Another Capital Infusion Program: The Community Development Capital Initiative

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Research Question and Results

- Research Question

  - During the Great Recession, could MBIs qualify for the Community Development Capital Initiative Program (CDCI)? Are there bank specific or macroeconomic factors that correspond with being accepted into the CDCI program?

  - Is there a difference in the growth in small business lending between MBIs and CDCI banks? Are there bank specific or macroeconomic factors that influence the growth in small business lending?

Capital Infusion Programs During the Great Recession

- Capital Purchase Program (CPP)
  - The Capital Purchase Program (CPP) was launched to stabilize the financial system by providing tier 1 capital to help absorb losses and to stimulate the flow of credit to businesses and consumers.
  - Treasury initially committed $250 billion to the CPP. In the end, the Treasury had invested approximately $205 billion under the CPP.
    - Treasury provided capital to 707 financial institutions in 48 states, including more than 450 small and community banks and 22 certified community development financial institutions (CDFIs).
  - Participating banks pay the Treasury a five percent dividend on preferred shares for the first five years and a nine percent rate thereafter.

Capital Infusion Programs During the Great Recession

- Small Business Lending Fund (SBLF)
  - Enacted into law as part of the Small Business Jobs Act. The Small Business Lending Fund (SBLF) was a $30 billion fund to encourage small businesses to qualified community banks with assets of less than $10 billion.
  - Treasury invested over $4.0 billion in 332 institutions.
    - Investments include $3.9 billion in 281 community banks and $104 million in 51 CDLFs. Collectively, these institutions operate in over 3,000 locations across 47 states and the District of Columbia.
  - The initial dividend rate is at most 5%. The dividend rate on SBLF funding declines as a participating community bank increases its lending to small businesses. If lending does not increase in the first two years, however, the rate will increase to 7%. After 4.5 years, the rate will increase to 9%.

Capital Infusion Programs During the Great Recession

- Community Development Capital Initiative (CDCI)
  - Treasury created the Community Development Capital Initiative (CDCI) on February 3, 2010 to help viable certified CDFIs and the communities they serve cope with effects of the financial crisis.
    - CDFIs focus on providing financial services to low- and moderate-income, minority, and other underserved communities.
  - Treasury completed funding through this program in September 2010. The total investment was $570 million for 84 institutions
  - CDFI banks, thrifts and credit unions pay an initial dividend or interest rate of 2 percent and the dividend rate will increase to 9 percent after eight years.

Data

- This study analyzes two groups of banking institutions for the 1st quarter of 2010:
  - All minority banking institutions (MBIs)
  - All participating banks in the Community Development Capital Initiative Program (CDCI banks)
- Variables used in the analysis:
  - Bank specific data
    - Asset size, capital ratio, asset quality measures, age, return on assets, percentage of liquidity and percentage of small business lending
  - Macroeconomic data (state level)
    - Growth rate in personal income, growth rate in business bankruptcies, growth rate in private sector jobs and growth rate in unemployment

Selection Model Results

- Is there a difference between CDCI banks and MBIs?
  - CDCI banks are larger in size
  - CDCI banks have been operating longer
  - CDCI banks have lower loan losses as a percentage of assets
- In summary, the financial health of MBIs and the economic environment where MBIs operate was very similar to CDCI banks
  - On average, MBIs would have been eligible to participate in the CDCI program

Small Business Lending Model

- Is there a difference in the small business lending behavior between CDCI banks and MBIs?
  - CDCI banks experience stronger growth in small business loans 2009-2016
  - Banks in the sample experience stronger growth in small business loans if they have:
    - Stronger asset quality measures
    - Higher capital ratio
    - Less profitable
    - Higher liquidity ratio
    - More experienced small business lender

Summary and Implications

- Summary of the results:
  - MBIs that were eligible were likely to receive funding under the CDCI program.
  - CDCI banks experienced stronger growth in small business lending relative to MBIs
- Implications:
  - Given the economic environment, MBIs would have gained access to low cost capital that was not tied to any lending standards.
    - Why not participate?
      - Not a certified CDFI
        - Can participate in other government programs
      - Strong asset quality
      - Lack of demand for credit in the service area