NC3 NATIONAL COALITION for COMMUNITY CAPITAL

Community Investment Fund – Financial Modeling Guidelines

Overview

This Guide lays out the fundamental financial choices that fund designers will need to make in order to create a robust, actionable financial model and forecast. Every decision reached during the design phase has bottom line implications for the fund itself and more importantly, for the community it seeks to serve.

For example, if you want to offer investors an attractive rate of return *and* you anticipate that your fund will make many small investments (e.g. $10k-$50k), your financial model might show the fund operating at a deficit, at least for the first several years. In such a case, you'll need to decide whether to modify the assumptions and expectations in your model, or perhaps seek philanthropic partners to finance early operating costs.

There are no easy answers. With that said, a financial model does not need to be tremendously detailed or complex to be useful. We provide a snapshot of a simple financial model below. Alternatively, the Sample CIF Financial Model on the NC3 website demonstrates the level of detail you could include and is based on an existing community investment fund's financial model. This downloadable Excel file is offered for illustration purposes, but please feel free to use it as a starting point and customize to meet your fund's particular needs.

NC3's goal in sharing these tools is to help streamline the design process and to facilitate creation of community investment funds to launch, scale, and succeed. If you need assistance with financial modeling, contact NC3 (nc3@comcap.us) for referrals to financial experts and consultants.

Components of a Financial Model: Revenues

It's helpful to think of your CIF as a business in which your "product" is the portfolio of investments made into local businesses, and the interest/dividends/principal repayment on those investments are your "sales revenue."

If you've completed the "Calculator" and "Impact Reality Check" worksheets of NC3's Fund Calculator Tool, you've taken the first steps toward modeling out your "sales projections" i.e. your Return on Investment (ROI) model that will forecast the timing and amount of financial returns you expect investments to generate.

Exhibit 1 below is a simple income statement from the Boston Impact Initiative (BII) Fund that shows a variety of revenue sources. Following are definitions of BII's revenue sources and other types of revenue:

- *Investment Income:* This is the earned income or ROI generated from your portfolio's investments.
- *Interest Income:* It's likely to take time to fully deploy your fund into investment opportunities, so consider parking your fund in an interest-bearing account to earn some income in the meantime. If it's with a locally-owned bank or credit union, you'll be delivering on your fund's mission for local investment simply by virtue of banking with another local capital provider.
- *Origination Fees:* Traditional lenders often generate fees on loan applications to offset some of the costs of administering a loan. Of course, the goal of most community capital providers is to keep investee costs down, so you might choose to omit origination fees altogether. However, there is some benefit to requiring a potential investee to put some "skin in the game" to encourage effective participation.
- *Grant Support:* Grant income, especially in the early stages of launching a fund, is vitally important to help cover the costs of initial infrastructure building as well as the higher transaction costs associated with making investments into businesses that are less experienced with raising capital.
- *Donor Support:* Some funds ask investors to consider a philanthropic contribution alongside their investment to address the costs mentioned above in Grant Support.
- *Carry Fees:* Investors could be asked to support some of the on-going overhead fees not covered by philanthropy, as in a traditional VC fund model.
- *Other Earned Revenue:* In addition to revenue from Speaking Engagements and Shared Services Agreements (as shown in the BII example), your fund could generate fees from Events, Consulting Projects, or other activities.

EXHIBIT 1: Boston Impact Initiative Fund Income Statement

BII Fund Budget				
REVENUE		**2018**		**2019**
Interest Income	$	56,097	$	165,254
Investment Income	$	6,059	$	17,700
Grant Income	$	400,000	$	400,000
Speaking Engagement Income	$	25,000	$	40,000
Shared Services Agreement	$	50,000	$	50,000
TOTAL REVENUE	**$**	**537,156**	**$**	**672,954**
EXPENSES				
Fundraising	$	2,500	$	2,500
Grants	$	-	$	-
Interest	$	37,914	$	116,363
Investment Management	$	72,500	$	100,000
Overhead	$	66,600	$	64,800
Professional Fees	$	17,813	$	47,313
Salaries	$	280,000	$	310,000
TOTAL EXPENSES	**$**	**477,327**	**$**	**640,976**
PROFIT (LOSS)	**$**	**59,829**	**$**	**31,978**

Components of the Financial Statement: Expenses

NC3's Operating Structure Checklist contains a comprehensive list of the types of operating costs you can expect to incur. We strongly recommend your team spend significant time with the Operating Structure Checklist to think through all aspects of managing a fund. This will mitigate the chance of being negatively surprised by unexpected costs as you get up and running. If possible, include your financial expert in the exercise so they can start thinking about the timing and scope of these costs to create a more accurate forecast.

Other Cost Considerations

Local Management vs. Outsourcing: Depending on the existing resources and infrastructure within your community, and the size/complexity of your fund, you may decide to outsource some aspects of fund management or you could manage your fund entirely with your own proprietary staff.

While it may be costlier in the near term to create a new LLC or nonprofit organization to launch and manage your fund, this model does offer the most local control and oversight. Less expensive models might rely on service contracts with a local CDFI, accounting agency, or impact investment firm to manage some or all aspects of investor relations management, investee underwriting, and other "back office" needs. You might also decide to start by outsourcing some management functions and then bring them in-house over time as your local fund management team gains experience and confidence.

There are many ways to approach fund management and many existing case studies to follow as role models. Contact NC3 (nc3@comcap.us) for introductions and referrals.

Technical Assistance: Some funds choose to offer technical assistance (TA) such as bookkeeping, marketing/social media management, or human resource development to their investees. This can be seen as a kind of insurance policy for your portfolio as you help develop knowledgeable, effective business leaders whose success will translate into ROI for your fund.

The downside of offering TA is the cost. Especially for early stage community investment funds, TA costs might end up being a large percentage of your fund's total expense. This is where philanthropic partners might be able to provide some relief to your bottom line through grants or donations. Alternatively, you might be able to partner with existing TA providers in your region to outsource TA and reduce your cost. Regional Small Business Development Centers, CDFIs, incubators, and other organizations in your entrepreneurial ecosystem are a good place to start for TA partnerships.