Carolina Small Business DEVELOPMENT FUND

Revolving Loan Funds and Community Development Financial Institutions (CDFIs)

Efficient Promoters of Local Economic Growth

This brief is produced as part of CSBDF's research program on community and economic development. For the full version of the analysis, please visit carolinasmallbusiness.org/research. If you or your organization have an interest in supporting CSBDF's programs, we invite you to learn more about opportunities to give at carolinasmallbusiness.org/give.

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What are loan fund CDFIs and how do they help the community?

Carolina Small Business Development Fund (CSBDF) is a revolving loan fund. Loan funds help communities prosper because they inject small business capital at very low interest rates. When small businesses repay their loans, the principal and interest goes back into the fund to support additional loans. Some loan funds – including CSBDF – have been designated as community development financial institutions (CDFIs). The CDFI designation comes from the US Department of the Treasury and indicates that the organization exists primarily to promote sustainable economic growth at the neighborhood level.

But what does it mean to promote *sustainable* economic growth at the local level? CDFIs are devoted to responsible and affordable financial services that help disadvantaged people and places improve their economic mobility. In general, CDFIs must be profitable in order to be financially sustainable, but they are not profit-maximizing like traditional banks or financial corporations. Many CDFIs (including CSBDF) are 501(c)3 charities. CDFIs can be structured in many different ways. Beyond loan funds, other types of financial institutions that can obtain a CDFI designation include banks, bank holding companies, credit unions, and venture funds.[i]

Who supports loan fund CDFIs?

Like other nonprofits, loan fund CDFIs depend on public, corporate, and philanthropic support to sustain operations and programming. A notable amount of funding for CDFIs comes from financial institutions, which are incentivized to provide support through federal regulations.[ii] The generous and continued support of CDFIs by leading financial institutions, local community banks, federal agencies, state governments, local municipalities, community foundations, and individuals has helped CDFIs become beacons of neighborhood-level economic growth.

To give some context, it is important to consider how CDFI loan fund revenues from philanthropic sources compare to giving trends in the nonprofit industry as a whole. Industry reports show giving across the nonprofit spectra come primarily from individuals (70%), foundations (18%), and corporations (8%).[iii] Industry data do not include statistics on revenue from public sources, but there are obvious differences.

Revenue Source[iv]	Loan Funds	Other CDFIs
Governments	48%	55%
Private Philanthropy[v]	22%	19%
Financial Corporations	13%	12%
Corporations (Non-Finance)	6%	4%
Other Sources	11%	9%

Source: CDFI Fund Institution-Level Report, 2003 to 2017. *Note: Figures do not sum to 100% due to rounding.*

Note: Private philanthropy includes receipts from individuals, philanthropic foundations, religious institutions, and other private charities.

Over the past decade, CDFI loan funds have been heavily reliant on public sector support and, to a lesser extent, private philanthropy. While the stream of public sector revenue appears to be fairly constant, the inherent uncertainty in public policy and future regulatory changes raises questions about the long-term stability of public funding for CDFIs. For example, federal agencies have recently proposed regulation changes that could adversely impact CDFIs writ large.[vi]

The bulk of private philanthropic giving to CDFI loan funds for operating expenses comes from foundations. However, there is a great deal of variability both in terms of mean philanthropic support and the amount of philanthropic funding as a proportion of total operating support. Compared against institutional giving, other sources of private philanthropy remain a small share of CDFI funding. Between 2003 and 2017, support from individual giving ranged between 2% and 4%of total loan fund operating revenues.

How efficient are loan fund CDFIs in serving the community?

Whether they be individuals or institutions, we know it's important that donors can make a large impact with their dollars. One way of maximizing the impact of donations is by ensuring funds are used in an efficient matter. Quantifying the efficiency of loan funds (as with any non-profit) is challenging, but the data suggests they operate at very lean staffing levels given their range of activities. On average loan funds like CSBDF are able to serve 56 entrepreneurs per staff member at a cost of $1,150 per client

Our research suggests that CDFI loan funds are already being efficient with existing funds and are maximizing available revenue sources. While this speaks to the short-term sustainability of the loan fund model, the data also show a continuing need for both institutional and individual support. CSBDF strives every day to put this kind of evidence into practice, focusing on both diversifying our revenue sources while continuing our strong emphasis programmatic efficiency. Evidence suggests these strategies can promote long-term sustainability.

Measures of Staff Efficiency	CDFI Loan Funds
Direct Clients Served Per FTE	44
Indirect Clients Served Per FTE	11
Mean Compensation Per FTE	$63,223
Staff FTE Cost Per Client Served	$1,150

Source: CDFI Fund Institution-Level Report, 2003 to 2017.

Why should you support loan fund CDFIs like CSBDF?

At CSBDF, our mission is to serve and support underserved small businesses. Our goal is to lift up those entrepreneurs who are the foundation of the region's economy. One of our core values is that our programs should be backed by robust research. We don't just *believe* small businesses are the engine of economic prosperity – we provide theoretically sound scholarship to prove it. Through research like this, we want the individuals and institutions who support the work of CDFIs to know that their generosity has a large impact. The capital and technical assistance programs provided by CSBDF and other CDFIs ensures small business owners have an opportunity to flourish no matter their background or location.

[i] There are 120 cases in which the CDFI Fund's dataset does not record a institution type. In those cases the institution is classified as not being a loan fund for purposes of comparing loan funds to other CDFIs.
[ii] Federal regulations, mainly the Community Reinvestment Act, are structured to encourage large banks to support CDFIs.
[iii] Total giving percentages are based on 2017 data from Giving USA's latest annual report on philanthropy.
[iv] All data are sourced from the CDFI Fund's transaction level report for CDFIs that were awarded technical assistance and financial assistance awards from 2003 to 2017.
[v] Includes revenue from individual donor and corporate philanthropy.
[vi] For example, the Office of the Comptroller of the Currency's recently proposed changes to the Community Reinvestment Act could dramatically alter CDFI revenue sources.