

**Understanding Microfinance
National Community Development Lending School
March 25 – 28, 2012
Seattle, WA**

INTRODUCTION

Small business financing continues to gain traction through alternative financing methods in the U.S. One such method is microfinancing. Microfinance is defined as providing capital to individuals who are unable to access capital through a traditional bank loan. Microloans provide financing opportunities for new and emerging businesses throughout the U.S. This interactive session will provide tools for establishing and operating successful microfinance programs, and provide examples of effective and productive partnerships with financial institutions.

OBJECTIVES

This course will provide participants with the following:

- Insight and understanding of the microfinance field
- An understanding of the utilization of the “C’s” of Credit in a traditional lending institute versus a microcredit organization
- Tools for managing a successful microfinance program
- Strategies for managing portfolios
- Mechanisms for establishing and maintaining partnerships with financial institutions

INSTRUCTORS

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Understanding Microfinance

March 27, 28, 2012

8:30-12:00

AGENDA

- | | |
|--------------------|---|
| 8:30-9:15 | Welcome, Introductions, Participant Objectives |
| 9:15-10:00 | Overview of Microfinance and ACCION Texas Inc.
Janie Barrera |
| 10:00-10:15 | Microloan Collections and Growth at VEDC
Roberto Barragan |
| 10:15-10:30 | Break |
| 10:30-11:00 | Microloan Collections and Growth Continued |
| 11:00-11:45 | A Successful Microloan Partnership at Capital One Bank
Laurie Vignaud |
| 11:45-12:00 | Q &A |

GLOSSARY OF TERMS AND DEFINITIONS

Collateral: Assets that will be utilized for securing a business loan. Authorized collateral policies are set by individual lending organizations and vary.

Capacity: Cash flow of an applicant's household and business to determine ability to service debt. Depending on the applicant's business structure, length in business and loan amount capacity is measured by analyzing debt to income ratios. Should an applicant meet the lender's capacity requirement with the new debt included a loan may come to fruition.

Debt to Income Ratio: Is measured by examining all long and short term debt service and all household revenue and/or business revenue. Typically if the DTI is at or over 50% an individual or organization does not have the capacity for a loan.

Credit Score: The number generated by the credit bureaus which is a numerical representation of a person's credit profile, ranging from 450 on the low side to 900 being the highest score possible. The score examines long term debt, collections, inquiries, payment history, open accounts, revolving accounts, and more. It also highlights an individual's bank score along with bankruptcy indicator.

Character: An assessment of applicant based on credit score, capacity, engagement, past experience, and engagement during application process. Character is assessed by loan officer.

Conditions: The applicant's overall financial condition along with industry condition and market conditions.

Community Development Financial Institutions: CDFIs are specialized, community-based financial institutions that serve low-income people or work in economically distressed communities, often working in market niches that may be underserved by traditional financial institutions.

There are four main types of CDFIs, and each provides a different mix of products geared to reach specific customers:

- Community development banks are for-profit corporations that provide capital to rebuild economically distressed communities through targeted lending and investment;
- Community development credit unions are non-profit cooperatives owned by members that promote ownership of assets and savings and provide affordable credit and retail financial services to low-income people;
- Community development loan funds (usually non-profits) provide financing and development services to businesses, organizations and individuals in low-income urban and rural areas and can be further categorized based on the type of client served: micro-enterprise, small business, housing, and community service organizations; and
- Community development venture capital funds include both for-profit and non-profit organizations that provide equity and debt-with-equity features for businesses in distressed communities.

Community Development Financial Institutions Fund: The CDFI Fund was created for the purpose of promoting economic and community development through investment in and assistance to Community Development Financial Institutions (CDFIs). The Fund is a department of the U.S. Treasury.

EQ2s: Equity Equivalent Loans or Investments bearing longer terms and lower rates than conventional loans from banks to nonprofits.

JVs: Joint Ventures between a community organization and a CDFI for the purpose of the development and later management of a loan fund.

Microloan: A loan ranging from \$500 to \$50,000 at ACCION Texas Inc. with a length of no more than five years.

Microlender: An organization that provides microloans to entrepreneurs who are unable to access capital through a traditional banking/lending organization.

Microenterprise: A business with 5 employees or less.

MOUs: Memorandum of Understanding between a community organization and a CDFI for the purpose of the former originating loans for the latter.


Multiple Product Lender: A provider of microloans and small business loans.

Single Product Lender: A provider of one loan product.

Technical Assistance: Business support in the form of consultations, seminars, financial education, business and marketing planning and overall business management support.

Tickler System: System within a loan portfolio management software that reminds the operator when financial statements, tax returns and other loan requirements must be collected from the borrower.

UCCs: Liens filed under the Uniform Commercial Code that must be rerecorded every five years.




ACCION
TEXAS INC.
Leading. Supporting. Inspiring.

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ENTREPRENEURSHIP

“Social entrepreneurs are not content just to give a fish or teach how to fish. They will not rest until they have revolutionized the fishing industry.”

(Bill Drayton, CEO, Chair and Founder of Ashoka)




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ACCION TEXAS INC.

To achieve our mission we provide:

- Loans**
 - Microloans ranging from \$500 to \$50,000
 - Mid size to large loans ranging from \$50,000 to \$250,000 with local funds and as a designated Community Advantage 7a lender
 - Macro loans through the SBA 504 program in Texas
- Business Support**
Business consultations and business seminars
- Innovation**
Microlending Management System TM (MMS)



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ACCION TEXAS INC.



- ACCION Texas Inc. (ATI) lends to over 1,000 small businesses every year
- We make loans to a wide spectrum of entrepreneurs, from those with no credit to those with excellent credit but who still are turned away by banks

- Average loan is just over \$16,000
- Active portfolio over \$25 million with over 2,200 borrowers.
- Total number of clients served: 8,140

CDFIs

- Community Development Financial Institution (CDFI) Fund.
- Created by the U.S. Department of Treasury in 1994.
- The CDFI Fund was established by the Riegle Community Development and Regulatory Improvement Act of 1994, as a bipartisan initiative.

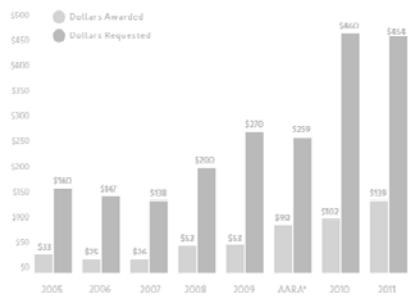
CDFIs

- CDFI certification is a designation conferred by the CDFI Fund. An organization must be a legal entity and meet the following six statutory and regulatory criteria:
- Have a primary mission of promoting community development;
- serve principally an investment area or targeted population;
- be an insured depository institution, or make loans or development investments as its predominant business activity;
- provide development services (such as technical assistance or counseling) in conjunction with its financing activity;
- maintain accountability to its target market; and
- be a non-governmental entity and not be controlled by any governmental entities.

CDFIs

- Nationally there are over 900 CDFIs
- In Texas there are 40 CDFIs
- In the Houston area, there are several CDFIs including ATI. Four are local or "homegrown," two operate on a national basis, and three operate statewide
- In addition to its CDFI designation, ATI is an SBA Certified Development Corporation, 7A Community Advantage Lender, and a WBC Host.

CDFI FINANCIAL ASSISTANCE
(AMOUNTS REQUESTED & AWARDED (\$ MILLIONS))



THE LANDSCAPE: 18 YEARS AGO

- Access to capital for minority, low income, recent immigrant, and women was a challenge.
- Community Economic Development was forming.
- ACCION International decided to tackle poverty in the U.S. with ACCION organizations in designated states including Texas. ACCION Texas was established in 1994.
- 1996, the Community Development Financial Institutions (CDFI) Fund, part of the Treasury Department, was created; by 1998, there were 300 designated Community Development Financial Institutions in the U.S.
- The CDFI Fund awarded \$167.3 million in 2011, and there are now a total of 963 CDFIs in the U.S.

THE LANDSCAPE: TODAY

- Access to capital for minority, low income, recent immigrants, and women is a challenge.
- The definition of “unbankable” extends beyond low-and moderate-income (LMI) and diversity. There is a wider pool of individuals entering ACCION for a microlending solution.
- 18 years later, ATI has become a leader in the microfinance industry. We are located in eight states, and as of 2012 hold the largest portfolio of microloans in the nation.

HOW MICROFINANCE WORKS IN THE U.S.

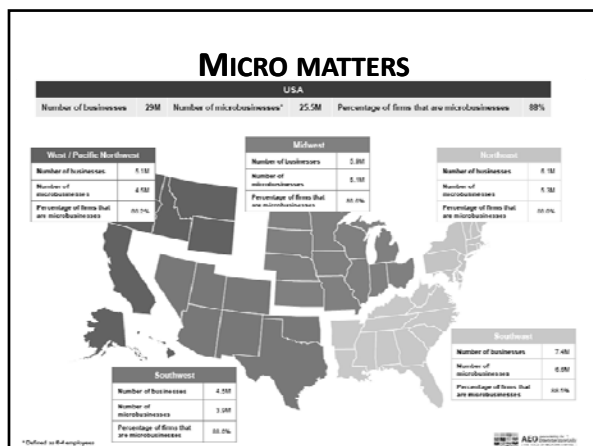
Loan features including size, collateral requirements, and repayment terms typically are more flexible than those of standard bank loans and are tailored to the needs of low- and moderate-income entrepreneurs.



Maria Cortes de la Torre
Maria Luisa Sport
Dallas, Texas

MICROLOAN

- Defined as a very small business loan to build assets and improve credit of an entrepreneur.
- Relies heavily on personal credit.
- In U.S. under U.S. Small Business Administration (SBA) a microloan is capped at \$50,000 and cannot exceed six years of payment.
- At ACCION a microloan ranges from \$500 to \$50,000 with the same time frame (company average is no more than 50 months).
- Our average microloan size ranges per market but as a system it is \$16,000.



THE ECONOMIC CRISIS

- Nearly 30 million people in the U.S. have limited or no access to checking or savings accounts, or use non-bank financial services.
- An estimated 7.7 percent of U.S. households, approximately 9 million, are unbanked.
- 18 percent of U.S. households, roughly 21 million, are underbanked.
- Source: <http://www.fdic.gov/householdsurvey/>


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THE SOLUTION


- Organizations like ACCION Texas Inc. that provide microlending.
- Why?
 - To assist individuals in improving their credit to grow their wealth.
 - To serve as a stop gap in business financing.
 - To end poverty, rebuild communities, and create jobs.

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ACCION TEXAS MILESTONES



1994
ATI founded & provided microloans and frontline business support.





2000
Started with SBA Microloan & TA funding



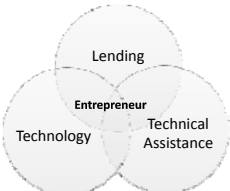
Today
Largest Microlender in the US.
Host of WBC, SBA 504, SBA 7a, SBA microloan programs and other private and public funding programs


Over 8,000 loans provided with over \$116M deployed in 18 years.





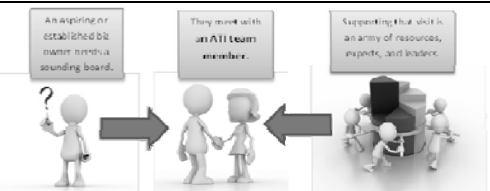
HOW DOES BUSINESS SUPPORT FIT WITHIN ACCION TEXAS INC.






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OUR DIFFERENTIATING FACTOR



Full one stop shop for aspiring or established business owners. * Support individuals build and establish their credit * Serve as a stop gap * Efficient application process * Creative with collateral * We utilize an internally designed risk formula * No minimum credit score requirement * Average loan size is \$12,000-\$15,000 * Interest Rates range from 10.5% to 18%



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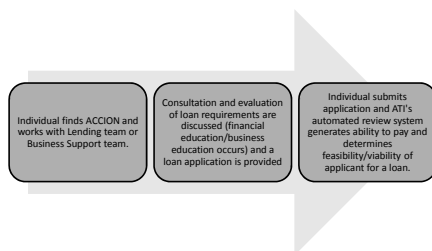
TRAITS OF BUSINESS FINANCING

Analysis	Traditional Bank	ACCION Texas Inc.
Credit Score (debt and credit management)	650- higher score opens doors for financing	Views 650 as a good credit score and works with individuals who have lower scores
Capacity (Cash flow and financials)	Varies, DTI 40-50% with loan. formal financials	Less than 50% DTI with ATI loan informal and formal financials
Collateral (assets)	Business assets, land clear and free.	Business assets, personal assets, assets older than 10 years, jewelry, land that is not homesteaded
Character	Business plans, expertise, engagement, references	Business plans, expertise, engagement, references
Conditions	Include assessment of individual/business, and market place.	Include assessment of individual.

LENDING ACTIVITY

Type of Activity	Traditional Bank	ACCION Texas Inc.
Microloan	Starts with higher \$ loans from banks; and use of small business credit cards continues to increase	Secured loan starting at \$500 up to \$50,000
Step Lending	Not provided, negotiated method is provided though.	Negotiate method of accessing smaller amounts of funds to meet business needs and not tax business owner. With a good track record, may re-apply in six months.
Business Support	Seminars are provided.	Business consultations and seminars are provided pre, during, and after the application period.

OUR METHOD STEP 1



OUR METHOD STEP 2

After ATT's automated review, a person is denied, approved, or under consideration. If approved or under consideration, the due diligence begins and a document list for verification is issued.

The required documents are verified by an underwriting team and a final decision is made by the underwriter.

Decision along with loan amount and payments are discussed with client if approved. If denied, the client is provided a reason and may reapply in six months. The client is referred to consultation.

OUR METHOD: BUSINESS SUPPORT

Individual considering a loan, is starting up or in business, and needs a sounding board

Applies or does not apply for a loan

Needs support in writing a business plan or in building financials

Business Support model allows for a business owner to have support pre- and during the loan application process and after funding.

INNOVATION

- **MMS** – an innovative loan origination platform that speeds up the lending process
- Applications receive an **automated preliminary review**; a key feature is a statistical analysis of 16 years of borrower repayment data
- Microsoft CRM software tailored to microfinance and is **paperless**
- Since 2008, ACCION Texas Inc. has sold MMS to other microlenders; 15 U.S. organizations now use the platform to increase their microlending capacity
- High tech *and* high touch: We continue to work extensively with each borrower to understand their story



SOLID PARTNERSHIPS



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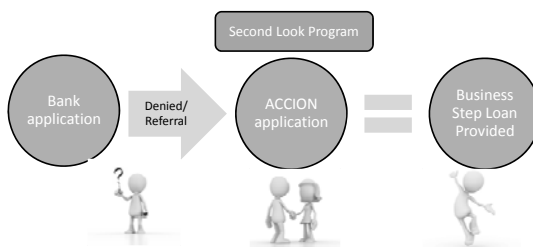
FINANCIAL PARTNERSHIPS

- Utilization of CRA and beyond.
- Local and Regional Bank Partners
- National Bank Partners



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PROVIDING A SECOND LOOK



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FINANCE PARTNERING

Tandem loan


Bank Loan


+


ACCION Loan

=

Financing to meet the consumer financing needs!








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BAKE, BROIL & BREW TANDEM LOAN




Home based cupcake business that recognized limitations due to code compliance impact on aspiring chefs and bakers.

Utilized ACCION Services:
Business Center for business planning and strategic planning and pricing.


Accessed mid-size loan with a traditional commercial loan to open a commercial leasing kitchen.

Job creation: Two employees, one part time and one full time .




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LOS MECATES (SECOND LOOK PROGRAM)



Lending. Supporting. Inspiring.



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ACCION TEXAS INC.

PHILOSOPHY

Credit, a word that comes from the Latin verb "to believe," is what ACCION Texas is all about. Giving people credit for who they are and seeing collateral in a person's character. Believing that people can succeed, and giving them the tools they need to do so.



Moises Reyna
Owner, Tienda La Reyna



Valley Economic Development Center, Inc.

**National Community Development Lending School
Understanding Microfinance**

Roberto Barragan, President
Valley Economic Development Center, Inc.
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Micro Finance

History

- **Year Established:** 1998
- **Production**
 - Total Loans Funded as of 12/31/2011: 1,070
 - Total \$\$ Funded as of 12/31/2011 : \$13,012,480
 - Average Loan Amount: \$12,024
 - % of Minority Business 44%
 - % of Women Business 42%
 - % Start-up in : 40%

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Micro Finance

- **Funding**
 - Microloan Funding as of 12/31/2011: \$5,300,000
- **Collections**
 - Total # of Loans Written-Off to Date: 138
 - % of Write-Offs: 13%
 - Total of \$\$ Written-Off to Date: \$ 1,186,297
 - % of \$\$ Written-Off : 9.1%

3



Micro Finance

Impact

- **Hybrid program of lending**
 - Achieve volume of microlending
 - Credit, collateral, cashflow plus character
 - 90% payback
- **Participation with other funding sources**
 - Maximum funding, minimum risk

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Micro Finance

Issues

- **High cost of operating a micro finance program**
- **How to go to scale**
- **Achieving sustainability**
- **Controlling defaults**

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Loan Servicing

- **Portfolio Management**
 - Invoicing
 - Payment collection and posting
 - Tickler system
 - Contact management
 - Loan software

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Loan Servicing

- **Annual Portfolio Review**
 - Annual review to determine current status of borrower
 - Annual submission of tax returns
 - Annual site visits
 - Annual review of credit reports, UCCs expirations
 - Update cashflow vs. projections

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Loan Servicing

- **Constant Monitoring of Delinquencies and Defaults**
 - Calls or visits once payment is 5 days past due
 - Late Letters at 45 and 60 days past due
 - Default letter and call at 90 days
 - Acceleration at 105 days
- **Target of <15% delinquency; <5% net charge offs**

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Collections

- **Collateral analysis**
 - **Vehicles and equipment**
 - Market value less repossession and sale costs
 - **Trust Deeds**
 - Market value less senior liens and sale costs
 - Consider arrangements with senior lenders to avoid foreclosure
- **Recommended action**

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Collections

- **Liquidation of collateral at 120 days**
 - Repossession of vehicles or equipment
 - Foreclosure of real property
 - Legal action i.e. judgments and small claims
 - Collection agency

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Collections Case Study

- **ABC Company received a \$10K Microloan**
- **ABC Company secured the loan with a vehicle valued at \$10K and a UCC filing valued at \$2K.**
- **Servicing**
 - Once the payment was 5 days past due the borrower was called.
 - A Late letter was mailed out when the loan became 45 then 60 days past due.
 - A Default letter was mailed out, certified mail, and the borrower was given 15 days to cure.
 - An Acceleration letter was mailed out, certified mail, and the borrower was given 15 days to payoff.

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Collections Case Study

- **When the Acceleration letter for ABC Company expired there was a current loan balance of \$8K**
- **Collateral Analysis**
 - Current value of vehicle was \$5,500
 - Less: Cost to Obtain vehicle \$500
 - Current value of UCC was \$2,000
 - Less: Cost to obtain equipment \$150

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Collections Case Study (cont.)

Recommended Action

- **Repossessed Vehicle (Best Asset)**
 - Sold Vehicle for \$5,000
 - Applied to Loan Balance with a \$3,000 deficit.
- **Liquidated Equipment**
 - Sold Equipment for \$1,850
 - Applied to Loan Balance with a \$1,150 deficit
- **Deficiency: \$1,150**
- **Small Claims Court**
 - Obtained a Judgment
 - Judgment impacts all future credit transactions

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Recommended Action (cont)

- **Borrower attempts to refinance to a lower rate**
 - Judgment prohibited action without VEDC's cooperation
 - VEDC worked out a payment plan with borrower to pay all outstanding principal owed

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Marketing

- **Growing the Business**
 - Website
 - www.vedc.org
 - www.microloan.org
 - www.wheresthemoneyinLA.com

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Marketing

- **Events**
 - “Where’s the Money”? Access to Capital Expo
 - Grand Openings
 - Ribbon Cutting Ceremonies
 - Check Presentations

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Marketing

- **Partnerships:** U.S. SBA, Banks, Community Organizations
 - Referrals
 - References
 - Resources
- **Partnerships:** Bank denials
 - Turndowns
 - Concept: provide banks an alternative to saying “No”

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Technical Assistance

- **All approved borrowers are required to participate in an Entrepreneurial Training Program**
 - Six weeks, one night weekly 3 hour classes
 - One all day Saturday class
 - 10 hours of One on One consulting

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Technical Assistance

- **One on One Consulting**
 - Women's Business Center
 - Business Source Program
 - Any reputable government, educational or non profit resource, chamber of commerce, business advocacy group

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Growing the Business

- Critical Issues:
 - Approaches
 - Funding
 - Staffing
 - Operations

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Growing the Business

- Single Product Lender
- Multiple Product Lender
- Business Development Organization: TA and Lending
- Joint Venture between community organization and micro lender

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Growing the Business

- SBA Micro lending Program 7(m):
- CDBG, EDA, USDA
- Bank Contributions and Investments, including EQ2s
- Foundation grants and Program-Related Investments
- CDFI Fund

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Growing the Business

- Loan Officers: Accounting, finance skills
- Business Development/Customer Service: Good outreach and business acumen
- Loan Administrator: Familiarity with trust deed filings, UCC, vehicle registration, loan documentation
- Collections: Ability to deal with the “hard” part of the business

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Growing the Business

- Management: Financial management experience
- Loan committee development
- Loan policies that control losses, but encourage more and more lending
- Short Term: Generate sufficient net interest income to cover losses; obtain grant support for operations
- Long Term: Generate sufficient net interest income to fund 66% of program costs.

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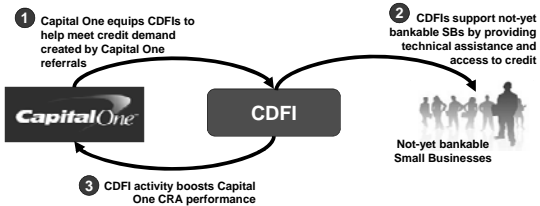
Understanding Microfinance:

2012 National Interagency Community Reinvestment Conference

Laurie Vignaud
Senior Vice President
Community Development Banking

Confidential

Small Business Development and CDFIs are important aspects of Capital One's economic development program



CRA Test	Considered in Exam
Lending	- Loans originated - Partnerships lead to future pipeline of new SB lending in LMI areas
Investment	- Grants
Service	- Volunteerism (mentoring, technical assistance)



Confidential

2

Underwriting criteria for CDFIs mirror standards established by U.S. Dept. of Treasury

Financial Analysis

- Organization in good standing with CDFI Fund
- Net Asset Ratio (equity/total assets) > 20%
- Minimum requirement:
 - * Min. cash = 3 months of operating expenses
 - * Min. cash loan reserve = 9% of total loan portfolio
- Net Income >= \$-0-

Mission and Program Benchmarks

- Strength of management, board and staff relative to the CDFI's size, complexity and risk profile
- Clarity of Business Plan with regard to mission, strategy and measurable program benchmarks
- Appropriate staffing with suitable MIS staffing in particular
- Capital One associate involvement (i.e., on the Board or Loan Committee)



Confidential

3

We partner with ACCION Texas Inc. to support access to capital

- ACCION Texas Inc. provides credit to small businesses that do not have access to loans from commercial sources
- ACCION helps micro entrepreneurs:
 - strengthen their businesses
 - stabilize and increase their incomes
 - create additional employment
 - contribute to the economic revitalization of communities
- Languages: English and Spanish
- ACCION also provides technical assistance



Confidential

4

Capital One Micro Finance Programs

- \$second Look Program
- Getting Down to Business
- Straight Talk Series



Confidential

5

Our \$second Look program promotes access to credit

- The goals of the \$second Look program are to:
 - Strengthen the bank's ability to meet the credit needs of our existing and potential small business clients
 - Strengthen deposit relationships, and
 - Win new customers
- Declined small business loan applicants are referred to ACCION Texas Inc., or a select non-profit alternative micro lender for a "second look."



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The \$second Look program allows us to meaningfully address small business challenges

- Banks are unable to approve many small business loan applicants - often due to lack of time in business and credit scores
- Many of these applicants are appropriate for micro lenders
- Declined loans jeopardize deposit relationships and the ability to attract new customers
- Small Business Lending is the heart of the Community Reinvestment Act (CRA)
- Win – Win for all partners: Capital One, Micro Lender and the Small Business Owner



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Our \$second Look Program supports CDFIs and small businesses

- Our **\$second Look** Program refers non-bankable small businesses to nonprofits for access to capital and technical assistance.
- We provide loans to nonprofit micro-lenders, like ACCION Texas Inc., to capitalize their loan funds.
- Our **\$second Look** Partners include:
 - ACCION Texas
 - PeopleFund
 - Plan Fund
 - SeedCo
 - Others!!!!
- 2011 YTD Totals:
 - 194 loans for \$5.4 million
 - 1,633 Referrals



Mr. Archie White of Archie's Bar B Q (second from left) was approved for a \$5,000 loan with ACCION Texas, Inc. which will be used for operational capital to secure a City permit and to purchase inventory.



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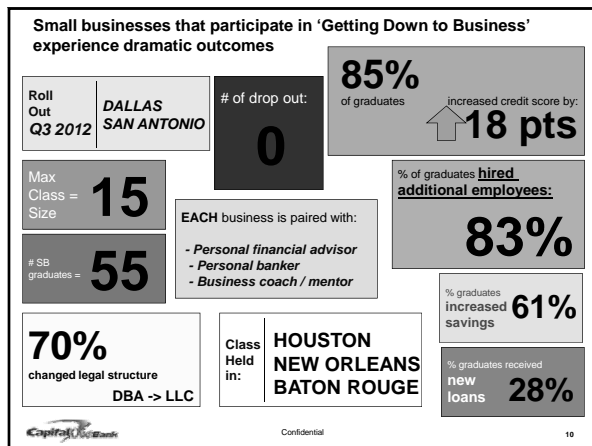
We created 'Getting Down to Business' to provide sustainable technical assistance to small businesses

- Small businesses have unique needs and challenges that are often not addressed in traditional training courses
- GDTB was designed to provide deeply customized information, identify relevant resources, mentors and financing options that meet unique business needs
- GDTB is a 7-month, 14 course highly interactive, matched savings program. Graduates receive a 2 to 1 match on their business savings account in addition to other benefits
- ACCION Texas Inc. is one of our CORE partners providing one-on-one technical assistance and access to credit



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- Our Straight Talk series offers small business workshops in LMI communities**
- Straight Talk was created to provide small businesses located in LMI communities with access to information and resources
 - One-on-one mentoring is included to allow businesses time to discuss their unique needs and network with others
 - We focus on 'Access to Credit' and resources available to small businesses
- Capital One Bank Confidential 12

Straight Talk seminars meet businesses where they are and offer critical technical assistance

- Small Businesses located in LMI communities are struggling to thrive in the current economy
- Workshops are conducted in local community churches, multipurpose centers, schools...near the small businesses ensuring easy access
- Local partners...including ACCION Texas, Inc. and others... volunteer to present at the workshops
- Overwhelming positive response and turnout
- To date, 40 workshops have touched more than 2,000 small business owners!



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Straight Talk Workshops



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Questions



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Laurie Vignaud, Senior Vice President
Capital One | Community Development Banking

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