Carolina Small Business

DEVELOPMENT FUND

Assessing Public, Private, and Philanthropic Support for CDFIs:

Data on Contributing Operating Revenues and Measures of Efficiency

This report is produced as part of CSBDF's research program on community and economic development. As a nonprofit loan fund, CSBDF seeks to produce scholarship which adds to broader policy dialogues on issues of relevance to small businesses.

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Introduction

Community development financial institutions (CDFIs) have a long and storied history of promoting economic growth and improving local quality of life. Scholars have consistently argued the use of social enterprises generally, and community development finance institutions specifically, represent an innovative policy solution to America's most enduring development problems.[i] But while the evidence suggests community economic development institutions are highly effective, much data concurrently shows an ongoing and persistent decline in public and private financial support for these efforts.[ii]

In such an environment, there is a strong need for CDFI staff and practitioners to consider alternative approaches to raise their capacity. There are many ways to increase organizational capacity, but we examine two primary strategies. We first examine trends in CDFI operating revenues over time and

across different types of CDFIs. Next, we propose a few basic ways to measure efficiency in the context of CDFI revenues. Overall, we believe the evidence suggests a need for revenue diversification and continued emphasis on programmatic efficiency. These strategies will likely be key for the long-term sustainability of CDFIs and similar types of organizations.

Methodology

The United States is home to countless organizations that exist to promote community economic development at the local level, and there is no singular source of data on their activities. One of the largest existing datasets come from the Department of the Treasury's CDFI Fund. The Fund releases annual data on CDFIs that receive grant awards.[iii] The data include information on operating revenue sources and full-time staffing. CDFIs can be structured in many different ways. The Fund classifies CDFIs as banks, bank holding companies, credit unions, loan funds, Native American Program institutions, or venture funds.[iv] Carolina Small Business Development Fund is a revolving loan fund. While our analyses draws on the Fund's data for all types of CDFIs, we have a particular interest in examining measures of revenue and capacity for loan funds compared to other types of CDFIs.

The dataset for this analysis is the CDFI Fund's latest institution-level report. The data include a wide swath of financial and compliance information for certified CDFI grant awardees between 2003 and 2017. Unless otherwise specified, dollar values for revenue figures are adjusted for inflation with 2017 dollars as the base year.[v] Our analysis examines contributed operating revenues (*not* earned revenue) in order to capture funding that supports CDFI operations. This excludes revenues which may be derived from debt sources. There are several limitations to keep in mind about the data. First, only institutions receiving financial and technical assistance awards are included in the dataset. While a diverse array of institutions receive these grant awards, is it not truly a dataset which represents the entire population of all certified CDFIs.[vi] Because the grant process is extremely competitive, awardees tend to disproportionately represent larger and well-resourced CDFIs. When an institution receives an award, reporting is only required for 3 years (unless it receives a new award). Although we believe the data represent the best available information on this topic, it is *not* a representative sample.

Trends in CDFI Revenue Sources

To examine how CDFI's support operations, we condensed operating revenue data from 18 sources measured by the Fund into four basic categories: (1) public sector funding, (2) philanthropy funding, (3) financial institutions, (4) funding from non-financial corporations.[vii] While public sector funding makes up the largest percent of CDFI operating revenues by far, loan fund CDFIs are slightly more diverse in funding streams. Compared to all CDFIs, loan funds are *more likely* to source revenues from non-financial corporations, and less likely to draw on public funds.[viii]

Proportion of CDFI Operating Revenue Sources by Category, 2003-2017[ix]

Revenue Source	Loan Funds	Other CDFIs	Difference	Sig.[x]
Public Sector	48%	55%	-7%	**
Private Philanthropy*	22%	19%	+3%	-
Financial Institutions	13%	12%	+1%	-
Corporations (Non-Finance)	6%	4%	+2%	**
Other Sources	11%	9%	+2%	-

Source: CDFI Fund Institution-Level Report, 2003 to 2017.
Figures adjusted for inflation by authors.
*Significant differences noted at *p < 0.05, **p < 0.01.*

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

Aggregate figures on revenue are a starting point, but it is important to consider whether sources of operating support for CDFI operations may have changed over time. The past decade has seen a series major economic events that could dramatically shift how CDFI's fund operations. For example, it's unclear how the macro-economic impacts of the Great Recession could still persist in this area. But when looking at a 10 year snapshots for loan funds between 2008 (n=131) and 2017 (n = 189), it is interesting to note the remarkable consistency. There have been some minor changes by revenue source, but the only *statistically significant difference* is an increase in funding from non-financial corporations.

Proportion of CDFI Loan Fund Operating Revenue by Source, 2008 and 2017

Revenue Source	2008	2017	Difference	Sig.
Public Sector	49%	44%	-5%	-
Private Philanthropy	24%	26%	+2%	-
Financial Institutions	13%	11%	-2%	-
Corporations (Non-Finance)	5%	9%	+4%	*
Other Sources	10%	9%	-1%	-

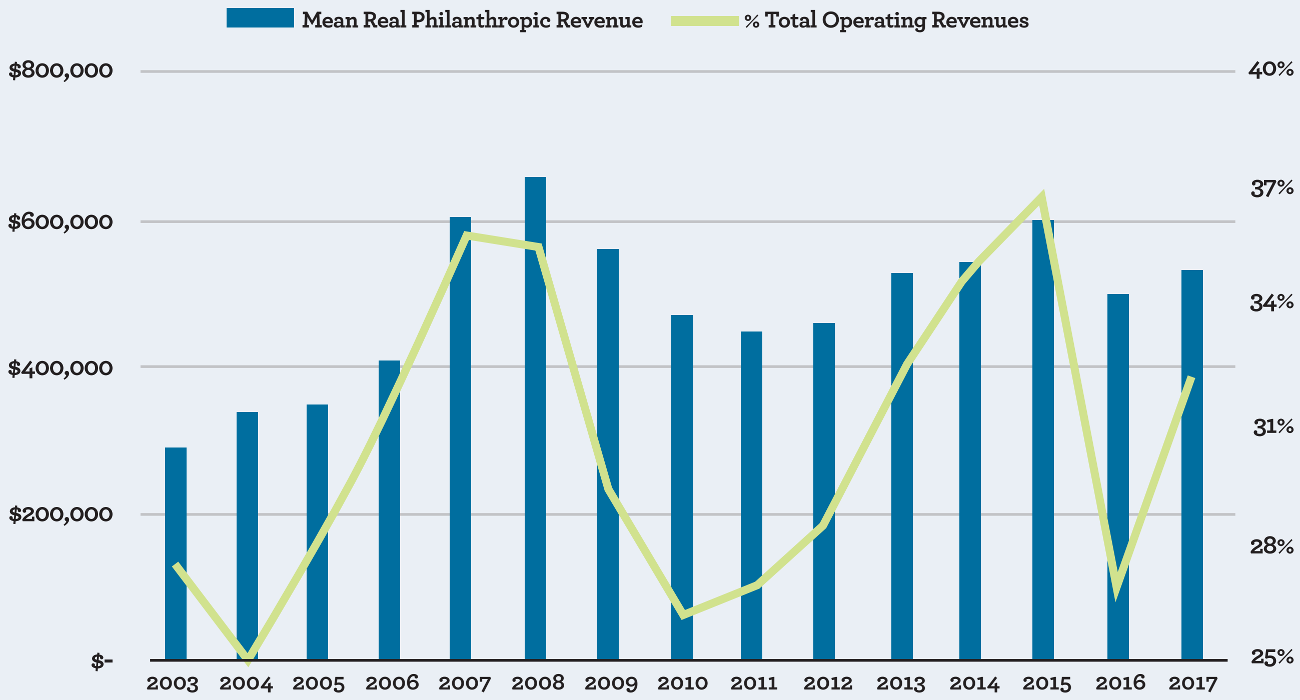
Source: CDFI Fund Institution-Level Report, 2003 to 2017.
*Significant differences noted at *p < 0.05, **p < 0.01.*

Average public sector revenues for CDFI loan funds increased in inflation-adjusted terms from $415,513 in 2008 to $663,976 in 2017. However, this increase is not statistically significant, and as a proportion of overall operating revenues public funding actually declined during this time period. Nearly half of CDFI loan fund revenues (49%) were from the public sector in 2008 versus 44% in 2017. This is consistent with research that has highlighted the long-term decline of public support for community economic development. Extant literature suggests the largest systemic drops in community development support work came from state funding in the 1990s and early 2000s, but our data suggests this trend may be continuing.[xi] On a percentage basis replacement of public funding has mostly come from non-financial corporations, which were almost 10% of total operating revenues in 2017.

A Closer Look at Philanthropic Revenues

The aggregated data mask some important trends in CDFI operating revenues, particularly in the area of private giving. 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 proportional of total operating revenues. Average support from philanthropy peaked in 2008 at $658,587 but was $531,858 in 2017. The percent of total revenues from private philanthropy is highly volatile, ranging from a low of 25% in 2004 to a high of 37% in 2014.

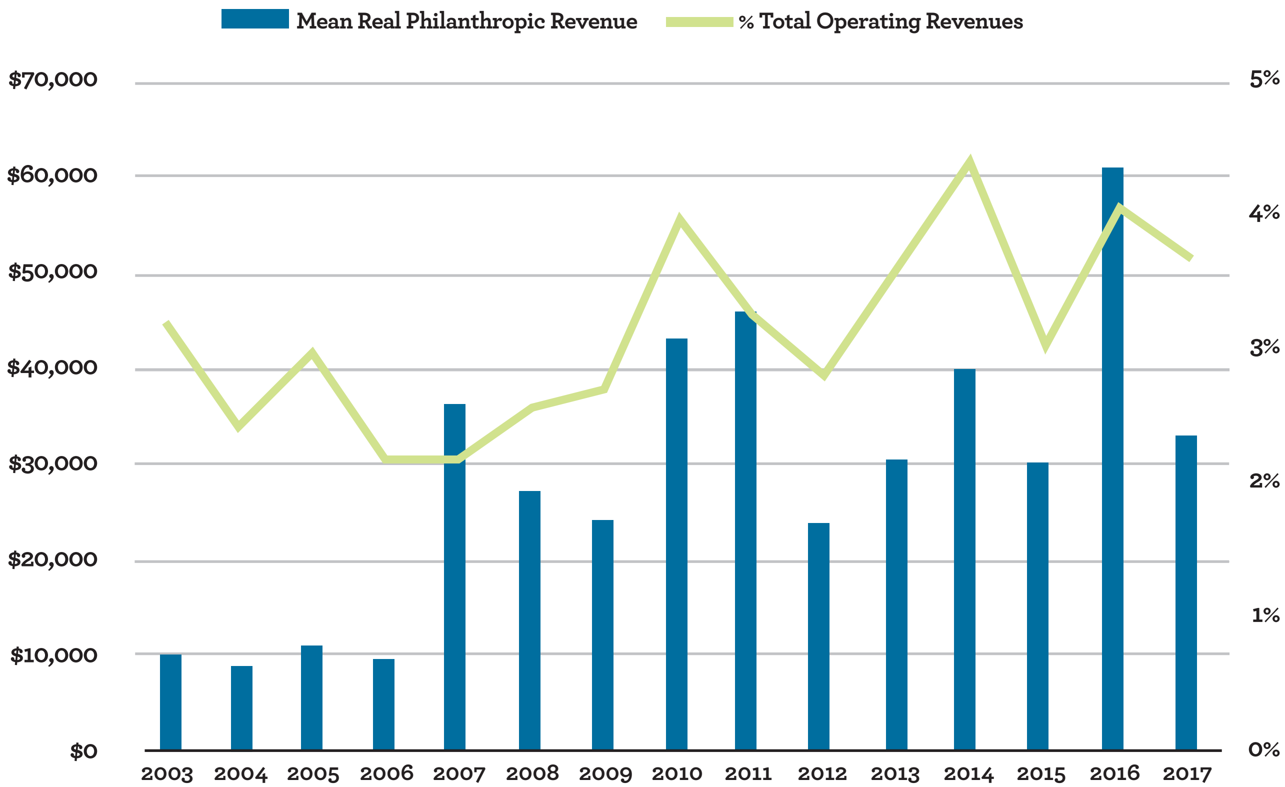
CDFI Loan Fund Revenues from Philanthropic Sources, 2003-2017



Source: CDFI Fund Institution-Level Report, 2003 to 2017. Figures adjusted for inflation by authors.

The data also suggest that *institutional* philanthropy - which is the largest subcategory of private giving support for loan fund CDFIs - may not be a good long-term source of sustainability. But, compared against institutional giving, other sources of private philanthropy remain a small share of CDFI funding. Revenues from individual giving have ranged between 2% and 4% of total loan fund operating revenues since 2003. The average inflation-adjusted amount of gross individual donations received by loan funds ranges from a low of $8,951 in 2014 to a high of $61,200 in 2016. Historical volatility from this source is likely due to the fact that it remains a small portion of total operational funding.

CDFI Loan Fund Revenues from Private Philanthropy, 2003-2017



Source: CDFI Fund Institution-Level Report, 2003 to 2017. Figures adjusted for inflation by authors.

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%). [xii] Industry data do not include statistics on revenue from public sources, but there are obvious differences in CDFI loan fund support from philanthropic sources and nonprofit revenue sources writ large. While most nonprofits use individual donors as their primary source of support, CDFI loan funds primary utilize public sources.

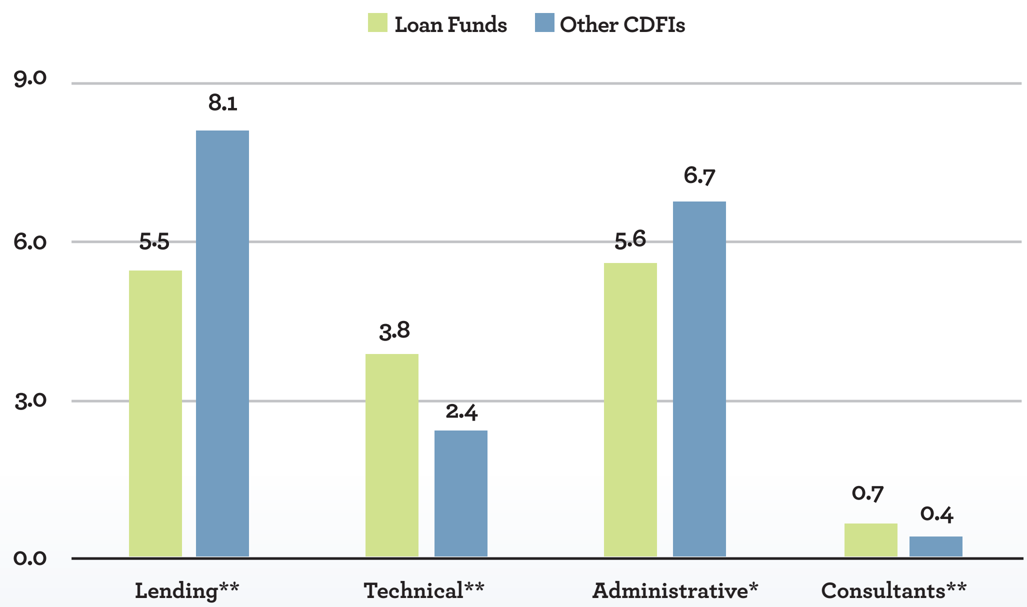
At an organizational level, CDFIs face ongoing capacity constraints that require new ways of thinking about sustainability. We think individual giving may represent an untapped source of revenue for operational expenses in the CDFI loan fund community. When structured appropriately, individual giving programs can create sustainable and unrestricted revenue streams. Revenue from individuals, when incentivized through long-term giving programs, could be more reliable than large one-time or even multi-year support received from foundation grants.

Trends in Staff Capacity and Cost Efficiency

Beyond diversifying revenue streams, an alternative path to increasing CDFI sustainability is to promote cost-efficient use of existing funds. Quantifying and operationalizing the operational efficiency of institutions is difficult in any context – but it is especially challenging with CDFIs due to limited data availability. One lens through which operational capacity can be viewed is staff size – theoretically, institutions seeking to be efficient should aim to do more with the same numbers of staff.

CDFI loan funds have substantially lower levels of full-time staff across categories of employees involved in lending activities and administrative/management functions. Loan funds do tend to employ more people in technical assistance roles, consistent with the fact that these entities often offer a wide array of non-lending assistance through entrepreneurship and small business programming. Overall CDFI loan funds employ about 15.6 FTEs, compared to 17.6 FTEs for other types of CDFIs.[xiii] For all categories of employees tested, the differences between average FTEs across loan funds and other CDFIs are statistically significant. In general this data suggest that CDFI loan funds operate with notably less staffing than other types of CDFIs.

FTE Capacity by CDFI Type, 2003-2017



Source: CDFI Fund Institution-Level Report, 2003 to 2017. *Significant differences noted at *p < 0.05, **p < 0.01.*

Based on available data, determining CDFI cost efficiency is difficult. For loan funds, each staff member served about 55 direct and indirect clients on average at a cost of $1,150 per client. Other types of CDFIs serve about 62 direct and indirect clients per staff member at a cost of $1,126 per client. Loan fund staff on average are compensated less than other CDFIs, but other types of CDFIs are able to serve more clients per staff member. Without a basis for comparison, there are insufficient data to determine whether a cost of $1,126 to $1,150 per client served represents a high or low level of efficiency. [xiv]

Measures of Per Capita Staff Efficiency, 2003-2017[xv]

Measure	Loan Funds	Other CDFIs	Difference
Direct Clients Served Per FTE	44	58	-14**
Indirect Clients Served Per FTE	11	3	+8**
Mean Compensation Per FTE	$63,223	$69,821	-$6,598
Staff FTE Cost Per Client Served	$1,150	$1,126	+$24

Source: CDFI Fund Institution-Level Report, 2003 to 2017.
Figures adjusted for inflation by authors.
*Significant differences noted at *p < 0.05, **p < 0.01.*

Data on average FTE staff changes over time show that loan fund staff levels have increased slightly in the past decade. However, with the exception of consultants (which declined slightly), none of the reported changes by category is statistically significant. This supports the idea that most loan funds operate with lean staffing, as growth in staff has been immaterial over time. Total CDFI loan fund staff have only increased 1.8 FTEs on average, from 16.1 total staff in 2008 to 18.0 in 2017.

CDFI Loan Fund FTE Capacity, 2008 and 2017

Staff Category	2008 FTEs	2007 FTEs	Difference	Sig.
Lending	5.2	7.0	+1.8	-
Technical	4.6	4.2	-0.4	-
Administrative	5.5	6.2	+0.7	-
Consultants	0.8	0.6	-0.2	**

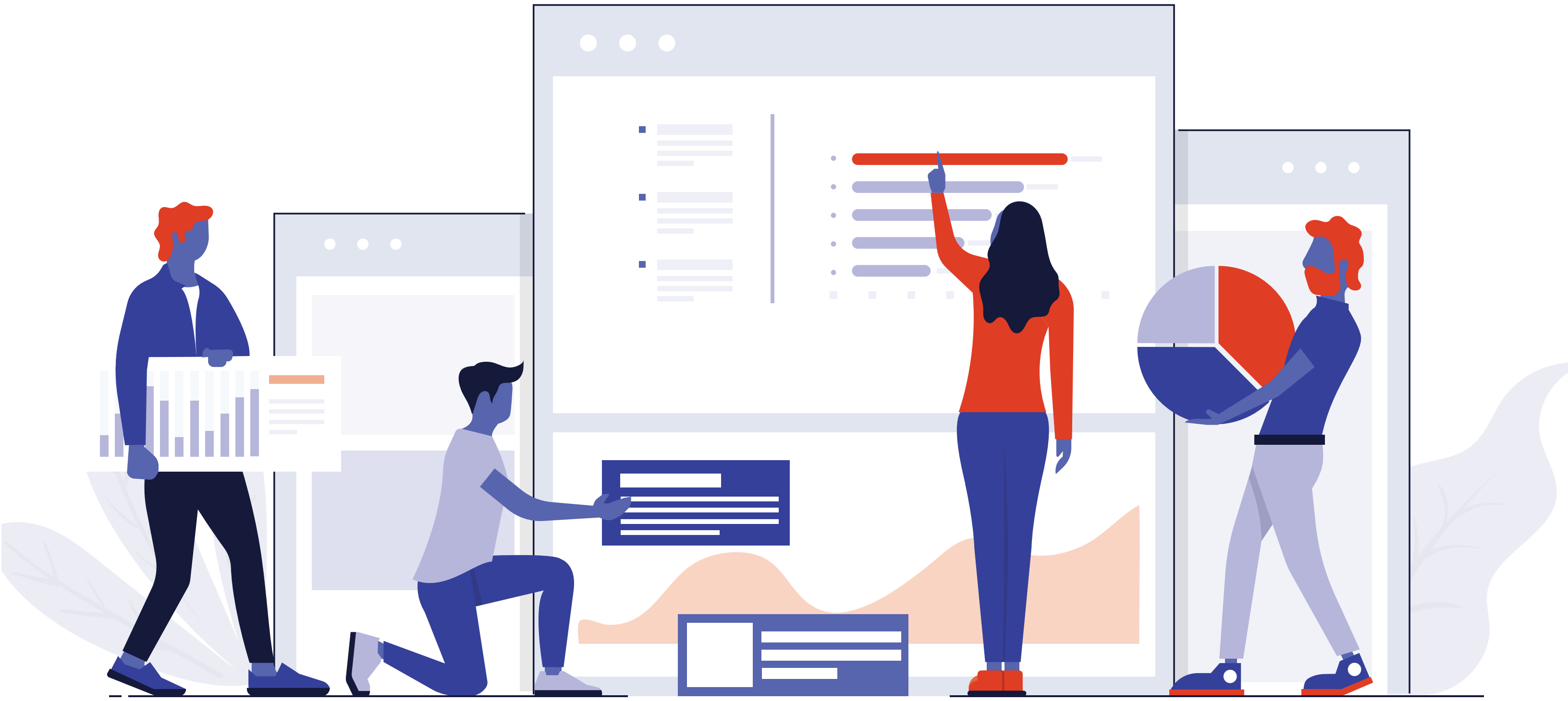
Source: CDFI Fund Institution-Level Report, 2003 to 2017. *Significant differences noted at *p < 0.05, **p < 0.01.*

Conclusions

Over the past decade, CDFIs have been heavily reliant on public sector support and, to a lesser extent, private philanthropy. While these revenue streams have remained fairly constant, their long-term stability requires that existing policy and regulatory regimes remain unchanged. The inherent uncertainty that is omnipresent in the policy process makes this unlikely.[xvi] For example, federal agencies have recently made proposals to change regulations that could directly impact CDFI revenue streams. [xvii]

Given the policy landscape, we believe there is a need to leverage individual giving to diversify CDFI revenues. A large array of scholarship has argued that diversification of revenue for nonprofits brings greater flexibility, autonomy, and community embeddedness.[xviii] However, it is important to note that not all the literature agrees with this consensus. Some have argued revenue diversification may lead to “crowd out” effects, increased administrative costs, and risks associated with increasing the complexity of a nonprofit’s portfolio.[xix] But in aggregate we believe the research shows the costs outweigh the benefits.[xx]

The importance of diversifying revenues is important because the data suggest most CDFI loan funds are already being efficient with existing funds. Seeking additional increases in program efficiency is important, but there are inherent limitations to solely relying on this approach. At an aggregate level, the data suggest CDFIs are mostly maximizing available revenue sources. Despite having less staffing than other types of institutions, loan funds are able to serve a large number of clients. Loan fund staff size has essentially remained unchanged since the Great Recession. But while such indicators bode well for the CDFI model, the data also indicate a need for institutional innovation.



Guidance for Practitioners

From a practical standpoint, leveraging individual donors to diversify CDFI loan fund revenues is not an easy task. Given how little current activity is supported through private individuals, it is unreasonable to expect any sort of shift in short-term. However, our research suggests CDFIs should consider this approach in their development strategy. To aid practitioners, we recommend keeping the following things in mind when crafting strategies to engage individual donors:

Individual giving campaigns for CDFIs require a different kind of messaging.

Being successful in attracting individual donors requires consistent marketing with a fundamental message and clear branding. The first step for CDFI loan funds is to identify the audience of prospective individual donors. This can be a challenge because the targeted audience must have both affinity *and* capacity to support the organization's mission. The primary missions of most CDFIs are hard to define in a succinct manner. For example, the broad mission of most loan funds is to support underserved small business owners. But this mission could appeal to many different types of individuals and interests. Market research into the potential donor audience - including testing strategies for how to communicate the CDFI's mission - is key for success.

The outcomes of CDFIs are difficult to translate to individual donor audiences.

The economic development work of CDFIs is hard to quantify for individual donor audiences. While potential donors in loan funds are often interested in the inspiring success stories produced by clients, communicating a "return on investment" in dollar terms is difficult. In particular, the outcomes of loan funds are primarily related to creating entrepreneurial networks and fostering financial stability, concepts which are hard to translate to lay audiences. This is likely one reason that CDFIs tend to spend most of their development efforts on grant proposals to large foundations and financial institutions. These audiences are theoretically more likely to understand the hard-to-define impacts of CDFI programs.

Competition for donations is high, making it hard to attract individual supporters.

Research from CDFI industry partners like FUND Consulting has noted that CDFIs are a “hard sell” in social philanthropy.[xxi] This is certainly supported by the data. Reported CDFI loan fund gross revenues from individual donors in 2017 was $7M, a mere fraction of the nearly $30B in donations given by individuals during the same time period. We think being a competitive option for donors requires engagement with the CDFI’s existing stakeholders – including board members. FUND Consulting survey data show that only 30% of CDFIs have boards actively engaged in fundraising. Notably, nearly half of respondents said that even engaged boards were not successful in raising funds for the organization. Understandably, CDFI board members are often concerned about how their role in fundraising might impact their professional relationships. But in order to be truly successful in this area, we think staff development efforts must be bolstered with meaningful assistance from board members.

CDFI staff face resource constraints which may impact the design of individual giving strategies.

The expression “it takes money to make money” is every bit as true when it comes to nonprofit fundraising, especially when establishing new programs and initiatives. Data show most CDFIs have limited organizational staff capacity. Robust individual donor programs take time and resources to create and sustain. Staff capacity for such efforts is restrained when they are already tasked with development initiatives involving more traditional revenue sources (like writing grants for foundational philanthropy). Beyond direct development staff time, individual giving programs must be backed by data on program outputs that will attract and motivate donors.

Despite the challenges, we encourage all CDFIs – regardless of capacity – to consider whether individual donors can be a part of their development strategy. CDFIs can offer a compelling message to individual donors around the efficiency and cost effectiveness of their work to improve local economic outcomes. Through concerted efforts to identify potential donors and strategically target messaging campaigns, individual donors can play a role in the organizational sustainability of community development institutions.

References and Sources

[i] Wilson, T. (2012). Supporting Social Enterprises to Support Vulnerable Consumers: The Example of Community Development Finance Institutions and Financial Exclusion. *Journal of Consumer Policy*, 35(2), 197-213.
[ii] Bratt, R. G., & Rohe, W. M. (2007). *Challenges and Dilemmas Facing Community Development Corporations in the United States*. *Community Development Journal*, 42, 63–78.
[iii] Specifically, the data include all institutions receiving assistance awards which are included in the 2019 CDFI Program and NACA Program data release.
[iv] There are 120 cases in which the CDFI Fund's dataset does not record an institution type. In those cases the institution is classified as not being a loan fund for purposes of comparing loan funds to other CDFIs.
[v] Inflation adjustments have been calculated using the yearly average of the Chained Consumer Price Index for Urban Consumers (CPI-U), as produced by the Bureau of Labor Statistics.
[vi] According to the CDFI Fund's annual report, as of September 2018 there were 1,112 certified CDFIs across the United States. Around 264 organizations received awards during the last grant cycle. While the number of awardees and total certified CDFIs changes each year, this indicates that about 1 in 4 CDFIs are typically included in the datasets published by the Fund.
[vii] In our analyses, *public sector funding* includes the following categories: the CDFI Fund, federal government, state/local government, and government-sponsored entities. *Private philanthropic* revenues includes receipts from individuals, philanthropic foundations, religious institutions, and other philanthropic entities. *Financial institution* revenues are those from banks, CDFI lending intermediaries, insurance companies, investment banks, pension funds, and venture funds. *Non-Financial corporation* funding counts revenues from real estate developers, utility companies, and other corporate entities. Finally, other revenues includes any source not collapsed into the previously mentioned categories.
[viii] Contrary to our expectations, loan funds do not receive a larger share of revenues from financial institutions compared to other types of CDFIs. We had hypothesized that the scope of programmatic work conducted by loan funds should incentivize higher levels of support from traditional lending institutions. In particular, the tendency of loan funds to target underserved populations means they should receive disproportionately more support from large banks due to the Community Reinvestment Act. See Getter, D. (2019). *The Effectiveness of the Community Reinvestment Act (CRS Report No. R43661).* Retrieved from Congressional Research Service.
[ix] Percentages may not sum to 100% due to rounding.
[x] Throughout this analysis, statistical significance flags for differences in mean values are based on an independent samples t-test of percentages or values for the indicated time period.
[xi] Berner, M., Brown-Graham, A., McCall, J., Morgan, J., Mulligan, T., Floyd, N., Hatton, C., & A. Mahood. (2019, May). *Building Bonds and Bridges (and Leveraging Links): A Place-Based Mobility Strategy Based on Social Capital Creation*. Paper presented at the biannual Federal Reserve Community Development Research Conference, Washington, DC.
[xii] Total giving percentages are based on 2017 data from Giving USA's latest annual report on philanthropy.
[xiii] This total excludes other financial staff, because due to the CDFI Fund's typology of employees this category is 0 for loan funds.
[xiv] Additionally, this data must be interpreted with caution for several reasons. The ability of CDFIs to accurately report things like indirect clients served is difficult. The values reported above have large standard deviations, and thus the mean differences on compensation and cost efficiency measures are not statistically significant.
[xv] For clients served per staff member, total full-time staff includes consultants. Compensation per staff member excludes consultants because the salaries and benefits variable does not include consultant compensation.
[xvi] Baumgartner, F.R., Jones, B.D. (2009). *Agendas and Instability in American Politics*. 2nd Ed. Chicago, IL: University of Chicago Press.
[xvii] 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.
[xviii] Hung, C., & Hager, M. (2019). The Impact of Revenue Diversification on Nonprofit Financial Health: A Meta-Analysis. *Nonprofit and Voluntary Sector Quarterly*, 48(1), 5-27.
[xix] Chikoto, G.L., & Neely, D.G. (2014). Building Nonprofit Financial Capacity: The Impact of Revenue Concentration and Overhead Costs. *Nonprofit and Voluntary Sector Quarterly*, 43(3), 570-588.
[xx] Carroll, D.A. & Stater, K.J. (2009). Revenue Diversification in Nonprofit Organizations: Does it Lead to Financial Stability? *Journal of Public Administration Research and Theory*, 19(4), 947-966.
[xxi] FUND Consulting. (2015, November). *CDFI Boards and Fundraising*. Panel at the annual meeting of the Opportunity Finance Network, Detroit, MI.