Wouldn’t it be easier and more efficient to invest in Community Development Financial Institutions if a rating system existed to provide an objective, third-party analysis?

The newly established CDFI (Community Development Financial Institution) Assessment and Rating System (CARS) makes monitoring CDFI investments easier and more effective. Reports by analysts with CDFI experience consider financials, portfolio and other CDFI information to document any deterioration or improvement.

New CDFI rating system
CARS makes it possible for banks and other investors to access ratings and analyses on a growing number of CDFIs. The Opportunity Finance Network of the National Community Capital Association began analyzing and rating CDFIs through CARS in late 2004, and the number of rated institutions is growing along with investor interest in the new system.

Thus far CARS has rated 22 CDFIs and provides regular annual reviews on rated CDFIs. By the end of 2006 the number will grow to nearly 30. Its clients include some of the largest and best known institutions, such as The Reinvestment Fund in Pennsylvania and Low Income Investment Fund in California, as well as smaller CDFIs like the Florida Community Loan Fund, The Housing Fund in Tennessee and People Fund in Texas.

CARS assesses CDFIs in the areas of impact performance, financial strength and overall performance. Each report includes ratings and a thorough analysis of at least twenty pages with user-friendly summaries, in-depth assessment, financial statements and ratios, and tables showing trends.

Reports cover four key impact performance criteria and provide analysis of capital, assets, management, earnings and liquidity in a "CAMEL" format. It also includes a peer comparison that investors can use to establish a context for the investment opportunity they are considering.

In a recent speech, Federal Reserve Board Chairman Ben Bernanke highlighted the value of CARS for investors and community development:

"...the Opportunity Finance Network’s CDFI Assessment and Rating System (CARS) gathers data to evaluate a CDFI’s overall creditworthiness and effectiveness in using its financial resources to achieve its development objectives. A CDFI is rated in a manner broadly analogous to the way a supervisory agency would rate a commercial bank...Although still in its early stages, this initiative, if successful, will have the double benefit of attracting more funds into community development and helping to ensure that those funds are effectively used."

CARS can increase the efficiency and effectiveness of both CDFI underwriting and monitoring. Sixteen leading CDFI investors including banks, socially responsible investors and foundations, are already using CARS in their due diligence process, to structure loan covenants, and to monitor their existing investments.

CDFIs also benefit from rating system
Not only is CARS helping investors, but rated CDFIs are benefiting as well. As investors increase their use of CARS, they demand less information (and thus less time and energy) from rated CDFIs during both the underwriting and monitoring processes. Some investors are beginning to give priority to rated CDFIs and to use the CARS ratings in their covenants. Some are also considering offering discounts to rated CDFIs because lending to them is less expensive.

One of the most significant initial impacts of CARS has been improved transparency and performance on the part of CDFIs. The rigor of the analysis helps CDFIs understand their strengths and challenges, and it motivates them to address issues that will help them improve and achieve a higher rating.

Although CARS is still in its infancy, it holds enormous potential to facilitate investing in CDFIs, to help new investors enter the CDFI market, to help CDFIs improve their performance and, ultimately, to increase the flow of capital to disadvantaged people and communities through sound investments in CDFIs.

This article was written by Kathy Stearns, executive vice president at Opportunity Finance Network.
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**Rated CDFIs** (analyses currently available)*

- Coastal Enterprises, Inc.
- Community First Fund
- Federation of Appalachian Housing Enterprises
- Florida Community Loan Fund
- The Housing Fund (Nashville)
- Low Income Investment Fund
- Lenders for Community Development
- Mercy Loan Fund
- Montana CDC
- New Hampshire Community Loan Fund
- Nonprofit Finance Fund
- Northern Economic Initiatives Corporation
- Northland Foundation
- PeopleFund (formerly Austin CDC)
- Primary Care Development Corporation
- The Reinvestment Fund
- Rural Community Assistance Corporation
- Unitarian Universalist Affordable Housing Corp.

**CDFIs in the Pipeline** (as of July 2006)*

- ACCION New York
- Arcata Economic Development Corporation
- Boston Community Capital
- Chicago Community Loan Fund
- Clearinghouse CDFI
- Connecticut Housing Investment Fund
- Enterprise Community Loan Fund
- Enterprise Corporation of the Delta
- Greater Berks Development Fund
- Housing Assistance Council
- Housing Development Fund of Lower Fairfield County
- Housing Partnership Network
- Illinois Facilities Fund
- Initiative Foundation
- Kentucky Highlands Investment Corporation
- LISC
- Mile High Housing Fund, Inc.
- NCB Development Corporation
- Nonprofit Assistance Fund
- Partners for the Common Good
- Seedco
- ShoreBank Enterprise Pacific
- South Hartford Initiative
- Spokane Neighborhood Economic Development Alliance
- Vermont Community Loan Fund
- Western Massachusetts Enterprise Fund

* Green text indicates the CDFIs in the process of being rated, or scheduled to be rated. Note: At this time, CARSTM is not rating depository institutions or venture capital funds.