of capital that investors have committed to the fund and includes drawn and undrawn capital. The chapter on CDVC funds reports CDVC capital under management by summing the capital commitments for each of the limited lifespan CDVC funds and the total assets for each of the evergreen funds.

total lending/investing pool or capital available for financing: Includes all capital for lending and investing held by a CDFI, as of FYE 2005. This lending/investing pool includes only capital shown on the statement of financial position as received—it does not include capital commitments, grants receivable for capital, or undrawn funds, with the exception of the venture fund sector (which includes committed capital).

total lending/investing pool: borrowed funds + deposits + shares + nonmember deposits + secondary capital + equity equivalent investments + equity capital.

> **borrowed funds:** Loans payable related to financing. Also referred to as debt capital or investor capital. Funds lent to a CDFI from a third party that the CDFI will relend or reinvest in the communities it serves.

> **deposits:** Funds placed in a depository institution by individuals or organizations, typically earning interest and insured by governmental agencies.

> **shares:** A deposit made in a credit union that confers ownership rights in the credit union on the depositor.

> **nonmember deposits:** Funds placed in a credit union by individuals or organizations that are not members of the credit union. Nonmember deposits do not confer ownership rights in the credit union to the depositor and are typically limited to a small percentage of a credit union's total deposits.

> **secondary capital:** A specific type of capital used only by low-income designated credit unions. It is defined by the NCUA as having several key characteristics: uninsured, subordinate to all other claims, minimum maturity of five years, and not redeemable prior to maturity.

> **equity equivalent investments (EQ2s):** Unsecured debt that has some of the same advantages as equity because it is subordinate to all other debt and carries a rolling term, the investor has a limited right to accelerate payment, and interest is not tied to income. The investing bank also receives advantageous CRA credit.

> **equity capital:** Also referred to as *net assets dedicated to lending* by nonprofit loan funds and as *equity* by credit unions, banks, and venture funds. It is the amount of equity at the CDFI that is available for lending or investing.

Capital Sources

nondepository financial institutions: Includes all financial institutions that are not banks, thrifts, or credit unions, including mutual funds, insurance companies, and finance companies.

Sectors Served

business: Financing to for-profit and nonprofit businesses with more than five employees or in an amount greater than \$35,000 for the purpose of start-up, expansion, working capital, equipment purchase/rental, or commercial real estate development or improvement.

community services: Financing to community service organizations such as human and social service agencies, advocacy organizations, cultural and religious organizations, health care providers, and childcare and education providers. Uses include acquisition, construction, renovation, leasehold improvement, and expansion loans, as well as working capital loans and lines of credit.

consumer financial services: All personal loans (secured and unsecured) to individuals for health, education, emergency, debt consolidation, and consumer purposes. In general, personal loans for business are classified as microenterprise or business; personal loans for home improvement or repair are classified as housing.

housing: Financing to housing developers for predevelopment, acquisition, construction, renovation, lines of credit, working capital, and mortgage loans to support the development of rental housing, service-enriched housing, transitional housing, or residential housing. Includes loans to individuals to support homeownership and home improvement.

microenterprise: Financing to for-profit and nonprofit businesses with five or fewer employees (including proprietor) and with a maximum loan/investment of \$35,000. This financing may be for the purpose of start-up, expansion, working capital, equipment purchase/rental, or commercial real estate development or improvement.

other: Any activities not covered in the sectors defined here (includes financing to other CDFIs).

Financing Outstanding

debt-with-equity-features: Includes convertible debt, as well as debt with warrants, participation agreements, royalties, or any other feature that links the investment's rate of return to the performance of the company that received the investment.

equity investments: Investments made in for-profit companies in which the CDFI receives an ownership interest in the equity (stock) of the company.

loan loss reserves: Funds set aside in the form of cash reserves or through accounting-based accrual reserves that serve as a cushion to protect an organization against potential future losses. Loan loss reserves typically show up as a contra-asset on the balance sheet.

guarantees: Includes guarantees or letters of credit provided to enhance the creditworthiness of a borrower receiving a loan from a third-party lender.

total loan losses: The net amount charged off. Losses are reported after default, foreclosure, and liquidation and are the net of any recovered assets. If any amount is reclaimed in the current fiscal year on loans/investments that were written off in previous years, that amount is subtracted from the amount written off in the current fiscal year.

total loans outstanding: The number of loans for which principal was outstanding as of the last day of the fiscal year. These loans may have originated during the fiscal year or in a previous year. This number includes any loans that have been restructured, but not those loans that have been written off.

Deposit Products and Services

individual development accounts (IDAs):

Matched savings accounts, similar to 401(k)s, that can be used by low-income households to purchase homes, seek postsecondary education, capitalize small businesses, or engage in other types of economic development activities.

Geographic Area Served

major urban area: A metropolitan statistical area of equal to or greater than 1 million. Includes both central city and surrounding suburbs.

minor urban area: A metropolitan statistical area of less than 1 million. Includes both central city and surrounding suburbs.

rural: All areas outside major urban and minor urban areas.

Clients Served and Outcomes

housing units created: Includes new construction, units projected to be constructed, or complete rehabilitation of existing housing units that were previously unoccupied.

housing units renovated or preserved: Renovated includes units that have been renovated or are projected to be renovated. Preserved includes mark-to-market and similarly preserved units.

jobs assisted: jobs created + jobs maintained.

jobs created: The change in the number of jobs at a microenterprise or business financed between two fiscal years (i.e., the net job change). When calculating the number of jobs at the microenterprise or business, only permanent FTE jobs are counted.

jobs maintained: Total number of employees at a microenterprise or business financed at the time a given loan or investment closed.

low-income: A customer who has an annual income, adjusted for family size, of not more than 80% of the area median family income for metropolitan areas, or the greater of (1) 80% of the area median family income or (2) 80% of the statewide nonmetropolitan area median family income for nonmetropolitan areas.

The CDFI Data Project

The CDFI Data Project

The CDFI Data Project (CDP) is an industry collaborative that produces data about CDFIs. The goal of the CDP is to ensure access and use of data to improve practice and attract resources to the CDFI field. The CDP collected FY 2005 data on 496 CDFIs. The data set includes approximately 170 data points on operations, financing, capitalization, and impact. Supported by the Annie E. Casey Foundation, the Ford Foundation, the John D. and Catherine T. MacArthur Foundation, HSBC Bank USA, Wachovia Foundation, and the W. K. Kellogg Foundation, this initiative convenes leading organizations in the CDFI industry.

Partner Organizations

> **Aspen Institute**
www.fieldus.org

National nonprofit that disseminates best practices and educates policymakers, funders, and others about microenterprise

> **Association for Enterprise Opportunity**
www.microenterpriseworks.org

National member-based trade association of more than 500 microenterprise development programs

> **Coalition of Community Development Financial Institutions**
www.cdfi.org

Lead organization in the United States that promotes the work of CDFIs

> **Community Development Venture Capital Alliance**
www.cdvca.org

Certified CDFI intermediary that serves community development venture capital funds through training, financing, consulting, research, and advocacy

> **CFED**
www.cfed.org

National nonprofit that promotes asset building and economic opportunity strategies, primarily in low-income and distressed communities

> **National Community Investment Fund**
www.ncif.org

Certified CDFI that channels equity, debt, and information to locally owned banks, thrifts, and selected credit unions with a primary purpose of community development

> **National Federation of Community Development Credit Unions**
www.cdcu.coop

Certified CDFI intermediary that serves more than 200 low-income credit unions across the United States

> **Opportunity Finance Network**
www.opportunityfinance.net

Leading national network that finances, trains, consults with, and advocates for CDFIs

For more information on the CDFI Data Project, contact any of the partner organizations or Jon Schwartz of Opportunity Finance Network at jschwartz@opportunityfinance.net (215.320.4308).