

## Building CDFI Capacity in Lending and Business Models\*

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Over the past three decades, community development financial institutions (CDFIs) have been nimble innovators, offering products and services to people, projects, and organizations that mainstream financial institutions could not or would not serve. They opened new lending pathways to address some of the most stubborn challenges facing poor communities across the country. The focus of CDFIs was originally on financing affordable housing and then shifted in recent years to financing schools and child-care centers, healthful food markets, small and microbusinesses, and community health centers.

CDFI partners<sup>1</sup> frequently ask CDFIs to scale successful local programs into replicable models to serve other low-income communities across the country or to enter new sectors of lending in communities where CDFIs are already working, in other words, to build their capacity to serve low-income communities.<sup>2</sup>

For the past two decades, the Opportunity Finance Network (OFN) has worked with CDFIs and their partners on a number of capacity-building initiatives to help CDFIs expand geographically, offer new financial products and services, and increase their positive impact on low-income communities.<sup>3</sup>

Capacity building occurs in two areas — lending sectors and business models. The first area helps CDFIs develop expertise in new sectors of lending, such as:

- **Healthy food financing:** Recently, OFN worked with experts in healthy food financing, including The Reinvestment Fund of Philadelphia, to codify the best practices to share in capacity-building efforts nationally. Over 1,200 individuals across the country participated in some aspect of this program.
- **Microfinance:** Currently, OFN is working with credit unions

and loan funds serving low-income communities to increase the availability of microfinance financial products to support job creation and growth of small businesses.

- **Community health centers (CHCs):** These pillars of the health-care system in low-income communities currently serve 20 million people and are expected to serve over 40 million people due to the expansion of Medicaid in the Affordable Care Act. OFN is bringing together three CDFIs<sup>4</sup> with the greatest expertise in financing CHCs and the National Association of Community Health Centers to train up to 100 CDFIs across the country to effectively lend to CHCs.

The second type of capacity building helps CDFIs implement innovative business models, such as:

- **Referral networks:** CDFIs can refer borrowers to other

\* The views expressed here are those of the author and do not necessarily represent the views of the Federal Reserve Bank of Philadelphia or the Federal Reserve System.

<sup>1</sup> Leading CDFI partners in capacity building include the Community Development Financial Institutions Fund of the U.S. Department of the Treasury (CDFI Fund), the Federal Reserve Banks, the Annie E. Casey Foundation, the Goldman Sachs 10,000 Small Businesses Initiative, Citi, Wells Fargo, and Bank of America.

<sup>2</sup> OFN-member CDFIs have demonstrated the ability to lend prudently and productively in high-risk markets. OFN-member CDFIs had a net charge-off rate of 1.7 percent in fiscal year 2011, according to an OFN report, available at [ow.ly/oQYrx](http://ow.ly/oQYrx).

<sup>3</sup> For more information, go to [www.opportunityfinance.net](http://www.opportunityfinance.net) and select Strategic Consulting.

<sup>4</sup> The three CDFIs are Capital Link in Boston ([www.caplink.org/](http://www.caplink.org/)), Primary Care Development Corporation in New York City ([www.pcdcnyc.org/](http://www.pcdcnyc.org/)), and NCB Capital Impact in Arlington, VA ([www.ncbcapitalimpact.org/](http://www.ncbcapitalimpact.org/)).

CDFIs that have different lending capabilities. For example, a housing lender might refer small business loan inquiries to a small business CDFI, and a small CDFI might refer a large deal to a CDFI with greater capital available to lend. Strong referral networks are built on shared values, a shared mission, and trusting relationships. OFN has helped facilitate this environment through dedicated efforts in Baltimore, Atlanta, and other cities as well as through OFN's regional meetings.

- **Technology:** CDFIs increasingly use technology at every stage of the lending process. CDFI loan officers work with borrowers at their place of business using remote scanning devices for loan applications. In some cases, new CDFIs adopt innovative uses of technology more aggressively than more established CDFIs.<sup>5</sup> CDFIs also use shared services technology platforms to support underwriting, loan administration, and participations.
- **Outsourcing:** CDFIs recognize that they can outsource activities that are performed better by others and focus on mission-critical activities. For example, CDFIs offering Small Business Administration (SBA) 7(a) loans through the Community Advantage program use lender service providers (LSPs) that provide compliance services for SBA loan guarantees. A more established practice is to outsource loan administration and servicing to local banks or other CDFIs.

In both types of capacity building, investment in capacity building allows CDFIs to serve low-income communities with a greater set of responsible financial products and services.

In capacity building work, OFN has found that successful capacity-building programs:

- **Use multifaceted approaches to help CDFIs learn and implement strategies.** Successful capacity-building programs include:
  - In-person training,
  - Ongoing webinars or teleconferences,
  - Communities of practice for groups with similar interests to share knowledge, and
  - Capital and operating grants to support expansion of new capacity.
- **Provide technical assistance following training:** It is important to provide follow-up technical assistance to help CDFIs implement new capacity. In healthy food financing, 75 percent of CDFIs receiving one-on-one technical assistance following training made healthy food loans within six months of receiving the assistance.
- **Are creative in designing capacity-building initiatives:** While developing the Scaling Up Microfinance initiative,<sup>6</sup> OFN recognized that credit unions serving low-income communities play a vital role in providing "micro" financial products to small businesses. Integrating credit unions and loan funds in building capacity for microfinance led to rich collaboration nationally and locally.
- **Incorporate talent development into all capacity-building initiatives:** Topics such as leading organizational change, negotiating effectively, creating an innovative culture, and understanding the employee life cycle ranked among the most highly valued aspects of capacity-building programs by participants.



Mrs. Hui Ping Liu came with her family from China to the U.S. in 2003 and started LH Human Resources, Inc., a 25-person home health-care agency serving Chinese and Vietnamese families with physically or mentally disabled members. Traditional lenders declined her loan application, and in 2010 she qualified for a \$35,000 microloan through the Business Center for New Americans, a CDFI and microlender in New York City. Today, the business employs more than 100 individuals.

- **Identify successful practitioners to replicate or create best practices:** In some cases, such as healthful food retail and CHCs, some CDFIs use proven underwriting models that can be codified and disseminated through training. However, when proven models do not exist, OFN convenes a meeting of cutting-edge thinkers to develop a new set of best practices. This approach was used to develop the curriculum for financing sustainable agriculture lending.

In conclusion, effective capacity building brings innovation to life at individual CDFIs and those across the nation. Capacity building is the disciplined and creative investment required to keep technical skills and business models of CDFIs aligned with the needs of the communities they serve.

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<sup>5</sup> The Intersect Fund, located in New Brunswick, NJ, is among the most technologically advanced microlenders.

<sup>6</sup> For more information about the Scaling Up Microfinance initiative, see [ow.ly/oQZ0S](http://ow.ly/oQZ0S).