CDFIs as Catalysts for Improving Social Outcomes

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Introduction

Community development financial institutions (CDFIs), which play an important role in providing financial products and services to underserved communities, are increasingly being asked to demonstrate measurable returns. This demand for quantifiable impact is not unique to the CDFI industry.[1] As public and private resources become increasingly scarce, it is a challenge they share with many other sectors. In response, both CDFIs and their investors have expressed increased interest in measuring social impact. In other words, how were people's lives improved as a result of a particular community development effort? This article identifies some of the primary challenges that CDFIs face when it comes to measuring these non-financial returns, and demonstrates how the use of a logic model, a tool used by evaluators, can help CDFIs effectively communicate their role as catalysts for improving social outcomes in underserved communities.

The Current State of CDFI Impact Measurement

Since the 2008 financial collapse, the role of CDFIs has become increasingly important in meeting the credit needs of low- to moderate-income (LMI) communities. According to a recent report by the Aspen Institute, CDFIs are being challenged to reach a greater share of underserved communities than ever before.[2]

At the same time, many investors, including philanthropic foundations, are requiring CDFIs to produce not only positive financial returns, but also data that demonstrate community- or household-level impacts. However, when it comes to measuring social performance, many CDFIs are not equipped to meet such demands. Instead, they most commonly track those end-products that are easily quantifiable, such as the number of loans granted, number of minority clients served, and number of housing units financed. In recent years, the industry has tried to move toward a more sophisticated form of measurement, but has done so with limited success.

One example is the CDFI Assessment and Rating System (CARS™). CARS began as a project of the Opportunity Finance Network and became independent in 2012. It provides investment quality ratings for participating CDFIs. CDFIs that are CARS rated receive two performance ratings: one for financial strength and one for "impact performance." CARS does not measure actual impact, but rather the extent to which a CDFI is having the impact it sets out to accomplish, including the institution's capacity to measure impact and use those measures to improve performance (see sidebar for more information on CARS). Although CARS recognition of the value of outcome measurement is a step in the right direction, CARS does not tell a CDFI what to measure or how to measure it, quantify social impacts for investors, nor generate impact measures by which CDFIs can be compared with each other.

Overcoming Measurement Challenges

CDFIs face many challenges when it comes to being able to demonstrate longer-term impacts. According to Denise Armbrister, Vice President and Executive Director of Wells Fargo Regional Foundation in Pennsylvania, one of the greatest barriers to measuring impact at the household level is that many of the customers served by CDFIs are highly mobile.[3] This characteristic is common in underserved communities, making it very difficult to conduct longitudinal studies that capture long-term impact.

Another issue that CDFIs face when it comes to measuring impact is the question of who gets credit. Kate Barr, Executive Director of the Nonprofits Assistance Fund in Minnesota, provides the example of a CDFI that finances a childcare center in cooperation with other investors.[4] Can that CDFI take credit for the initial childcare slots created, or should it attribute only a portion of these slots to its efforts? Furthermore, is it appropriate to look at return on investment over-time and count the anticipated number of children served by the center over the next ten years? Barr points out that "CDFIs cannot be held accountable for everything."

Armbrister offers some valuable advice. She says that the Wells Fargo Regional Foundation in Pennsylvania looks for contribution, not attribution. In other words, would the

CARS™ Ratings

Among the criteria used for CARS impact assessment are:

1) How well do a CDFI's strategies, products, and services (activities) align with its mission?
2) Has the CDFI identified outputs and outcomes that are appropriate to track given its mission?
3) What methodology does the CDFI use to collect data?
4) How does the CDFI interpret and use evaluation data to increase its effectiveness?
5) Do outcome data demonstrate the CDFI is reaching its target population with its products and services?

Based on these criteria, CDFIs that participate in CARS may receive an impact performance rating of AAA (highest), AA, A, or B (lowest). The CARS rating scale also takes into consideration a CDFI's role in supporting policy changes that benefit disadvantaged individuals and communities. CDFIs that demonstrate evidence of leadership in this area can receive a "policy plus" rating.[5]

The cost of obtaining and maintaining a rating for CDFIs can range from $6,000 to $10,000 every three years, depending on asset holdings. For potential investors, the cost of ratings reports can range from $2,500 for three years of reports on one CDFI to $15,000 for access to ratings reports on all CARS rated CDFIs during a 12-month period.[6] Because the CARS rating process is very rigorous—both on impact performance and financial strength—many CDFI loan funds delay the ratings process until they can prepare their organizations for a CARS assessment. To date, about twelve percent of all certified CDFI loan funds, which collectively manage 46 percent of all on-balance-sheet assets, have been CARS rated.

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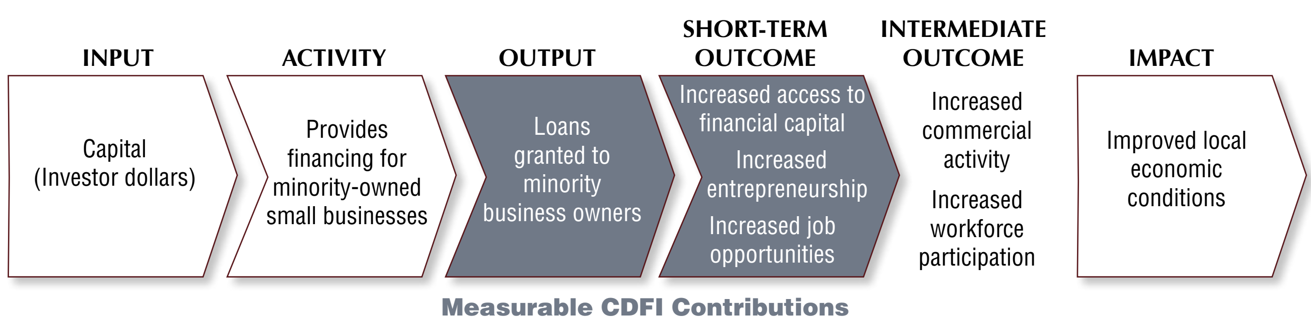
outcome have occurred if the CDFI had not contributed financing? Instead of focusing on longer-term impacts, she suggests that stakeholders look at the contribution of CDFIs from a catalytic perspective. This framework is particularly useful when it comes to demonstrating the value of CDFIs in producing improved social outcomes.

One simple way to visualize CDFIs as catalysts is to think in terms of a logic model. As described by Paul Mattessich, Executive Director of Wilder Research, a logic model is a visual diagram that uses a sequential point of view to measure the results of an effort. Figure 1 depicts a simplified sample logic model for a CDFI that finances minority-owned businesses. The model begins with the inputs that go into a community development effort, such as capital. It then moves on to activities: what does the CDFI do? In this example, the CDFI provides financing to minority-owned businesses. The next category in the sequence is outputs: the immediate, countable results from those activities, i.e. number of loans granted to minority business owners. And then outcomes: what happened as a result of the CDFI's efforts both in the short term and the long term?[7] The final category in the logic model, impact, identifies the ultimate goals or conditional changes we want to occur. Most often, a CDFI's measurable contributions fall into the "output" and "short-term outcome" categories. The value of a logic model for CDFIs is that it illustrates their role as catalysts by relating their contributions to broader social impacts.

Because CDFIs provide financing to underserved individuals and communities that would not otherwise have access to credit, many of the outputs that CDFIs currently track can be expanded to include measurable outcomes. For example, the output "number of loans granted to minority-owned businesses" can lead to the outcome, "increased financial access for minority-owned businesses." This poses the question, how can we be certain that these individuals would not have obtained a loan from a traditional financial institution? One relatively inexpensive way to provide supporting evidence would be to look at credit scores. If a CDFI's loan recipients have credit scores within a certain point-range or below the average minimum score accepted by traditional lenders in that same geographic area, it is reasonable to assume that the CDFI catalyzed the longer-term outcomes by providing increased access to credit.

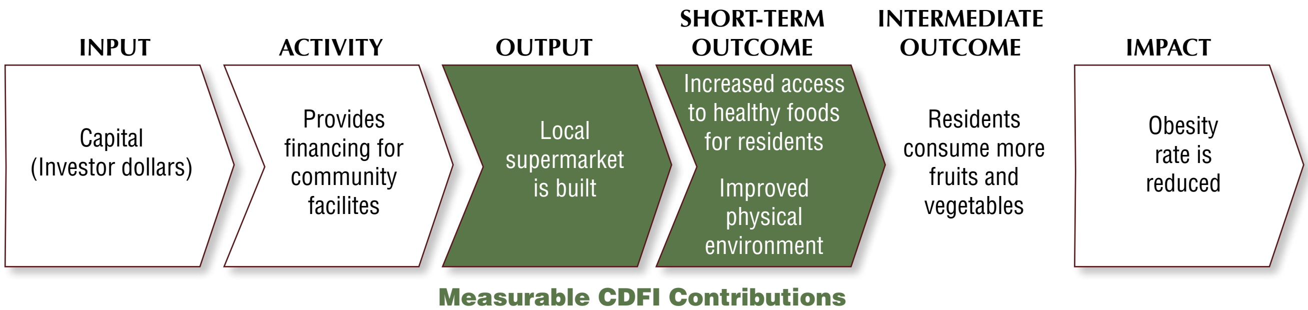
The case of healthy foods financing (Fig. 2) provides another example of the catalytic role that CDFIs can play in improving community conditions. In this example, a CDFI that provides financing for community facilities is the catalyst for a local supermarket being built. In a food desert, this measurable output leads to the short term outcome "increased access to healthy foods." The intermediate outcome "increased consumption of fruits and vegetables" is one behavior change that can have a positive effect on reducing the obesity rate. While CDFIs are not in the business of health behavior change, their lending activity leads to the increased access that makes this behavior change possible. Local supermarkets are illustrative of another community-level outcome that CDFIs

Figure 1. *Simplified Logic Model for CDFI That Finances Minority-Owned Businesses*



CDFIs play an important role by acting as a catalyst for impact.
Focusing on outputs and shorter-term outcomes can help meet investors' demand for measurable social returns.

Figure 2. *Simplified Logic Model for CDFI That Provides Healthy Foods Financing*



often catalyze, which is an improved physical environment. New or rehabbed buildings can increase the confidence of consumers who may choose to buy a home or locate their business in the neighborhood. In addition, they can also increase a given area's local tax base.

Adoption of these concepts used by evaluators can be extremely useful. When used correctly, the language and tools of evaluation can help communicate the value of CDFIs' contributions toward desired longer-term, community-level changes. For example, the output "number of participants who receive start-up loans" catalyzes the outcome "increased entrepreneurship," and the "number of houses rehabbed" catalyzes the outcome "increased affordable housing opportunities." Barr reminds potential investors and other key stakeholders that, when it comes to measurement, "we need to look at what is appropriate and what is realistic." It is difficult to measure long-term conditional changes over time. However, we can measure the outputs and shorter-term outcomes that are necessary in order for impact to occur.[8] A logic model helps illustrate the relationship between the two and can help CDFIs meet investors' demand for measurable social returns.

Making Broader Connections

When it comes to improving quality of life for individuals in underserved communities, community development investments are often, and sometimes literally, the bricks and mortar. Quantifying the net value of these investments, including their spillover effects, requires an accurate estimate of the dollar value of goods and services produced by the CDFI sector. This is a challenge for community development researchers to tackle as CDFIs seek to move toward more sophisticated methods of capturing non-financial returns. In the meantime, CDFIs can respond to investor demands for social impact measurement by focusing on the catalytic role they play in the production of outputs and outcomes necessary for longer term, community-level changes. Says Ambrister, "As a field, we are still trying to knit together our story." CI

Endnotes

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1. This article reflects the opinions of the author, and not necessarily those of Wells Fargo.

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