14 STRATEGIES for Partnering with Mission-Focused Banks

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These activities are designed to help people build meaningful lives in which they can experience health and well-being, pursue effective education and gainful employment, and access the resources required to create ever-expanding opportunities for themselves and their broader communities.

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EXECUTIVE SUMMARY

Throughout American history, not all segments of society have benefited from the prosperity generated by economic growth and job creation. Pockets of substantial inequality have existed, particularly in minority communities for whom median household wealth continues to lag significantly compared to nonminorities. Compounded by longstanding wealth disparities, the twin health and economic shocks spurred by COVID-19 have devastated minority and low-income households. Access to capital has been among the most important limitations for many minority-owned business enterprises on withstanding the current crisis, increasing scale, and driving post-COVID economic development locally and nationally.

Previous Milken Institute research found that federally designated and mission-driven Minority Depository Institutions (MDIs) and Community Development Financial Institutions (CDFIs) can be powerful fulcrums for equitable access to capital for minority and low-income communities. MDIs are financial institutions in predominantly minority communities, in which minorities own at least 51 percent of the voting stock and comprise the majority of the board of directors. CDFIs are financial institutions that must originate at least 60 percent of their loans and investments in eligible distressed and underserved communities. These institutions have an outsized presence in low-income and minority communities—which demonstrate profound unrealized economic and social potential. More importantly, MDIs are just as efficient as their non-MDI counterparts and, with increased scale, can do more to advance equitable access to the American Dream for underserved populations.

The Milken Institute, with support from JPMorgan Chase, has developed a primer for equitable economic development to bridge the racial wealth gap with a focus on equitable access to capital. The purpose of this research is to distill strategies of how stakeholders can partner with MDI and CDFI banks, which have strong track records of targeting underserved communities, to increase their capacity and scale of impact. The strategies are framed to guide various partnerships and encourage stakeholder (e.g., big banks, corporates, philanthropies) engagement. These strategies fall into three levels of engagement:

1. **Repairing** immediate balance sheet capacity needs thorough Tier 1 capital injections,
2. **Restoring** access to capital at parity across the nation by considering exemplary business models in the industry, and
3. **Reimagining** the banking system in light of the spectrum of financial services disruptions to ensure minority and low-income communities actively participate in post-COVID recovery and the banking future.

Notably, the Reimagining phase set of strategies is critical to ensure a sustainable future for both MDIs and CDFI banks and the communities they serve. In order to find success in the strategies of Repair and Restore, the Reimagine phase must be considered as the eventual target.

In 2020 there was a realization about the importance of racial equity and the stark vulnerabilities of low-income communities, resulting in billions of dollars in commitments towards bridging the racial wealth gap and focusing on better serving the underserved. In 2021 and beyond, leaders will need to follow through with action and a fresh eye towards both implementing sound strategies and creating a future with equitable access to capital, and therefore access to the American Dream. Through stakeholder discussions and quantitative analysis, we find that implementing these three sets of strategies will bolster MDIs and CDFIs to be that bridge. We encourage all stakeholders to collaborate to ensure post-COVID recovery is equitable.
METHODOLOGY

Each strategy serves as a high-level illustrative partnership approach towards scaling MDIs and CDFIs and potentially facilitating a bridging of the racial wealth gap; stakeholders should endeavor to refine approaches to their particular context, counterparties, region, and regulatory considerations.

Figure 1: Pathway to Community Empowerment

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Source: Milken Institute (2021)

Increasing the scale of MDIs and CDFIs is a multiprong strategy that includes strengthening capital structure, institutional learning, and operating efficiency. Partnerships vary by the entity and engagement level. As a result, this analysis is broken down into three levels of engagement: repairing MDIs and CDFIs, restoring accessibility to capital in underserved communities through MDIs and CDFIs, and reimagining the roles of MDIs and CDFIs in a future banking ecosystem. Secondarily, the analysis examines potential options that can apply to a variety of institutions.

In the Repair phase, the objective is to help MDI and CDFI banks strengthen balance sheets to a minimum 10 percent tangible common equity (TCE) ratio or maintain higher ratios to provide a sufficient capital cushion to support the risks that sometimes accompany lending to targeted populations. Our top-down approach focused on Federal Deposit Insurance Corporation (FDIC) data from the first, second, and third quarters from 2016 to 2020 to smooth out the balance sheet impact of the
Small Business Administration’s (SBA) Payroll Protection Program (PPP) on financial health determinants.\(^1\) By segmenting banks by total assets into five geometrically decreasing bands from in excess of $1 billion, the analysis resulted in roughly flat population distribution. Of the 249 CDFI and MDI banks in our model, approximately 50 fell into each asset band of upper bounds at $125 million, $250 million, $500 million, $1 billion, and in excess of $1 billion. This enabled us to compare the descriptive statistics of each band and, more importantly, highlighted the success of banks that were able to grow consistently across bands. It also became clear that the capital gap between Tier 1 and total capital is inhibiting growth for nearly a quarter of MDI and CDFI banks. Each strategy in this phase outlines how different entities can bridge this immediate need to catalyze healthy banks.

In the Restore phase, we identify potential best practices to help MDIs and CDFIs achieve scale, including Tier 1 capital multiplier strategies ranging from increased loan deployment and diversification into higher-margin products, to efficiency and customer acquisition investments such as digitization. To do this, we identified “lighthouse banks,” MDIs and CDFIs that have historically out-scaled their peers by analyzing the longitudinal and institutional trends defined by total assets, return on average equity (ROAE), return on average assets (ROAA), non-performing assets, efficiency, and tangible common equity as reported by the FDIC. We deconstructed lessons learned and formulated strategies for this phase through a dual approach of a bottom-up quantitative review of these banks and top-down qualitative interviews conducted with key stakeholders.

Finally, in the Reimagine phase, we held stakeholder calls with a range of experts, including a trade association of MDIs, leadership of MDI and CDFI banks, numerous national and regional banks, philanthropists, and policymakers to brainstorm and stress-test strategies for MDI and CDFI banks to evaluate how best to position their efforts for the future of banking.

\(^1\) As MDI and CDFI banks stepped up to deliver PPP loans, the 1 percent interest products began to inflate total assets, depressing key bank financial health determinants such as return on assets. In our multiyear analysis, we looked for consistency in trends across quarters rather than absolute figures.
What Are MDIs and CDFIs?

**Minority Depository Institutions** (MDIs) are federally designated financial institutions in predominantly minority communities, in which minorities own at least 51 percent of the voting stock and/or make up the majority of the board of directors. Minorities are defined as Black or African American, Hispanic American, Asian or Pacific Islander American, Native American or Alaskan Native American, and Multiracial. As of Q4 2020, there are 142 MDI banks with more than 1,000 branches and with total assets of $287.4 billion.

**Community Development Financial Institutions** (CDFIs) are federally designated financial institutions that must originate 60 percent or more of their loans and investments in eligible census tracts or to underserved populations. The Community Reinvestment Act (CRA) recognizes loans and investments in CDFIs as qualified CRA activity. As of 2019, there are 145 CDFI banks with more than 900 branches.

This report focuses principally on banks that are also MDIs and CDFIs, except Strategy 2, which addresses credit unions that are also MDIs and CDFIs.

MDI and CDFI Lighthouse Banks

From 2016 to 2020, the MDI and CDFI banking cohort has faced significant headwinds, shrinking from 334 banks to 290. Many banks have thrived despite this, and some have done so in ways that shed light on the future of mission-focused lending. Grouping all banks into bands by total assets, three banks particularly demonstrated consistent, industry-leading asset growth and other financial health determinants. The following banks signal promising ways for MDI and CDFI banks to transform Tier 1 capital into expanded access to finance:

**Quontic Bank:** A CDFI with a single storefront in Astoria, New York, Quontic Bank has grown its total assets from $227 million to almost $1.4 billion (including $800 million in PPP loans to the smallest businesses nationally) over the most recent four-year period as an “Adaptive Digital Bank.” Quontic has also funded an additional $1.3 billion in loans, which it sold to third parties—two-thirds of which were to low-income families or in low-income communities.

**Sunstate Bank:** A Hispanic MDI based in Miami, Florida, Sunstate Bank has grown through regional M&A and serving the digital financial needs of immigrants and their businesses.

**Gateway First Bank:** A Native American MDI based in Jenks, Oklahoma, Gateway First Bank has expanded from $336 million to over $1.6 billion in total assets via regional M&A, expanding access to differentiated financial products across Oklahoma.

**City First Bank and Broadway Bank:** Los Angeles-based Broadway Bank, an MDI, and DC-based CityFirst, a CDFI, merged in 2020, creating the largest Black-led bank in the nation, with more than $900 million in deposits and more than $1 billion in assets.
Figure 2: ROAA of All Banks Broken Out by Designation

Figure 3: Total Assets of Lighthouse Banks Broken Out by Institution

Source: Milken Institute (2021)
PHASE 1: REPAIR

For a bank, maintaining an adequate level of risk capital is not just a regulatory requirement: It is a prudent standard for ensuring a bank has enough capital to sustain operating losses and can protect its investors, depositors, and the communities they serve. US banking regulators have set a permanent floor for these requirements—8 percent for total risk-based capital (Tier 2) and 4 percent for Tier 1 risk-based capital. However, industry standards have evolved to closer to 10 percent for Tier 1 capital as an indicator of what investors are looking for and what will help grow these institutions. With less capital, MDIs and CDFIs are not drawing investor confidence and investments. This is heightened even more by the perception that the markets MDIs and CDFIs serve are riskier and in need of even greater capital.

With corporate and community stakeholders ready to make more deposits to MDIs and CDFIs, the pressure is now even greater to have more Tier 1 capital. Effectively, MDI and CDFI banks need to repair their balance sheets to bring them closer to industry best practices of 10 percent Tier 1 capital ratios. This gap can be closed through different types of capital as defined in the following strategies.

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2 Tier 1 capital is a bank’s core capital to fund operations and includes common stock, reserves, retained earnings, and certain preferred stock. Tier 2 capital, like Tier 1, funds capital needs of a bank but is limited to 25 percent of a bank’s capital requirements given it is relatively less liquid as determined by regulatory standards. Categories of Tier 2 capital include revaluation reserves, general provisions, hybrid capital instruments, and subordinated debt.
Tier 1 Capital Versus Deposits

In the wake of the 2020 George Floyd demonstrations and calls for racial equity and justice, addressing this market inefficiency by utilizing capital markets is a direct step towards empowering the Black community. Many institutions responded by offering support to MDIs and CDFIs through deposits.

**Deposits:** While deposits fuel the lending capacity of all banks, they require regulated institutions to maintain a minimum amount of equity capital. For smaller institutions, too many deposits add liability to income statements and the balance sheet, diluting limited capital bases of many banks in this cohort. To be more intentional in capacity building, stakeholders that wish to provide deposits should complement them with matching equity investments to MDIs and CDFIs.

**Tier 1 Capital:** To operate, banks require different forms of equity capital on their balance. Tier 1 equity capital is the most patient form of capital. It provides maximum flexibility for MDI and CDFI banks to scale and allows them to lend out with greater capacity to their communities. Importantly, Tier 1 capital is risk capital that provides MDIs and CDFIs a cushion to withstand potential losses, especially ones experienced in widespread economic downturns, like those seen in the current COVID-19-induced crisis.
STRATEGY 1

Direct Tier 1 Capital Investments

**Description:** Stakeholders that wish to create shared value in the communities they operate in can address these capitalization deficits through equity (and equity-like) investments in CDFIs and MDIs. Some of these banks offer comparable dividend policies and several demonstrate consistent return on assets. Beyond commercial returns, fueling the growth of these institutions can result in lifting communities up through financial inclusion and create stronger local economies where banks and corporations operate.

Mission-focused banks are increasingly open to sophisticated arrangements, such as fixed and floating rate perpetual preferred shares, to better meet both their and investors’ needs. Smaller mission-focused banks will tend to prefer subordinated debt and instruments with debt-like nature. Opportunities for meaningful impact are not limited by check size.

**Smart Action:** Banks and corporations looking to make non-concessionary investments, patient or otherwise, could reach out directly to CDFI and MDI banks for potential individual investments. Trade associations can act as effective intermediaries for these investments. For example, the National Bankers Association can arrange introductions with MDIs as a group or individually. By opening a dialogue with smaller CDFI and/or MDI banks, a range of options can be discussed.

Moreover, equity investments could be pursued in the following different forms: preferred stock that can productively be augmented with common stock investments, and through equity funds that are focused on Black banks and/or MDIs and CDFIs generally.

**EXAMPLES FROM THE FIELD**

- **Southern Bancorp:** One of the largest CDFI banks in the nation recently closed a $35 million round of fundraising by offering a regular dividend and share-buyback program.

- **Quontic Bank:** One of the fastest-growing CDFI banks and of comparable size to Southern Bancorp, Quontic Bank recently closed an offering totaling $8 million in fixed-to-floating rate noncumulative perpetual preferred stock. It deployed

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3 However, special attention should be paid to control triggers for compulsory regulatory disclosures, as well as limits to designation as a minority-owned institution.
Tier 1 capital to further digital transformations, yielding best-in-class asset growth and strong returns on equity.

- **Gateway First Bank**: The largest Native American MDI recently raised $40 million in equity in its merger to transform from a mortgage company to bank. It used its funds primarily to acquire a CDFI, Farmers Exchange Bank.

- **Broadway Federal Bank**: This bank raised $9.7 million to clean up its capital stack and invest in its infrastructure, resulting in a three-year climb from $366 million to $438 million in total assets. Broadway has since merged with City First Bank of DC, creating the largest Black-led bank in the United States.
STRATEGY 2

Direct Philanthropy Support

**Description:** MDIs and CDFIs have track records of supporting the underserved communities they reside in: For every dollar of Tier 1 capital invested, $10 of lending is deployed to the community, of which at least 60 percent is typically engaged in low-income and other underserved communities. According to previous Milken Institute research, Black MDI small business loan productivity is greater than that of non-MDI banks, which implies that not only would Tier 1 capital injections to CDFIs and MDIs go to underserved communities, job-creating small businesses would disproportionately benefit as well.4

However, due to MDIs' and CDFIs' undercapitalization, their full potential remains unrealized. Although Milken Institute research showed that MDI return on assets was just as efficient as non-MDI's, the perception of inefficiency persists. As a result, commercial capital markets consider social objectives as the only rationale to support MDIs. Unfortunately, they consider the social implications of an institution's strategy as countering their fiduciary duty to maximize return. Thus, philanthropies that are considerate of social return are well-positioned to mitigate perceived investment-associated risk assessments and support MDIs and CDFIs with non-dilutive grant capital. In addition, these stakeholders have the potential to crowd in private capital with customized blended financing tools, guarantees, and other credit enhancements.

**Smart Action:** If the objective is to mobilize access to capital to underserved communities, philanthropists could consider supporting MDIs and CDFIs regardless of their for-profit or nonprofit status. One way to do this is by providing a loan with interest up front that can be forgiven partially or entirely based on social outcomes the institution delivers, such as a specific amount or dollar value of loans to small businesses of minority ownership. The second way is the reverse: The philanthropy identifies requirements for institutions to get reimbursed (similar to a challenge grant that leverages other capital as the upfront funding) for activities with prioritized outcomes.

In tandem with supporting mission-aligned investments through capital, philanthropies can channel their resources towards tracking social metrics of MDI and CDFI banks’ activities, building or licensing FinTech products, managing public

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relations, marketing of mergers or acquisitions, and providing technical assistance for lower and moderate income (LMI) customers to use advanced banking products.

Another avenue of partnership could be, at the recommendation of MDI and CDFI banks, to provide low-interest and/or forgivable loans or grants directly to low-income and minority borrowers seeking down-payment assistance to facilitate homeownership that might be otherwise unachievable without such aid.

**EXAMPLES FROM THE FIELD**

- **Shorebank Corporation:** Although often cited as a failure, this innovative CDFI bank tested new organizational models and was the largest CDFI of its time. It failed in 2010 after 37 years of operation due to overconcentration in the real estate sector during the 2008 financial crisis. Nonetheless, Shorebank offers many lessons as a progressive social enterprise that multiple foundations supported.

- **W.K. Kellogg Foundation:** An overview of its mission-driven investments bank deposit strategy to community lenders can serve as a potential guide for other philanthropists.

- **SBA's Economic Injury Disaster Loans:** Loans and grant money provided by the Small Business Administration through a program that targets alleviating disaster-hurt small businesses can serve as a model for philanthropies to replicate.

- **Community Investment Guarantee Pool:** This platform allows guarantors to combine resources and expertise by establishing a one-stop-shop for intermediary lenders, such as CDFIs and MDIs. It was designed and launched a year ago and was founded by a group of philanthropies including The Kresge Foundation, Annie E. Casey Foundation, and Chan Zuckerberg Initiative.
MDI and CDFI Obligation to Low- and Moderate-Income Communities

CDFIs have similar mission-driven mandates requiring them to serve the underserved as MDIs do. CDFIs are federally certified private financial institutions created under the Community Reinvestment Act (CRA) in 1977. CDFIs were created to ensure lending was made in economically depressed neighborhoods in response to redlining and are required to designate 60 percent or more of financing activities to low- or moderate-income communities.

Figure 4: CDFI Bank Average NCIF Social Performance Metrics (SPM) Comparison (1996-2008)


MDI and CDFI Credit Unions

While the focus of these strategies is on for-profit MDI and CDFI banks (since nonprofit MDI and CDFI credit unions cannot receive equity investments), in this case, nonprofit MDI and CDFI credit unions present a smart approach, too. These credit unions need risk capital for the same reasons the banks do; thus, philanthropies can assist this group with grants.
STRATEGY 3

State and Local Matching Federal Efforts

**Description:** Governments have a critical role in creating a fertile environment to strengthen the institutions they administer. In fact, the federal government engaged in an exceptional level of economic intervention related to the 2020 COVID-19-induced crisis, demonstrating that it can act quickly to help underserved communities. In December 2020’s COVID-19 relief bill, Congress included $12 billion in spending towards CDFIs and MDIs: $9 billion for the Emergency Capital Investment Program and $3 billion in appropriations for the US Treasury’s CDFI Fund.\(^5\) Of the latter $3 billion, the CDFI Fund appropriates $1.25 billion for CDFIs to address immediate economic hardships due to COVID through its new CDFI Rapid Response Program and $1.75 billion towards expanding CDFI lending, grantmaking, and investing activities. This is substantial aid to its capacity, since the CDFI Fund only operates around $270 million in standard budget appropriations annually and may serve as a model for partnership.

This aid is the latest effort, as prior to this relief bill, the US Treasury instituted a Mentor Protégé program to encourage large fiscal agent banks to partner with MDIs. However, good intentions require commitments to reach desired outcomes; MDIs are entitled to preference as depositories for federal government funds but currently receive very few such funds. Nonetheless, leveraging a whole of government approach is necessary, as a Milken Institute analysis found that MDIs and CDFIs are well-placed in hard-hit COVID communities. The counties in the worst-hit quartile of case rates are twice as likely to have an MDI and CDFI banking presence than the least-hit and have a three times higher presence in the quartile of counties with greater African American populations than the bottom quartile.\(^6\) Leveraging the momentum sparked by federal activities into targeted local action may help ensure the worst-hit areas are prioritized.

**Smart Action:** State and local governments can match federal stimulus spending towards these institutions by including relief MDI/CDFI spending in local stimulus. Additionally, integrating local economic development efforts with MDIs and CDFIs, either through including them as fiscal agents and/or engaging them as underwriters/syndicators of well-funded public projects, can help diversify their

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revenue, strengthen their balance sheets, and, ultimately, improve their ability to help local communities.

EXAMPLES FROM THE FIELD

- **Federal stimulus bill**: Congress included a $12 billion carve-out for CDFIs and MDIs in the COVID-19 stimulus package, which includes $9 billion towards the capital investment program and $3 billion in grants to be awarded by the CDFI Fund. Provisions were included in the stimulus package from the Jobs and Neighborhood Act sponsored by Senator Mark Warner of Virginia, which establishes investment programs and revises provisions related to CDFIs and MDIs in the CARES Act of March 2020.

- **SBA and Treasury $10 billion for CDFIs**: As a part of the CARES Act’s Paycheck Protection Program, the SBA allotted $10 billion of Round 2 Funding to be lent exclusively by CDFIs.

- **California stimulus package**: The governor of California signed a $7.6 billion stimulus package that targets relief for small businesses.

- **Expanding Opportunity for MDIs Act, HR 5315, 116th Congress**: This bill establishes a Treasury mentorship program to better prepare MDIs to perform strongly as financial agents.

- **Ensuring Diversity in Community Banking Act, HR 5322, 116th Congress**: This bill establishes a Small Business Administration Task Force to support MDIs and CDFIs. It also encourages federal government deposits in MDIs and requires reports on diversity, equity, and inclusion from each prudential regulator.

- **FDIC Chairman Jelena McWilliams’ financial inclusion efforts**: In the age of COVID-19, the FDIC has increased its focus on community lenders by tripling MDI representation in their Community Bank Advisory Committee, enabling MDIs to review potential purchases of a failing MDI before non-MDI institutions are given the opportunity, and facilitating commitments to support MDIs, among other actions.

- **Illinois’ equity-centric legislation**: Illinois has enacted various legislative initiatives, including investing in CDFIs and MDIs ($150 million), creating a loan guarantee pool for Black and Brown entrepreneurs ($50 million), and expanding grant authority ($5 million per year) to boost entrepreneurship for Black and Brown communities.
CDFI and MDI Presence in Counties, Broken Out by COVID-19 Impact: The counties in the worst-hit quartile of COVID-19 case rates are two times more likely to have an MDI and CDFI banking presence than are counties in the least-hit quartile.

Figure 5: COVID, MDIs, CDFIs, and Opportunity Zones

Counties in the worst-hit quartile of COVID-19 case rates are 33 percent more likely to have Opportunity Zone designated tracts than are counties in the least-hit quartile.

Figure 6: Opportunity Zone Designations and Coronavirus Incidence Across All Counties
STRATEGY 4

Indirect Investing via a Fund

**Description:** Aside from traditional investors in the financial institutions space, investing in an individual MDI or CDFI may seem too daunting. As such, comingled products may provide the potential for multiple investors to collaborate in supporting multiple MDIs and CDFIs in a potentially distributed risk approach that benefits from portfolio effects. Additionally, investors with limited bandwidth can set social targets rather than deal terms.

**Smart Action:** Identify, vet, and invest in investment vehicles that manage and/or invest in mission-focused banks. Investors can decide whether to invest through comingled and/or blind pool funds that intend to invest or participate in already syndicated transactions.

**EXAMPLES FROM THE FIELD**

- **The Keepers Fund:** The Keepers Fund invests in MDIs serving low- and moderate-income communities and counts Uber and Square, Inc. as investors.
- **The National Community Investment Fund (NCIF):** NCIF targets CDFIs and includes some of the largest institutions and commercial banks as investors. They publish performance indicators to track the impact of their portfolio banks.
- **The Black Bank Fund:** With corporate and philanthropic partners, this fund aims to raise and invest $250 million by purchasing noncumulative and nonvoting preferred stocks in Black banks across the nation.
- **FDIC Mission-Driven Bank Fund:** This FDIC fund targets resilience-building MDIs and CDFIs.
- **Inclusiv:** For community development credit unions, Inclusiv dedicates resources beyond financial capital to support member lenders, amplifying investment impact.
- **Calvert Impact Capital and its Investment Note:** This leading impact investor explains its theory of change and investment approach in CDFIs and how a partner can invest in its portfolio.

**Relevant Stakeholders**
- National and regional banks
- Corporations
- Endowments and corporate and community foundations
- Entities looking to make investments with wide criteria of returns
- Financial institutions looking at mobilizing CRA activity
PHASE 2: RESTORE

According to previous Milken Institute research, approximately 70 percent of minority neighborhoods do not have a bank branch, and a lack of access to capital remains one of the critical gaps to driving economic prosperity in minority and other low-income communities.\(^7\) Given the longstanding wealth disparity in minority communities, modest improvements will not be enough. To close the racial wealth gap and restore economic prosperity, “overinvesting” in the scale and capacity of MDIs and CDFIs is necessary.

In our longitudinal analysis of mission-focused banks, it became clear that total asset size (i.e., scale) mattered. Virtually every measure of balance sheet health improved with increasing asset size and especially so for CDFI and MDI banks. Our “lighthouse banks,” or banks we have studied for outsized asset growth and performance, are representative of diverse communities and banking strategies. Still, all have demonstrated significant absorptive capacity for Tier 1 capital. Creating modern, robust foundations for these banks is made possible by the liquidity and safety provided by various forms of equity ownership. For some of these banks, rounds of fundraising are leveraged for regional M&A activity. For others, the funds are focused on digital infrastructure investment.

Restoring MDIs’ and CDFIs’ capacities involve enhancing capital and earnings, which includes organizational efficiency through human capital and technical assistance. This phase addresses the MDI and CDFI universe from the bottom up by identifying transferable lessons learned through an analysis of lighthouse banks that demonstrate strong, replicable business models. In addition to core growth strategies, our conversations with industry leaders revealed other systemic challenges inherent to mission-focused banking where investors can impact the barriers to parity. These can be considered forms of technical assistance and government-led intervention.

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STRATEGY 5

M&A-Fueled Scale

**Description:** Market forces and the regulatory response of the 2008 financial crisis resulted in consolidation across the sector. As a result, the number of FDIC-insured institutions has dropped significantly over the last decade, especially in minority and low-income communities. The same market forces hold true for the MDI and CDFI banking groups. Mergers and acquisitions are an effective way to rapidly scale MDIs’ and CDFIs’ capital, making banking more convenient for customers and enhancing competitiveness in the banking industry.

In our review of lighthouse banks and the greater cohort of mission-focused banks, mergers and acquisitions also contributed to their rapid increase in scale and services. In some cases, lenders with differentiated niches combined to balance their portfolios and expand access.

**Smart Action:** Stakeholders could consider their role in supporting MDI and CDFI bank holding companies that are parents to mission-focused banks in merging or acquiring other MDIs and/or CDFIs to spearhead the consolidation-fueled scale-up of the sector. Inorganic strategies could focus on supplementing gaps in capabilities: capital, technology infrastructure, legal, and/or human capital. Thus, prior to pursuing a merger or acquisition, the bank holding entity could do an internal needs assessment and external assessment to ensure an optimal post-integration outcome.

Foundations and philanthropists can also engage in this by (1) directly investing in/or creating an MDI acquisition vehicle through below-market-rate investment as a General Partner (GP) or a Limited Partner (LP), (2) supporting investors indirectly by providing credit enhancements (e.g., guarantees or subordinated capital) to the vehicle, and (3) supporting investors by co-investing in MDIs alongside an MDI acquisition vehicle.

**EXAMPLES FROM THE FIELD**

- **CityFirst and Broadway Bank:** A CDFI based in Washington, DC, merged with Broadway Financial, a Black-owned MDI based in Southern California, in August 2020 with combined assets of now more than $1 billion and approximately $850 million in total deposits.

- **Liberty Bank and United Bank:** Liberty Bank, an MDI based in New Orleans, acquired United Bank, increasing its footprint to 17 branches in five states.
• **Gateway First Bank:** Formed from the merger of a mortgage lender and a 100-year-old Native American MDI, Gateway First Bank has greatly expanded homeownership financing for the Oklahoma region with $11.3 billion in mortgages in 2020.

• **Sunstate Bank:** In 2018, the Hispanic MDI acquired Intercontinental Banking, expanding digital and international services to small businesses and minorities in the south Florida region.
STRATEGY 6

Digitizing a Bank

**Description:** Disruptive innovations by the FinTech and tech industries have challenged the traditional banking activities and models, inviting new opportunities for growth in underserved markets and creating uncertainty about the future of these banks. Whether examining underwriting, customer acquisition, advisory services, or the loan products themselves, the make-or-buy decision to incorporate advances in marketplace technology is transforming the banking industry at large. Importantly, COVID-19 has fueled progress in this area: Many customers, who were not digitally comfortable previously, now are and are demanding these services.

The high-touch approach championed by mission banks has benefited from business model transformations as well as added services. CDFI and MDI banks have begun to adopt customer-facing and back-office solutions to serve their constituents better. For some, this looks like identifying the appropriate partners to provide a mobile experience. For others, tailoring services and loan products in real time to the financial health of their customers has created more nimble organizations capable of managing nonperforming assets and higher loan deployment. While the majority of lower asset band MDI and CDFI banks struggle with efficiency, Tier 1 capital investments in core processors and effective participation can remove barriers to digitization and shift the inflection point of total assets and efficiency over purely commercial banks to earlier asset bands.

Hispanic and Black populations are also demonstrably more reliant on their smartphones for internet access, especially where home broadband access is limited. While COVID-19 has left minority and low-income communities sharply feeling the lack of this touchpoint, long-run digital habits are expected to continue to converge toward the mobile experience. Many mission-focused banks have proven apt at driving growth via tech investments. However, developing the digital flexibility necessary to create API interoperability with FinTech collaborators will require more.

**Smart Action:** Partner organizations could consider enabling a massive digitization transformation in MDI and CDFI banks’ front and back-office infrastructure to empower them with the ability to integrate with a wider array of modern solutions. Core processors can effectively partner with best-in-class FinTech solutions providers to eliminate trade-offs in product differentiation and a future-proof core for mission-focused banks.

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focused banks. Differently, tech firms with digital consumer experience offerings can “invest” in mission-focused banks and the markets they serve by ensuring the development of tailored products and support agreements that meet these banks’ needs.

**EXAMPLES FROM THE FIELD**

- **Finastra**: Community bank digital solutions through “bank in a box” technologies aimed at modernization.

- **First Independence Bank**: Detroit-based CDFI bank has invested in Finastra’s suite of digital banking tools to provide a fully digital service to its customers.

- **Quontic**: Trademarked as an “Adaptive Digital Bank,” investing Tier 1 capital over the years to develop APIs and other technology infrastructure necessary to automate as many facets of the business as possible, Quontic has increased its total assets sixfold in four years by successfully extending its offerings digitally nationwide.

- **Gateway First Bank**: By partnering with Black Knight, Gateway First Bank uses the Origination Technology Suite to manage origination costs and risk with artificial intelligence, ultimately delivering customers faster digital experiences.
STRATEGY 7

Local Bank and Big Bank Collaborations

**Description:** Large financial institutions with well-established systems that result in high banking performance (e.g., high-quality assets, greater margins, improved ratios) and customer reach are in an opportune position to mentor MDIs and CDFIs in best practices such as better leverage of capital markets and cash management strategies as MDIs and CDFIs encounter growing pains. Big banks have an increasing mandate on supplier diversity, and leveraging MDIs and CDFIs as supply chain partners can help deliver on that mandate while symbiotically supporting the diversification of revenue streams for MDIs and CDFIs through supply chain collaborations with big banks.

**Smart Action:** Using the US Department of the Treasury’s Mentor-Protégé Program as a framework, large financial institutions can develop a dual-track technical transfer first of capabilities and then supplier diversity that encourages the use of MDIs and CDFIs as suppliers in the banking value chain.

**EXAMPLES FROM THE FIELD**

- **Office of the Comptroller of the Currency’s Project REACH:** Roundtable for Economic Access and Change (REACH) brings together leaders from the banking industry, national civil rights organizations, business, and technology to reduce specific barriers that prevent full, equal, and fair participation in the nation’s economy.

- **Treasury Mentor–Protégé Program:** This program partners big banks with small banks to improve their performance.

- **Citibank’s mentorship:** Citibank participated in the Treasury Mentor–Protégé Program and outlines in a blog post what it looked like on the ground.

**Relevant Stakeholders**

- Large financial institutions
- Institutions with mentorship capacity on banking best practices
- Regulatory agencies that can serve as a platform for collaboration
STRATEGY 8

Efficient Technical Assistance

Description: Prior to recent FinTech innovations, many banking institutions engaged in a higher-touch, although costly, level of customer engagement. Often referred to as “relationship banking,” it allowed customers access to a suite of different services to improve their financial health and inclusion. For a host of reasons, market forces have resulted in far less human technical assistance, especially for small-dollar lending levels. One of the key factors driving costs for MDIs and CDFI lending is the dual need for small-dollar loans and significant customer technical assistance, which is pervasive in many low-income communities. The more hands-on customer service level this cohort of banks provides to their customers, the more cost to the banks.

MDI and CDFI banks could employ more effective methods of delivering high-touch technical assistance for services ranging from small-dollar lending to homeownership so they can have the balanced capacity necessary to scale efforts from endangered levels. Moreover, standardization of data collection and related analysis and market insights should be encouraged for impact accounting and analytics.

Smart Action: For technical assistance to be culturally competent, recognizing how race and income level shape a population’s relationship to financial products and services, organizations can design their programs to include employing minority teachers and specialists to deliver technical assistance (TA) curriculum and partner with local community colleges, nonprofits, and minority business associations. A curriculum could include banking basics, writing a business plan, and accounting.

Moreover, limited public awareness of available technical assistance is a significant challenge, primarily in underbanked communities. Media outlets and influencers in mass media can syndicate financial education programming to raise awareness for these services by partnering with mission-focused banks to delve into the behavioral stigmas capping wealth creation in minority and low- to moderate-income communities. That platform should include data collection to augment smart action and long-term success.

EXAMPLES FROM THE FIELD

- Milken Institute Best Practices for Technical Assistance: In partnership with the US Small Business Administration, this report includes actionable solutions to better technical assistance.

- Operation HOPE Inc.: This economic empowerment program includes a one-on-one coaching service on credit and money management, small business
development, homeownership, youth job skills, and more, all motivated by the need for financial inclusion for low- and moderate-income youth and adults.

- **Our Fair Share**: Sean “Diddy” Combs launched this education platform to help minority business owners apply for Paycheck Protection Program loans.
STRATEGY 9

Modify Opportunity Zone Legislation

**Description:** The Opportunity Zone (OZ) legislation within the 2017 Tax Cuts and Jobs Act (Section 1400Z-2) aims to drive private capital to underserved communities by incentivizing investors through tax benefits. Because Qualified Opportunity Zone businesses cannot have more than 5 percent of their assets in “nonqualified financial property” (as defined in US Code, Title 26, Section 1397C(b), Paragraph 8), CDFIs are excluded from eligibility for Qualified Opportunity Fund investments. While OZ investment would be in the form of equity, investors benefit when the enterprise’s value increases, which incentivizes a more holistic support for wealth transformation in underserved communities.

Many Opportunity Zone investments so far have landed in real estate, which raises concerns of gentrification. OZ investments in MDIs and CDFIs could act as a hedge against displacement, raising wages in small businesses where property values would increase.

**Smart Action:** The federal government should amend the 2017 Tax Cuts and Jobs Act to allow investments in MDIs and CDFIs to qualify for Opportunity Zone benefits to provide long-term capital support and an impact multiplier effect. The amendment should protect minority-ownership status, to the extent that they are also MDIs, from related party rules to comply with Section 308 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). Similar to short-term capital support, this should not trigger Bank Holding Company (BHC) limitations, including investments from other larger financial institutions.

**EXAMPLES FROM THE FIELD**

- **Turbocharging Opportunity Zones:** This *Milken Institute Review* article explores different strategies to improve the Opportunity Zone legislation so that it complements other economic development agents, including MDIs and CDFIs.

- **Jobs and Neighborhood Investment Act:** This bill, sponsored by Senator Warner, revises provisions of MDIs and CDFIs and establishes investment programs and revises provisions related to CDFIs and MDIs.

**Relevant Stakeholders**

- Policymakers looking to provide a network solution to enhance economic impact
STRATEGY 10

Payday TALF

**Description:** More than 12 million Americans engage in payday lending: short-term, high-interest-rate loans that are typically paid on a borrower’s payday that result in $9 billion in loan fees annually, often creating a predatory debt trap for Americans where their cost of living goes up faster than their income.⁹ To reset communities crippled with debt, refinancing those dealing with predatory and payday lending is imperative.

The Term Asset-Backed Securities Loan Facility (TALF), a US Treasury program for increasing credit availability and support for economic activity by facilitating renewed issuance of consumer and small business asset-backed securities at more normal interest rate spread, provides a unique model for how the federal government could help relieve the debt burden of payday lending.

**Smart Action:** Stakeholders could establish a TALF-like program to buy toxic payday loans from the MDIs and CDFIs, which are refinancing the loans. This would enable these regulated banking entities to refinance underbanked borrowers out of usurious payday loans and into more favorable loans, ultimately reintegrating consumers into the formal banking sector. Stakeholders could also provide the upfront liquidity needed for the program. A positive externality is including payday borrowers into the more formal banking sector, transitioning individuals with thin or no credit profile to building a credit profile in the long run.

**EXAMPLES FROM THE FIELD**

- **Troubled Assets Relief Program:** This US Department of the Treasury program is part of the 2008 crisis relief effort that included stimulating lending to small businesses.

- **Term Asset-Backed Securities Loan Facility, CARES Act:** This US Department of the Treasury program is part of the CARES Act that issues loans to banks using asset-backed securities as collateral, increasing banks’ liquidity to issue more credit to customers.

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PHASE 3: REIMAGINE

Before COVID-19, technological innovations in financial products and services were already evolving at a breakneck pace. Now, post-COVID-19, remote and distance products and services will become ubiquitous and the standard for how customers engage with their financial institutions. As a result, the entire banking sector—including MDIs and CDFIs—must be reimagined and, more importantly, over-investment is needed to achieve a healthy degree of access to capital, comparable to the national average, for minority and low-income communities. The strategies in this phase are meant as transformational for the community banking landscape and involve the greatest ambition and strongest impact on bridging the racial wealth gap. Accounting for pathways in which the banking sector is likely transforming is no longer optional when assessing how to increase the socioeconomic impact of MDIs and CDFIs; it is table stakes for the future. Stakeholders must consider the evolving banking environment in order to achieve sustainable impact in communities. Each strategy in this section is predicated on an assumption about the future, which is identified as the "premise."
STRATEGY 11

Local Banking and Big Tech

Premise: If we believe that big technology companies entering the banking space will significantly change the operating environment for banks nationwide, then this strategy is applicable.

Description: Distributed models in the restaurant business have in recent years led to the phenomenon of “ghost kitchens.” Similarly, Big Tech has led the charge into developing marketplaces for banking. This is different from the digitization of banking activities. However, the challenges inherent to transforming the back office into a FinTech API-ready organization are significant. The digitization category of progress is a step behind industry leaders. Customer-facing digital platforms aiming to host multiple participating banks will create a competitive shift in the dynamic of banking and technology.

Additionally, Big Tech has the potential to engender new levels of service for banks on top of impacting their ability to acquire customers, such as expanding offerings to include other customer needs like wealth management services. Assuming policy certainty regarding bank-nonbank regulatory, improved data servicing can go hand-in-hand with developing a bank’s products and services, which can be transformative in terms of profitability. Many banks operating in communities that include immigrant populations may need to provide remittance services (a multibillion-dollar capital flow annually) and even lend to businesses that export internationally. For marketplace tech providers, international expansion is often the most promising growth option. Big Tech could seek MDI and CDFI partners receptive to working in these markets to extend these mission-focused banks’ global growth potential, leveraging financial technology while improving cost efficiencies to best serve international communities.

Smart Action: Big Tech and participating banks could consider market structures, productive offerings, fee structures, and access to customer analytics along with the benefits of promoting access to capital for consumers and increasing customer acquisition and retention for MDIs and CDFIs. Both parties could work with policymakers and regulators to ensure compliance and transparency to clarify and commit to a common mission of preserving consumer protection and boost MDI or CDFI impact.

Relevant Stakeholders

- Marketplace technology providers
- Venture capital
- FinTechs
EXAMPLES FROM THE FIELD

- **Google Pay Partnership with Harbor Bank**: Google has launched its new online payment system and has included MDI Harbor Bank in its pilot partnerships.

- **Greenwood Bank**: Co-founded by Michael "Killer Mike" Render, this bank is still a startup. Although questions remain of its intent as a bank, Greenwood is a branded digital front for back-end banking services.
STRATEGY 12

Shared Services 2.0

Premise: If we believe that the cost of regulatory compliance will continue to burden smaller lenders, then shared banking activities may offer a framework to drive innovation and cost efficiencies, making this strategy applicable.

Description: Similar to the advent of interbank payment systems led by Visa and peer-to-peer platforms such as Zelle, a shared services platform can be leveraged to design, develop, and jointly scale up high-cost and value-add capabilities across multiple banks. Similarly, for MDIs and CDFIs, a jointly managed effort may gain buy-in quickly and result in shared benefits both in utilizing and commercializing the services.

By pooling investments into mission-aligned solution providers, MDI and CDFI banks can lower the costs of systematic challenges within their industry to focus better on differentiated activities. Systemic risks and challenges faced by mission-focused banks align closely with the social sector and may be eligible for philanthropic funding support. Therefore, ideal strategic partnerships would likely take the form of nonprofit entities for maximal leverage.

Smart Action: Stakeholders could create a support corporation that can function as a shared service for all MDIs and CDFIs. Services could include bulk technology buys, maintenance of an open ATM fleet, and cost recovery of technical assistance and financial health for low-income customers.

This strategy creates an opportunity for corporates and philanthropies interested in supporting MDIs and CDFIs to help build an ecosystem of support via a nonprofit structure. This new entity would enhance the capacity of MDI and CDFI banks, allow for increased flow of credit to target communities, and collect data to track indicators for financial and social return.

EXAMPLES FROM THE FIELD

- **Visa:** This leading brand of electronic payment card serves a number of big banks.

- **Zelle:** This banking app serves hundreds of banks and credit unions in the United States.

- **Empowering Communities and Their Banks: Strategies for Scaling Minority Depository Institutions:** This Milken Institute report outlines a shared services model (pages 13 and 14).
STRATEGY 13

Colocation Strategies

**Premise:** If we believe that some form of physical banking infrastructure will remain integral to bank services and that reducing the related fixed cost to the banks is worthwhile, then this strategy is applicable.

**Description:** Research shows that physical bank locations remain essential to advancing the service in communities. Anchor institutions (such as community colleges and HBCUs), big banks’ infrastructure (such as ATMs), and department stores (such as Walmart) across the nation can serve as collocation points of MDI and CDFI services to achieve higher accessibility. Diversified revenue streams for property owners and all the benefits of rising financial inclusion within their respective communities of operation present aligned benefits.

**Smart Action:** In the aftermath of COVID-19, anchor institutions operating in under-banked communities with spare physical capacity could look to partner with mission-focused banks to offer differentiated value to their constituents. The footprint can range from in-store kiosks to modern video-enabled ATM solutions.

**EXAMPLES FROM THE FIELD**

- **WoodForest Partnership with Walmart:** This community banking infrastructure is exclusively located in Walmarts across the country.

- **Chicago’s Ogden Commons:** A PNC-qualified Opportunity Zone fund development is bringing a Wintrust Bank branch into the same structure as affordable housing units and health services.

- **CitiBank partnership with MDIs:** Citi® ATM Community Network provides surcharge-free ATM access to partner credit union and minority-owned bank customers.

- **POPi/o and NCR:** This partnership brings together a video banking solution provider that has grown by multiples throughout the pandemic on community banking contracts and a producer of interactive teller machines used by banks with shrinking physical footprints.

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STRATEGY 14

Community Reinvestment Act for All

**Premise:** If we believe that various industries that benefited from the "public safety net" provided by the 2020 CARES Act are responsible for addressing socioeconomic inequalities experienced by minority and low-income communities, then this strategy is applicable.

**Description:** There is a growing debate on the need for various industries to step in and do more for their stakeholders, especially because the limited level of public goods, such as access to broadband and health care (which are dependent on geography), resulting in two Americas: the haves and have-nots. Similar to how financial services firms had to expand the financial inclusion of vulnerable populations through the 1977 Community Reinvestment Act (CRA), as a result of the "public safety net" afforded to these financial institutions (e.g., access to FDIC insurance and Fed overnight window), the COVID-19-induced crisis showed nearly all firms needed taxpayer-funded assistance. Accordingly, should all firms (especially those with products and services critical to socioeconomic disparities) be incentivized to engage in "CRA-like" support of low-income communities with increased access, affordability, and availability of their products or services? Effectively, CRA-like policy can be developed for a broad set of industries (telecommunication, health care, education, etc.) to address socioeconomic disparities in urban and rural minority and low-income communities. Moreover, given the importance of access to capital in creating economic prosperity, there could be a need for linking "CRA for all" and access to capital. As CRA defines how banks get credit (lending, investing, or services), corporates could get credit for aligning their products and services to augment access to credit via MDIs and CDFIs.

For example, for the broadband industry, it's become evident, from telemedicine to smart grids, that the value of broadband expansion has captured the attention and activity of investors and policymakers. Similarly, as mobile banking solution providers enter the market, regional banks have begun adopting the technology as a means of expanding their high-touch approach. MDI and CDFI banks often employ analog tactics to further financial education and inclusion, a disparity that tracks closely with access to broadband along poverty lines. MDI and CDFI banks need broadband infrastructure to reach these communities through cost-effective mobile banking solutions. Investors seeking to further access to broadband could consider MDI and CDFI banks as unique partners due to their experience bringing the underbanked into the fold. Investors should make sure to capture explicitly the value of mobile banking solutions as a means to reach these communities cost-effectively.

**Relevant Stakeholders**
- Federal, state, and local policymakers
- Industry leaders
- Entities interested in integrating siloed industries to meet common economic development goals
**Smart Action:** Policymakers could consider identifying critical industries that are foundational and develop a framework for encouraging (through both policy and regulations) their linkage with MDIs and CDFIs to promote access to capital for disadvantaged communities. Given the variety of ways banks can get CRA credit, corporations mandated in such a “CRA for all” policy could be encouraged to provide support for MDIs and CDFIs to leverage their platforms. Strategic industries can amplify each other’s efforts to facilitate access to capital and benefit other public welfare.

**EXAMPLES FROM THE FIELD**

- **The Vanishing American Dream:** This book, authored by former US Comptroller of Currency Gene Ludwig (under President Bill Clinton), focuses on the economic realities of low- and middle-income Americans.

- **Conscious Capitalism:** This book on reimagining capitalism that includes stakeholder integration is authored by Whole Foods co-founder John Mackey and Conscious Capitalism Inc. co-founder Raj Sisodia.

- **Business Roundtable statement:** The business group redefines the purpose of a corporation to promote an economy that serves all Americans through a commitment to stakeholders.

- **State-led expansion of CRA:** Several states have begun to enact their own oversight to ensure equitable investment in underserved communities; Illinois became the latest addition by signing the Illinois Community Reinvestment Act into law.
CONSIDERATIONS FOR A SOCIAL IMPACT FRAMEWORK

A plethora of agents is making socioeconomic-focused investments to achieve economic justice for all Americans, especially minorities, stemming from the realization of inequities highlighted by the events of 2020. Key to this is a deeper understanding of how certain activities achieve actual social outcomes (e.g., resilience and economic mobility) and not just outputs from activities (e.g., number of businesses banked). In this context, we consider the desired outcomes to be the increased ability of individuals, households, and their communities to withstand sudden socioeconomic shocks (resilience) and climb the socioeconomic ladder sustainably (economic mobility).

Social impact monitoring and evaluation have evolved considerably in recent years. Efforts by stakeholders such as the CDFI Fund, the Sustainability Accounting Standards Board (SASB), Operating Principals for Impact Management (OPIM), and many others have done much to advance the landscape. Focusing on nine principles, the OPIM is a framework for designing and implementing impact management systems, ensuring that impact considerations are integrated throughout the investment lifecycle. SASB standards include a framework that allows investors to assess sustainability information across sectors and have 77 industry-specific standards. More particular to community lending reporting, the CDFI Fund developed the Community Investment Impact System (CIIS), a web-based data collection system for CDFIs to submit institutional- and transaction-level reports as a part of their required compliance. This system has now collected 14 years of data on CDFIs’ operation, financial status, and impact in their communities. CIIS reporting includes 203 variables at the institutional level and 50 variables at the transaction level.

CIIS was discontinued in 2017 and replaced by the Awards Management and Information System Compliance and Reporting system to streamline gatherable information. In a similar vein of community development through lending, Section 1071 of the Dodd-Frank Wall Street Reform and Consumer Protection Act amended the Equal Credit Opportunity Act to facilitate fair lending and better identify community development needs. Its implementation requires the compilation and reporting of specific data on business loans to small businesses. The CFPB is currently resolving the legal and policy issues that come with its implementation.
Despite the great strides made, a key question remains: What is the best way to ensure individual, household, and community resilience and socioeconomic mobility? As the US heads into an unprecedented period of post-COVID recovery during high levels of national debt, ensuring efficient, effective interventions are supported will be critical in a period of potentially scarce resources.

Unfortunately, sustainable outcomes are usually a result of multiple causes. Providing access to credit is only part of the solution. To achieve socioeconomic mobility, increased access to capital must be combined with enhanced access to health care, education, and digital networks, among other things. Research shows that intergenerational mobility and resilient outcomes involve multiple variables grouped at the local community level, making holistic and place-based interventions an important strategy. According to Raj Chetty’s research, which he based on economic analysis of tax returns, while the average income of a neighborhood might improve, the original residents of that neighborhood did not necessarily have improved lives. Consequently, the stakeholders highlighted in this report must analyze the indicators to measure the impact and ultimate outcome of any particular strategy. Benchmarks in jobs and income creation (commonly referenced) are necessary, as well as a timeline to achieve them, resulting in a defined “resilience” of a borrower and a community (often overlooked). Failure to meet benchmarks should lead to a reevaluation of the interventions, and the extra monitoring should be relevant and easy to implement. The challenges of implementing the Dodd-Frank Act illustrate the necessity of clear sets of metrics that are easily trackable. Minimizing compliance costs will encourage institutions to participate in the monitoring and evaluation.

To develop a path forward, stakeholders should consider three steps:

1. Clearly define the end outcome desired,
2. Develop a Theory of Change with relevant metrics and threshold outputs that drive toward the desired outcomes, and
3. Consider roles and responsibilities for key institutions (e.g., what banks can/should do versus what philanthropy and public sector should).

1) Clearly define the desired outcome

Partnering with MDI and CDFI banks is ultimately about building capacity within institutions well-positioned to help finance underserved individuals’, households’, and communities’ resilience. Outcomes at the individual and household level could entail the ability to withstand socioeconomic shocks by improving economic mobility

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and, thus, intergenerational wealth creation. Outcomes at the community level could entail the ability of a specific demographic to withstand socioeconomic shocks by improving the target population’s economic wealth mobility by race, gender, and/or location. Through clearly defined outcomes (e.g., economic mobility of 10,000 minority households or all the residents of a specific at-risk community/ geography), financial products and services targeting job creation and/or homeownership can be building blocks that allow these mission-focused financial institutions and their partners to invest directly in sustainable impact.

2) Develop a Theory of Change with relevant metrics and output benchmarks that drive toward the desired outcomes

In economic development parlance, a Theory of Change is essentially a comprehensive description and illustration of how and why a desired outcome is expected to happen in a particular context. By first defining the long-term goals and outcomes and mapping necessary preconditions and causes and then tracking them with relevant metrics, stakeholders can ensure partnerships with MDIs and CDFIs build to ultimate goals.

Critical to the leap from activities (number of small business loans approved) to quantifiable outputs (number of jobs created) to true outcomes (number or percentage of the population with improved resilience) requires an understanding of the threshold of output (magnitude, quality, sustainability of jobs created) needed to induce outcomes (individual, household, and/or community resilience). Metrics should consider transaction-level and institutional-level variables and be evaluated longitudinally to understand their compounding effects on outputs more accurately. Transaction-level data could encompass loan-to-value ratios, portfolio by line of business, and share of products and services dedicated to key target markets. Institutional-level data (i.e., of the financial institution) could cover profiles related to race, geography, staffing level, and financial status of the borrower served, services and training provided, the quality of internal incentives to grow tailored financial and nonfinancial products and services, and the quality of internal processes for socioeconomic impact-related investments in target markets.

Also, to bridge the gap between outputs and outcomes, there is a need for a progressive and balanced portfolio of initiatives that reflect sustainable business strategies for long-term target market development. Central to impact is the sustainability of outcomes. Thus, effective evaluation requires rigorous monitoring and a clear assessment of outputs using longitudinal metrics.
2A) Improved Banking Products as Outputs

For any financial institution to claim improvement of its banking products and services for a particular customer, it must demonstrate enhanced accessibility, affordability, and availability for that particular customer.

**Accessibility:** Are the products and services within reach of the target population? If features are only accessible to specific income strata or geography, or via a marketing channel infrequently engaged with a particular population, it is less accessible. Increasing access for untapped markets supports not only resilient outcomes but also broad economic growth, which in turn promotes inclusiveness of jobs.\(^\text{12}\)

**Affordability:** Are the products or services sustainably priced for the target population? If certain products are initially low priced to entice borrowers but escalate due to exogenous and frequent circumstances and ultimately become a burden, they are less affordable.

**Availability:** Are those products and services present when target populations need them? If a bank lowers credit limits to credit cards held by LMI customers in the middle of a force majeure event the very moment LMI individuals would need them, then their availability is reduced.

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Each of these conditions of an improved banking product and service will require an understanding of the collective threshold needed to reach the ultimate outcomes and a set of relevant metrics to track them.

2B) Improved Local Economy as an Output

Sustainable mission-focused banks find a virtuous cycle where responsible stewardship of community financial markets allows them to influence local banking industry drivers such as consumer spending, unemployment, and population growth. To drive improvements in local economies and labor market conditions through MDI and CDFI strategy, the activity of products and services needs to be monitored and evaluated. Relevant metrics include the number of people and businesses banked, the amount of job creation in growth markets, the amount of income created, and the scale of part-time versus full-time job creation. Job creation in growth markets reflects whether banks effectively develop and promote products and services in key industries that can reliably grow future-proofed jobs within a community. Conceptually, if an agricultural community reveals high pay and progression potential within investments in solar energy production on farmland, banks can grow practices with tailored business lines.

Similarly, income data indicate whether banks effectively develop and promote products and services that support industries that have healthy local labor markets. Longitudinal tracking of individual customers within the data can control for exogenous factors, such as gentrification. Part-time versus full-time job creation can show if portfolio and transaction-level decisions have added to job security and safety nets typically offered with permanent jobs. Suppose full-time equivalence growth is stagnant relative to workforce population growth. In that case, the mechanisms traditionally built into salaried employment to mitigate systemic risks will be weakened at the labor market level. Effective partnerships within communities will inform the current state and, therefore, the threshold of balanced output progress for outcomes. As seen throughout, transactional, institutional, and longitudinal metrics will holistically describe these outputs. The Milken Institute Community Explorer provides insights into identifying community-specific benchmarks for behavioral, demographic, economic, and social variables, allowing for holistic and community-specific monitoring of the initiatives’ impact.
3) Consider roles and responsibilities for key institutions (e.g., what banks can/should do versus what philanthropy and public sector should)

Taken together, a balanced portfolio of transactional, institutional, and longitudinal level metrics with an explicit focus on the outputs listed above will allow stakeholders to effectively leverage the strengths of MDI and CDFI banks towards the ultimate goal of individual, household, and community resilience. Effective community partnerships are pivotal, and different stakeholders may be better able to collect and analyze some segments and not others. Dodd-Frank Section 1071 regulations, existing CDFI Fund and CRA requirements, standards created by organizations like SASB, the National Community Investment Fund, and the Global Impact Investing Network are collecting a wealth of relevant information for the assessment discussed here. This information can be used to widen the aperture of relevant data to distill a set of key metrics to account for impact over time.

Moreover, federal, state, local, and nongovernmental partners play critical roles in addressing inefficient markets through matching funds, supportive policy, and better-quality data. The public sector bears some responsibility for remediating inefficiencies at the collection level. Early opposition to Dodd-Frank Section 1071 centered on whether banks collect data versus other stakeholders on their behalf, as well as complications around 40 different definitions of small business in the federal government being costly. To have both an efficient and cost-effective approach, stakeholders should agree on a uniform set of metrics to collaboratively understand (i) the impact of activities and (ii) which stakeholder will best design the framework, implement it, and assess its results.
CONCLUSION

In 2020, there was a realization about the importance of racial equity and the stark vulnerabilities in low-income communities, resulting in billions of dollars in commitments to bridge the racial wealth gap and to focus on better serving the underserved. In 2021 and beyond, leaders will need to follow through with action and a fresh eye towards both implementing sound strategies and creating a future with equitable access to the American Dream. A lack of access to capital is a lack of access to the American Dream.

MDIs and CDFIs can be that bridge. However, to realize the full potential of these mission-focused banks to bolster equitable access to the American Dream, three phases of potential collaboration with partner stakeholders have been identified. Phase 1 focuses on relieving balance sheet needs for capital to improve core functioning. Phase 2 highlights ways to restore access to capital in minority and low-income communities at parity with the national average via stakeholder partnerships with MDIs and CDFIs to scale up and target key impediments. And phase 3 offers a mental reset button and reimagines the role and operations of the banking sector in the future and how stakeholder partnerships can play a part. The accelerated advancement and adoption of technology, the rapid and extensive government deployment of capital, and other system disruptions spurred by COVID-19 reveal that a transformed banking sector is on the horizon. This phase aims to ensure that developments in the banking system are accounted for in efforts to scale MDIs' and CDFIs' impact. Phase 3 is integral to the success of phases 1 and 2 because without considering the transformations afoot and networked solutions, relieving and restoring will not be enough in the long term.

These strategies should be supplemented by a social impact return strategy that emphasizes the outputs that promote an ultimate outcome of borrower and community resilience. Partners should consider the multiplier effects of the stronger MDIs and CDFIs they support, affecting improved banking of the underbanked, increased income levels for low-income individuals, net positive additional jobs, reduced displacement, and decreased unemployment of relevant communities that MDIs and CDFIs serve. Moreover, better understanding one's customers and markets could have other positive commercial effects for stakeholders, which justifies the impact strategy as a dual social and commercial multiplier.

The purpose of this report is to guide entities looking to improve access to capital and wealth-building in minority and low-income communities through MDI and CDFI banks. Each of these strategies should be treated as a thought-starter requiring customization to particular partners' goals. From repairing the balance sheet to transforming the banking system, unlocking MDIs' and CDFIs' immense unrealized potential requires thoughtful, intentional actions that continue beyond the COVID-19 pandemic and post-George Floyd moment we are in.
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