Measuring Financial Return, Social Impact, and Risk

March 16, 2010
Overview

Session Objective:

Provide new insights into

1) Analyzing social impact and risk beyond CRA
2) Effectively conveying social impact to your stakeholders
Overview

The Panel:

- Janneke Ratcliffe - Associate Director, Center for Community Capital, UNC
- Paige Chapel - Director of CARS™
- Carla Dickstein – Senior Program Officer, Research & Development, Coastal Enterprises Inc.
- Trinita Logue – President & CEO, IFF
Overview

Agenda:

- Social impact beyond CRA
- CARS™ impact and risk assessments
- Triple bottom-line impact
- The importance of stories
- Emerging approaches to impact and risk measurement
- Q & A
Beyond CRA

Janneke Ratcliffe
Associate Director
Center for Community Capital
University of North Carolina
Comprehensive third-party ratings system of CDFI loan funds. Launched in 2004 by Opportunity Finance Network.

- Bring greater transparency and standardization to the field.
- Augments investors’ due diligence.
- Rate impact performance and creditworthiness.
- 50+ CDFIs are rated with 20 more scheduled.
Impact Performance Rating measures how well a CDFI does *what it says it’s trying to do*. Four components:

- Alignment of strategies
- Effective use of resources
- Measurement, tracking, and use of output data
- Measurement, tracking, and use of outcome data

Take policy change into account.
Why CARS™ distinguishes between *impact* and *impact performance*?

- CDFI strategies are crafted to address local challenges and opportunities.
- Collected data should respond to mission, which makes industry-wide standardization difficult.
- Actual impact can only be measured through a long-term, expensive evaluation process.
Financial Strength & Performance Rating assesses *overall creditworthiness*.

- Based on a CAMEL analysis similar to the one regulators use for banks.
- CARS™ does not use benchmarks.

Focus is on how a CDFI’s impact strategy translates into risk and how the CDFI protects investors from that risk.
Ratings distributions at 3/10/10

Impact Performance Ratings

- AAA: 37%
- AA: 18%
- A: 43%
- B: 2%

FSP Ratings

- 1: 39%
- 2: 39%
- 3: 14%
- 4: 6%
- 5: 2%

n = 51
No direct correlation between impact and financial strength and performance:

- 38% of all rated CDFIs received a AAA; 6% received a FSP 1.
- 70% of CDFIs that received lower Impact Performance ratings (A or B) were financially sound (FSP 2 or 3).
- 60% of CDFIs that were financially vulnerable (FSP 4 or 5) received a AA rating for Impact Performance.
Important to look for risk mitigants to offset higher-risk but effective impact strategies:

- High deployment that strongly supports mission can squeeze liquidity. Off-balance sheet strategies can be an effective mitigant.

- Higher-risk lending to achieve mission can be offset by
  - strong borrower support programs,
  - a deeper, more flexible capital structure,
  - stronger credit and portfolio management practices.
In general, most CDFIs with a strong commitment to measuring outcome against mission, also understand that strong financial performance leads to stronger impact.
Triple Bottom Line

A TBL approach to investment expands traditional double bottom line CRA criteria and looks for “the 3Es”:

- **Economic returns**: financial returns, jobs and assets, community or regional economic growth.

- **Equity returns**: assets and jobs created for historically disadvantaged individuals, sectors, and communities.

- **Environmental returns** that increase positive and reduce negative effects on nature’s macro systems.
Triple Bottom Line

WHY is TBL IMPORTANT?

It is not required for CRA. But it’s of growing importance to:

- Consumers
- Businesses
- Investors
- Policy Makers
Triple Bottom Line

CDFI Experience

CEI

- Conducted studies defining what is green, how to undertake sustainable development
- Launched Green Fund to finance green industries and businesses greening their production processes and services.
- Undertook sector initiatives (farms, fisheries, forestry).
- Experimented with incentives in exchange for increased environmental benefit.
Triple Bottom Line

CDFI Experience

TBL Collaborative

- Started in 2004 with Ford Foundation support.
- 17 CDFI members around country
- Developed scorecard to document, demonstrate and assess impact of members.
Triple Bottom Line

CHALLENGES
- Environmental expertise to assess 3rd bottom line
- Finding TBL in one deal
- Additional Measurement Requirements – environmental measures differ according to sector.

OPPORTUNITIES
- New markets
- New partners
- New funding opportunities
- Greater impact
The Importance of Stories

Trinita Logue
President & CEO
IFF
Emerging Approaches

Janneke Ratcliffe
Associate Director
Center for Community Capital
University of North Carolina
2010 National Interagency Community Reinvestment Conference

March 2010
IFF Background

- CDFI established in 1988
- Standard product is long term real estate loan to nonprofit service providers in low income communities
- Illinois, Indiana, Iowa, Missouri, Wisconsin
- Major sectors are health clinics, supportive housing, child care centers, charter schools, multi-service community centers
Telling the Story of Investment Impact

The Borrower

• Background
• Mission
• Goals (defining success)

The Borrower’s client

• Needs
• Environment
• Goals (defining success)
How We Tell the Story

External to the Borrower

• Community needs
• Resource opportunities
• Relationships structured to take opportunities

External to the Borrower’s client

• Poverty
• Social issues/deficits
• Disability
Primary IFF goal:

- Building Net Assets over time
- We go back ten years and review audits
- Examples of combined stories in annual report
- Additions each quarter

www.iff.org
Thank you