A Survey of the Financial Situation of the Massachusetts CDC Sector

Prepared for

The Community Development Innovation Forum

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The CDC Sector Is An Important Engine for the Development and Support of Healthy Communities

The strengths that the CDC Sector brings to the development and support of healthy communities are widely recognized and include:

- local control for neighborhood improvement
- entrepreneurial responses to local social challenges
- a history of collaborations to achieve enhanced positive community impact
- capacity to identify and nurture existing skills of residents to build community leadership and revitalization.

The CDC Sector Faces Challenges on a Number of Fronts

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As is the case with community development organizations across the country and notwithstanding the strengths identified on the previous page, the CDC Sector is facing significant challenges.

The principal drivers of these challenges are:

- the dramatic changes in the business fundamentals of the CDC Sector,
- CDC business models that are struggling to find effective ways to adapt to these changes,
- systemic, structural constraints on the business practices and competiveness of CDCs and
- a recession that has hastened and intensified some pre-existing vulnerabilities in the CDC Sector's financial durability and sustainability.

Summary of Survey Findings and Recommendations

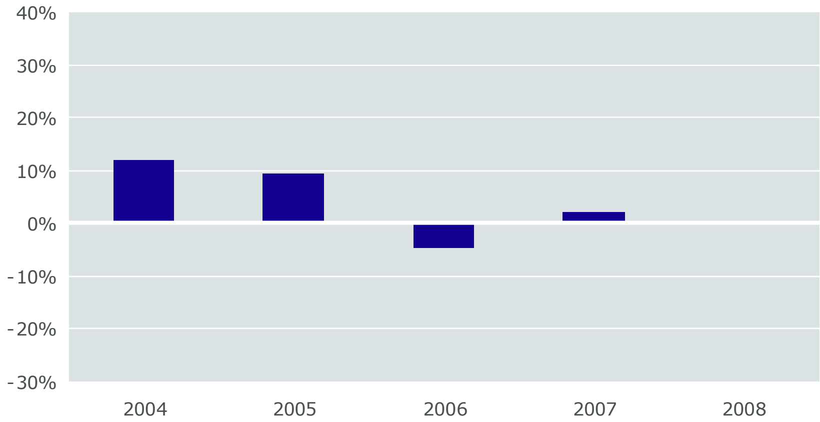
- More consistent financial reporting practices providing visibility into the true operating performance of the CDC Sector is needed
- Financial reporting inconsistencies can be a barrier to desirable voluntary collaborations
- Financial reporting inconsistencies aside, trend data for the CDC Sector are down for durability and up for risk
- Despite cost cutting, decreases in revenue from multiple sources are depleting CDC Sector cash
- Low absolute levels and steady decreases in liquidity = a CDC Sector on a comprehensive drive for cash

Summary of Survey Findings and Recommendations

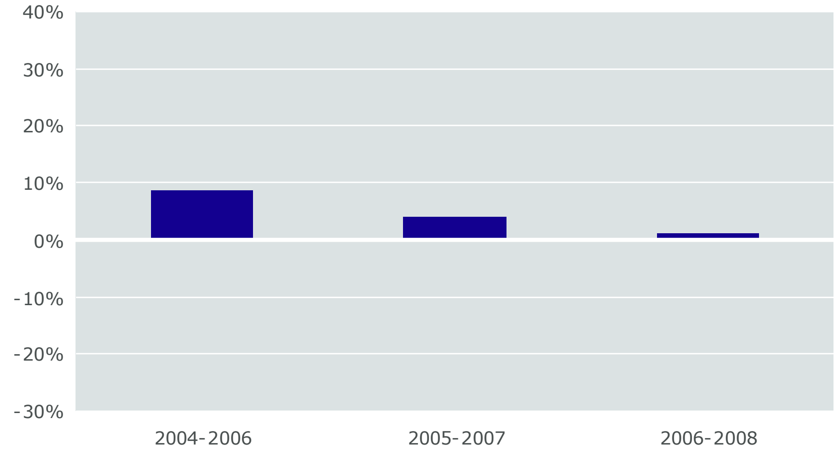
- Further investigation into some conflicting data on CDC Sector liquidity is recommended
- Historical levels of CDC Sector liquidity may have been lower than thought
- With some exceptions, the financial situation among CDCs by budget size and business model varies modestly
- Small CDCs appear somewhat more vulnerable to the economic and competitive forces buffeting the CDC Sector

Average Pre-depreciation Profitability for the CDC Sector Has Trended Down

All CDCs (annual)

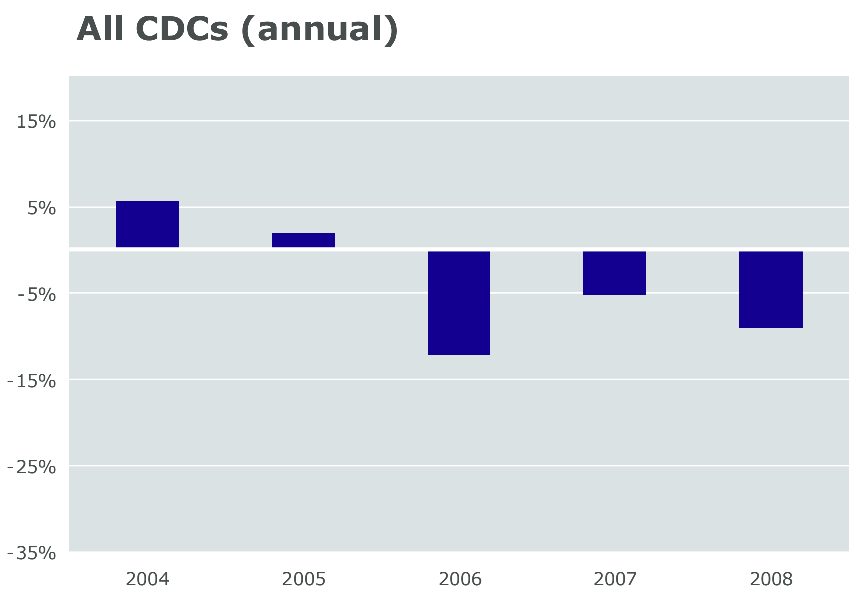


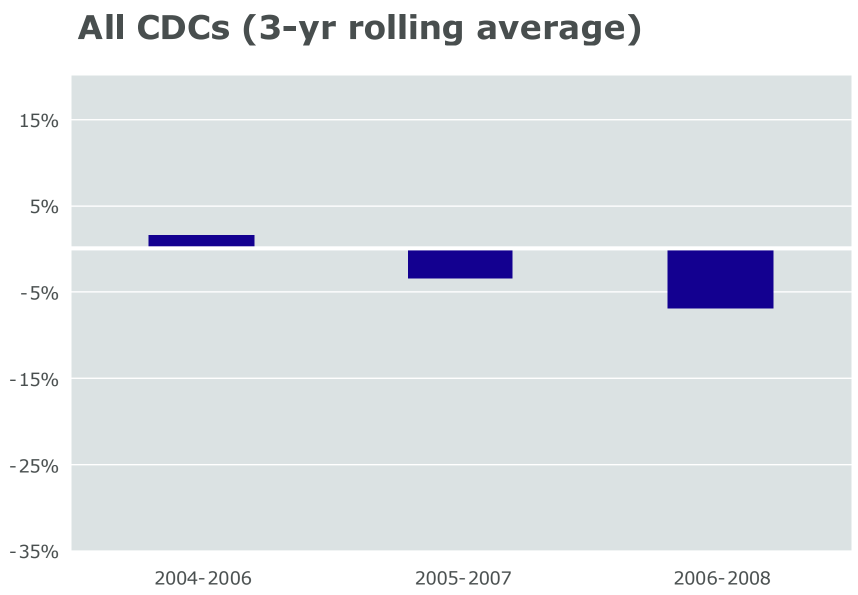
All CDCs (3-yr rolling average)



- 56% of the CDC Sector reported pre-depreciation profitability of 5% of revenues or higher in 2008
- Conversely, 32% of the CDC Sector reported negative pre-depreciation profitability (deficits) in 2008

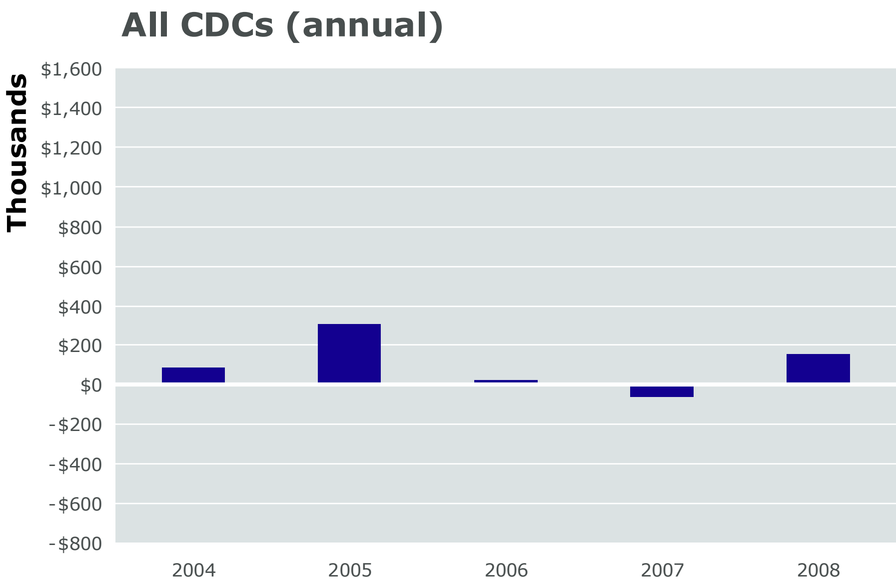
Average Post-depreciation Profitability Has Also Trended Down Significantly and Has Indicated Deficits for the Past Three Years

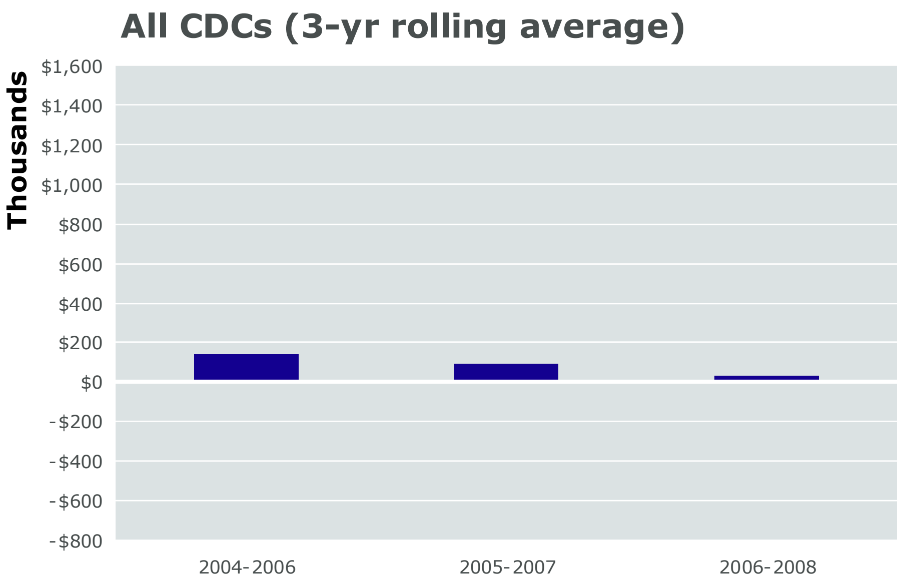




- 68% of the CDC Sector reported post-depreciation deficits in 2008
- Small CDCs comprised the largest percentage of CDCs in this deficit position (47%)

Prior to a Positive Change in 2008, Annual Changes in Unrestricted Net Assets for the CDC Sector Had Been Decreasing for 2 Years





- In 2008, 52% of the CDC Sector reported a decrease (negative change) in net assets
- Small CDCs comprised the largest percentage of CDCs in this negative change in net assets position (69%)

Average Debt Ratio Indicates a Steady Increase in Leverage Since 2005

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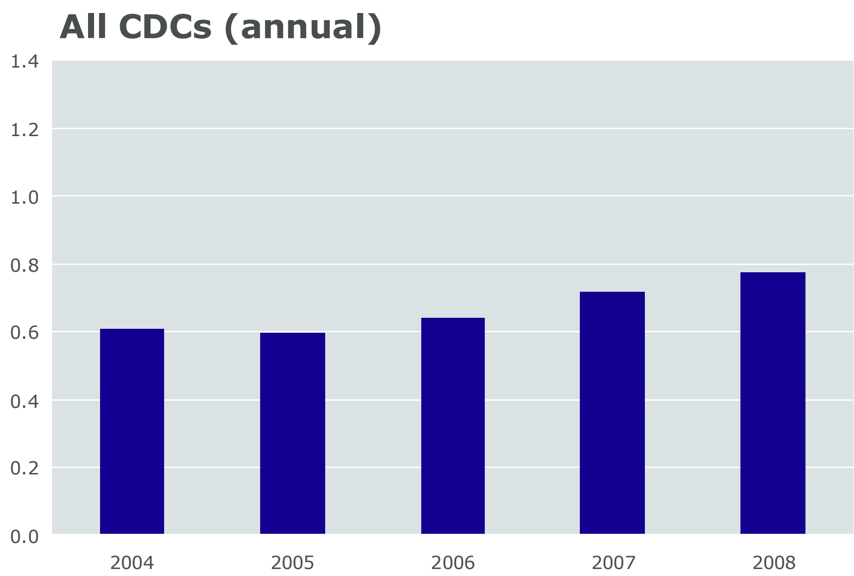
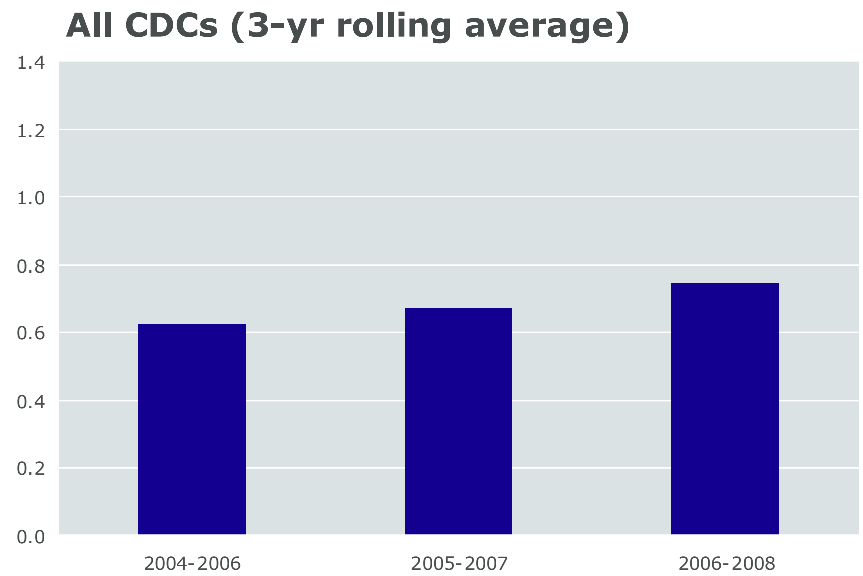
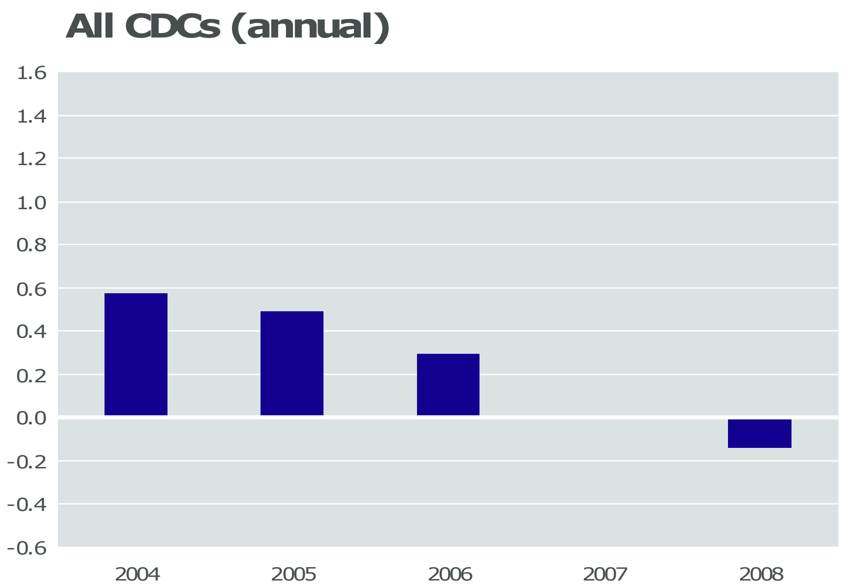
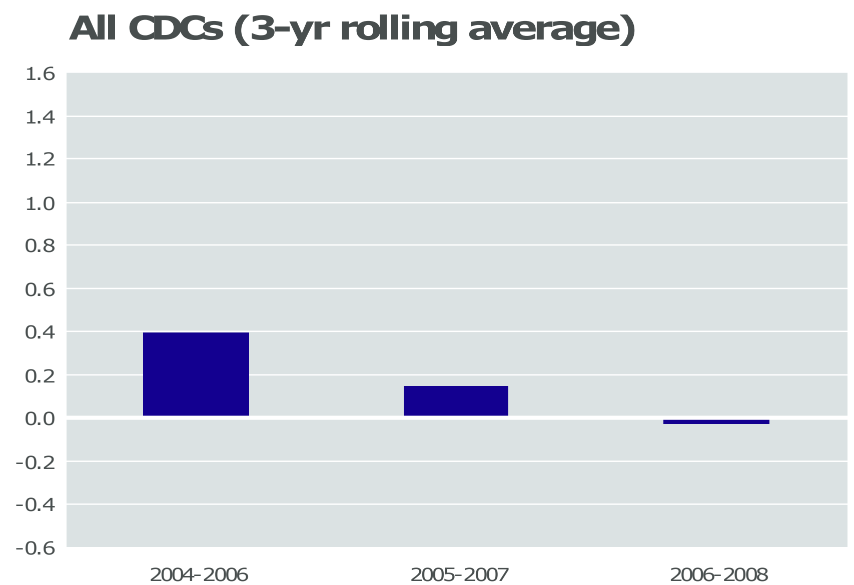




- Not withstanding this trend of increasing leverage, 72% of the CDC Sector still managed to achieve a Debt Ratio under 1.0 in 2008

Average Debt Coverage in the CDC Sector Has Trended Down Markedly and is Now Negative

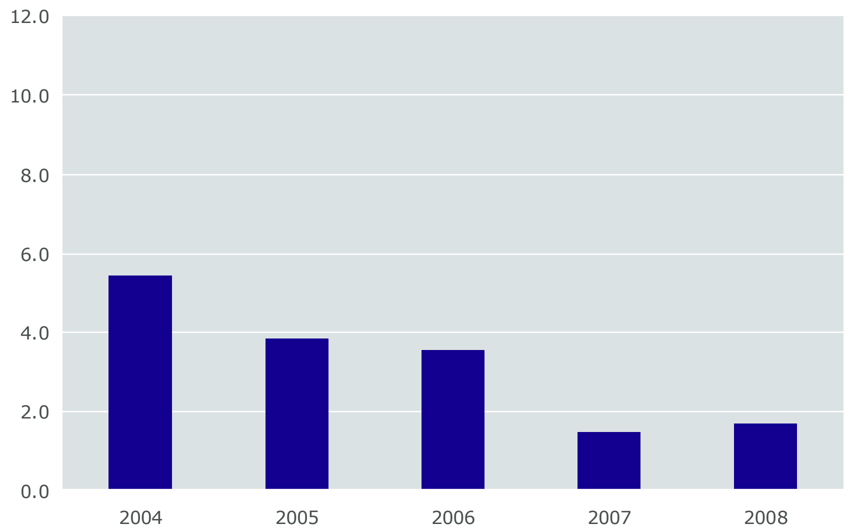




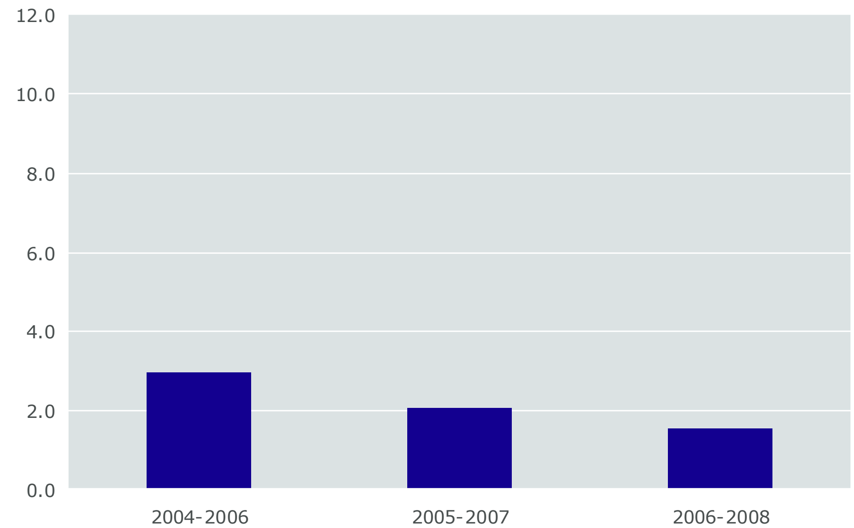
- For 76% of the CDC Sector in 2008, unrestricted net asset coverage of debt was negative or thin (0.00 to 0.05)
- 24% of the CDCs had negative Debt Coverage in 2008

Although the Current Ratio Has Trended Down, On Average for the CDC Sector it is Well Above 1.0X

Average Current Ratio (annual) All CDCs

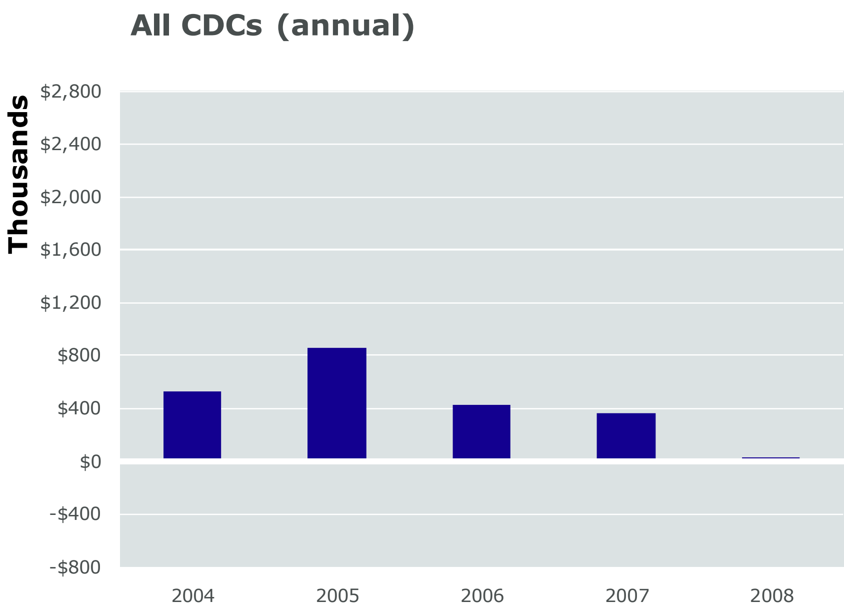


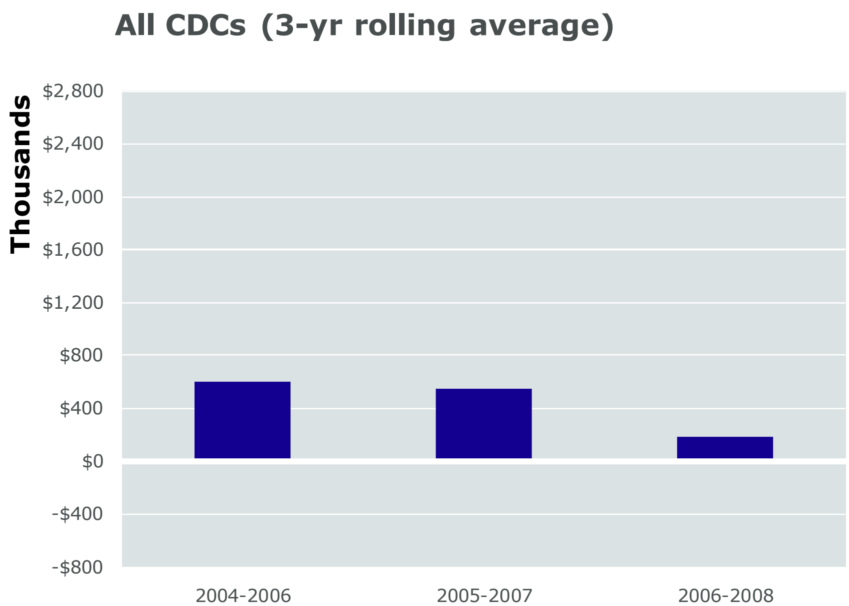
Average Current Ratio (3-yr rolling average) All CDCs



- At 1.19X, the median Current Ratio for the CDC Sector in 2008 is lower than the Sector average of 1.71X
- 40% of the CDC Sector had a Current Ratio below 1.0X in 2008.

Working Capital for the CDC Sector as a Whole Was Down to Almost Zero at the End of 2008





- In 2008, negative Working Capital (current assets less current liabilities) was reported by 10 CDCs, i.e., 40% of the CDC Sector

Levels of Average Days of Cash Are Not Consistent With Other Indicators – A More Detailed View Indicates Growing Stress

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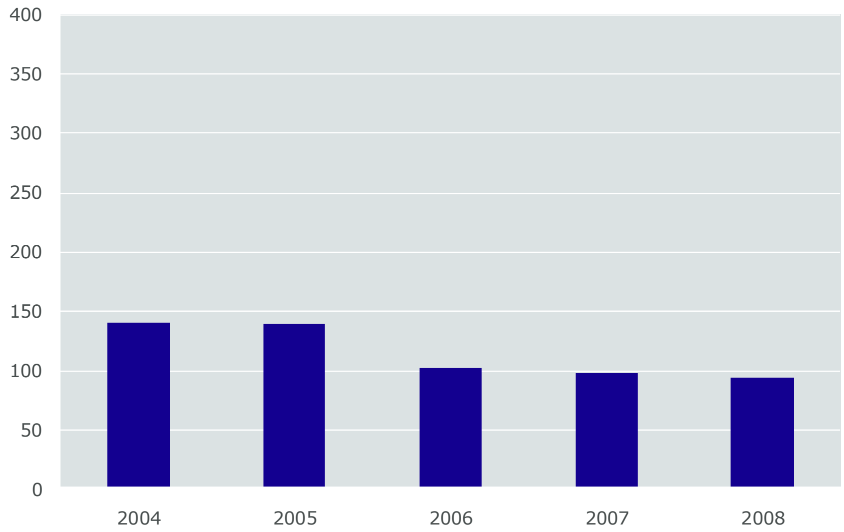
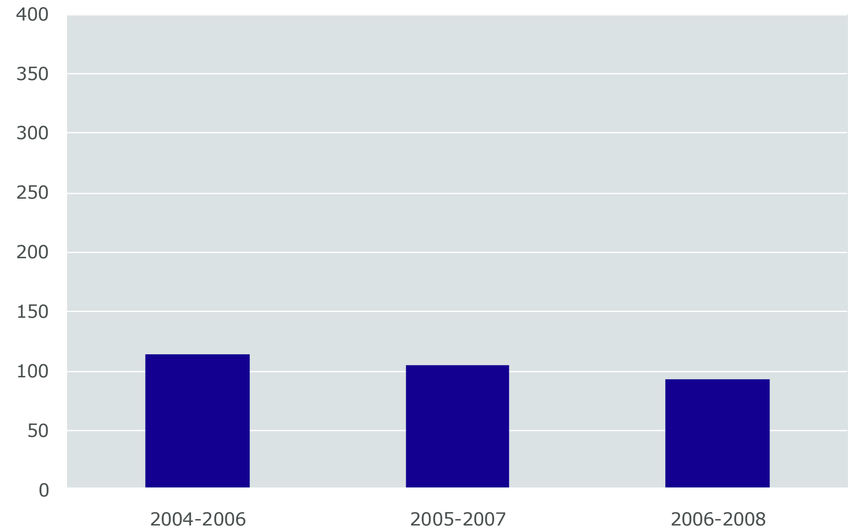
All CDCs (annual)

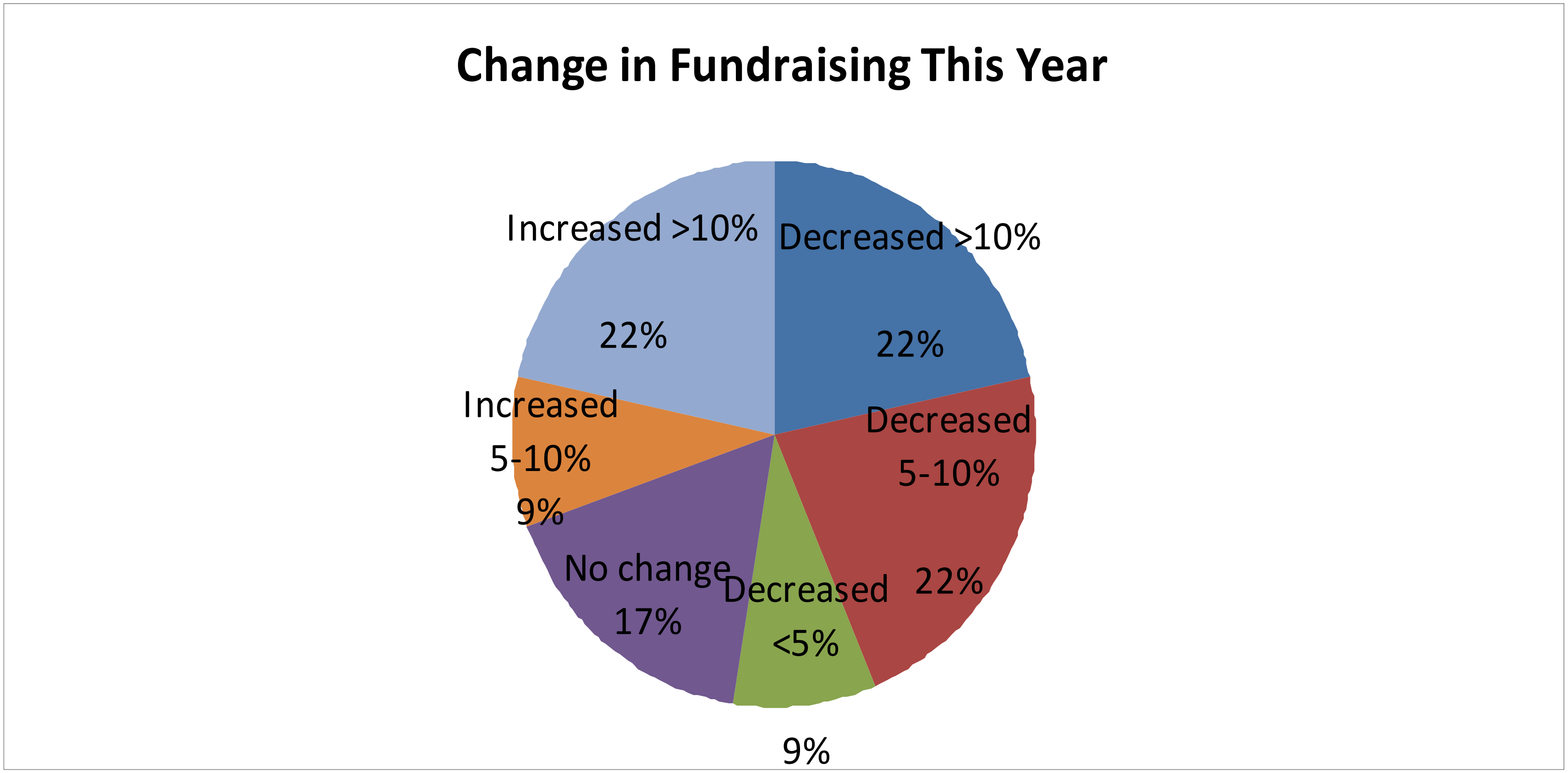


All CDCs (3-yr rolling average)



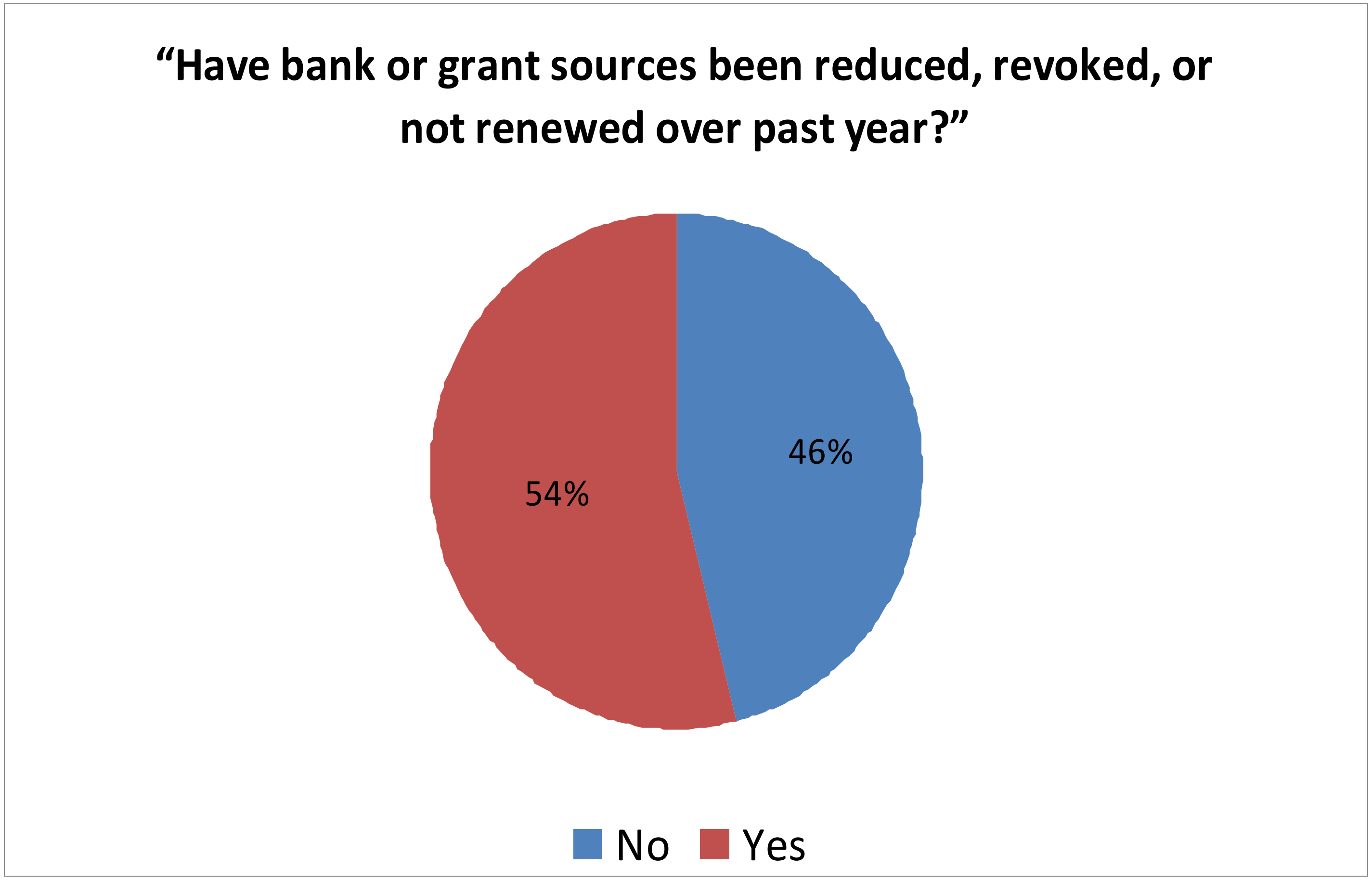
- When the days of cash data for 2008 are disaggregated, we find that 68% of the CDC sector had 90 days of cash or less, 40% had 60 days of cash or less and 24% had 30 days of cash or less.

Fundraising Revenue Decreases are Prevalent Among CDCs - 53% of CDC's Reported Decreases in 2009



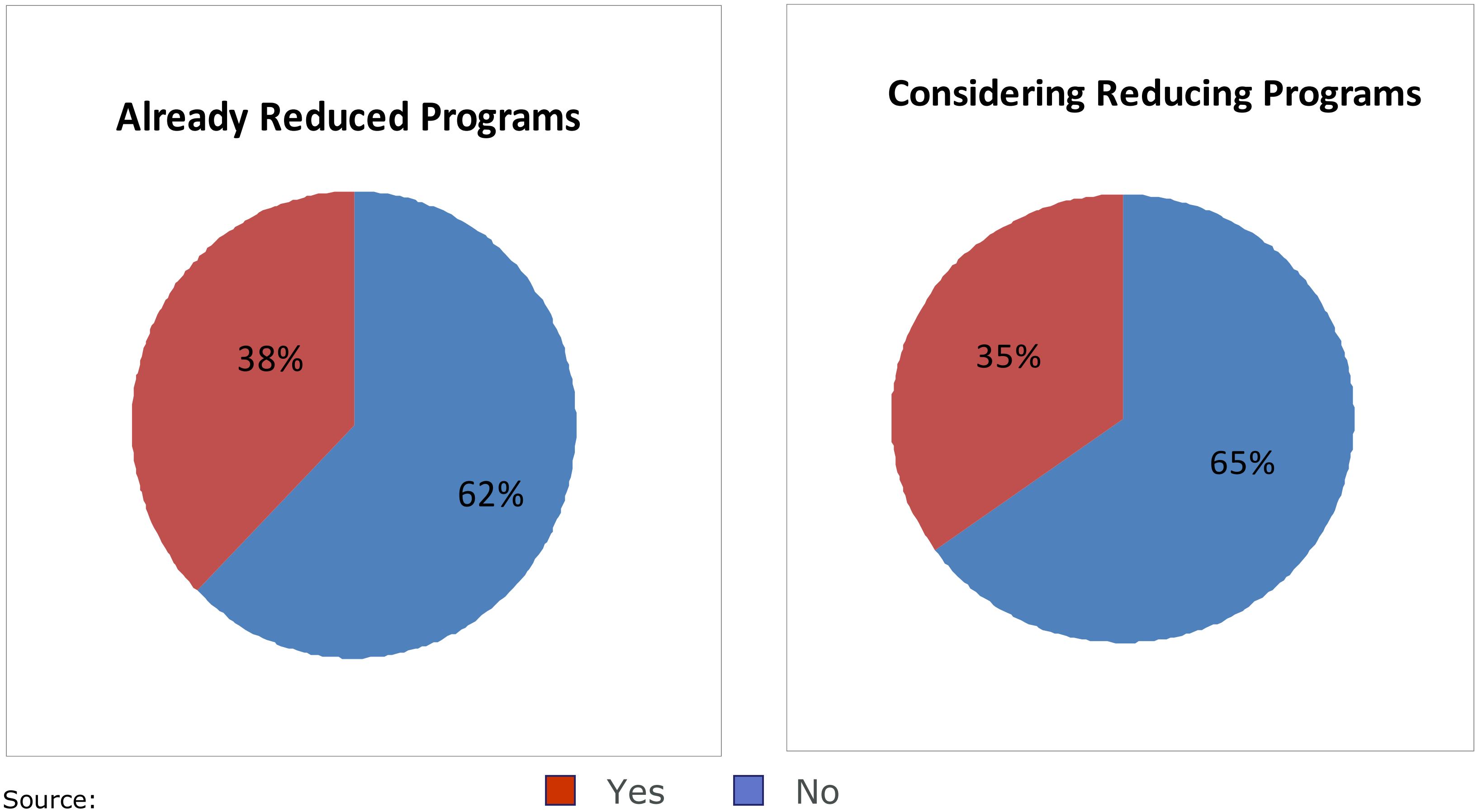
Source:
NSA - CDC Sector questionnaire results

Bank and Grant Funding is Down for Over Half of the CDCs Responding to the Survey Questionnaire



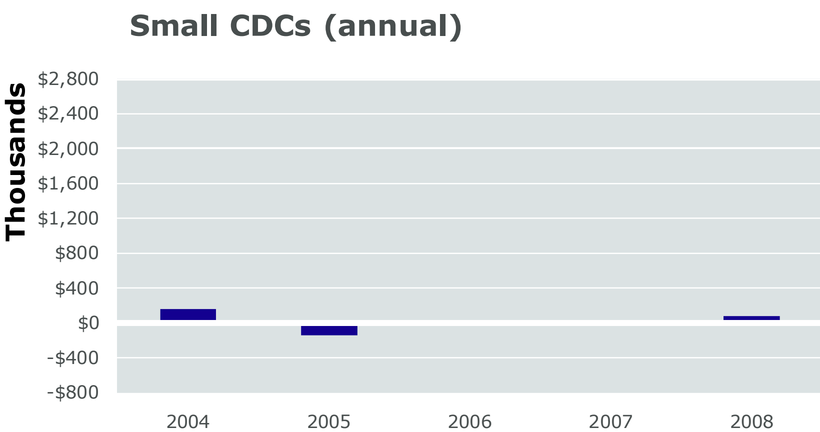
Source:
NSA - CDC Sector questionnaire results

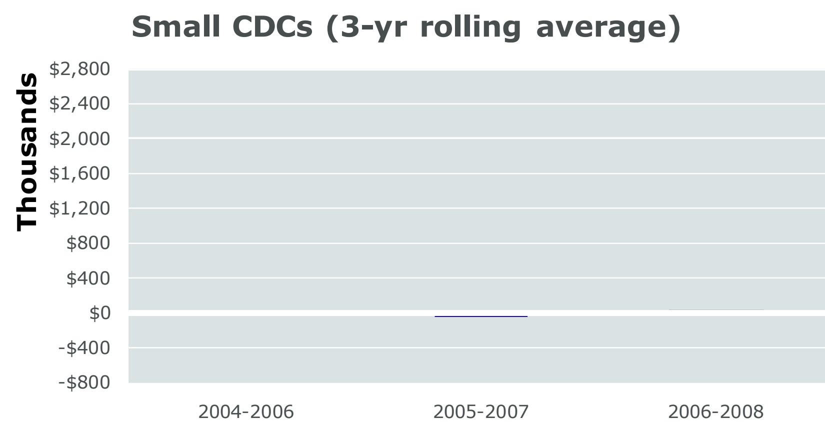
Financial Stress and the Drive for Cash Preservation Has Lead to Significant Cuts in CDC Programs



Source:
NSA - CDC Sector questionnaire results

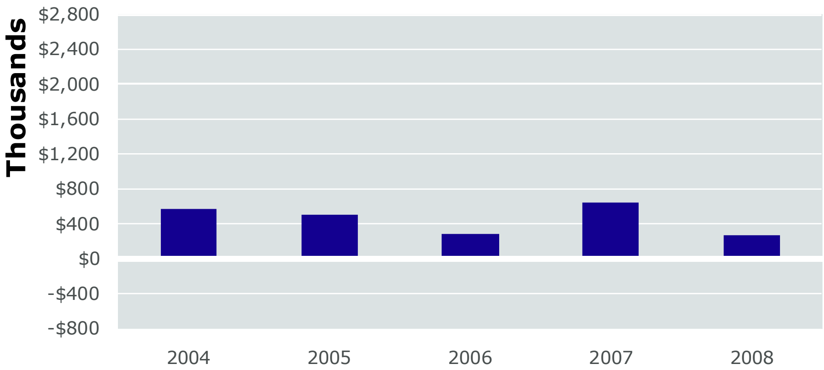
On Average, Small CDCs Have Historically Had Little Working Capital



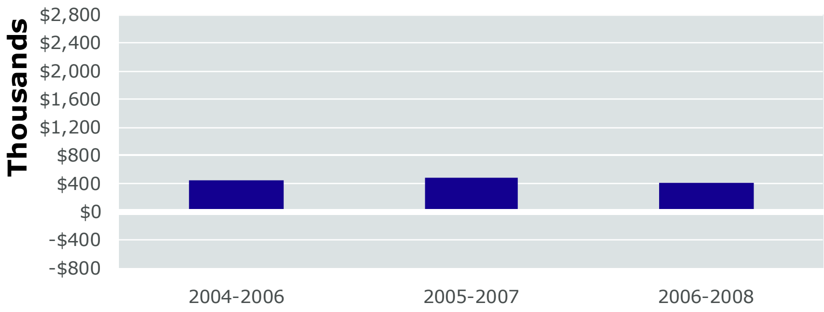


On Average, Medium-sized CDCs Have Maintained Modest Levels of Working Capital

Medium-sized CDCs (annual)

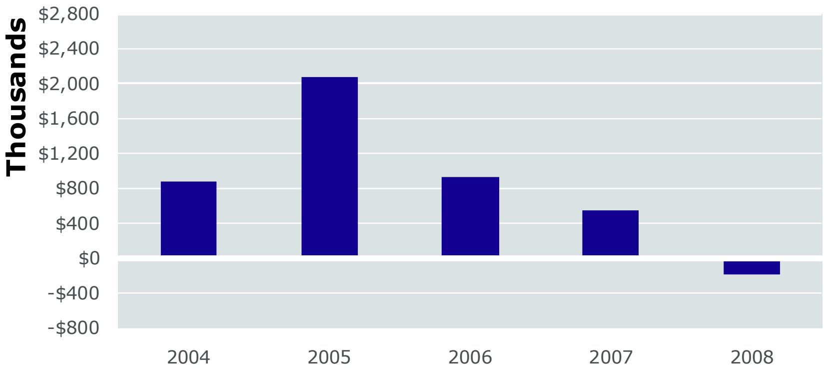


Medium-sized CDCs (3-yr rolling average)

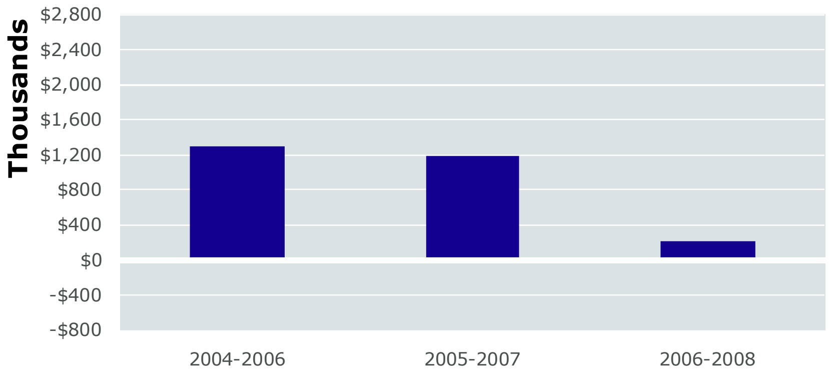


There Has Been a Steep Down Trend in the Working Capital Level for Large CDCs – At End of FY 2008 It Was Negative

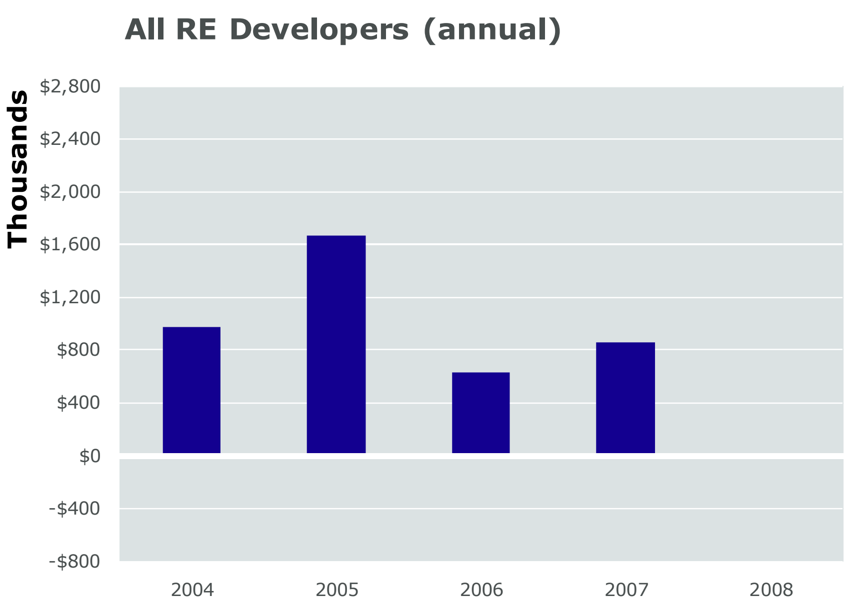
Large CDCs (annual)

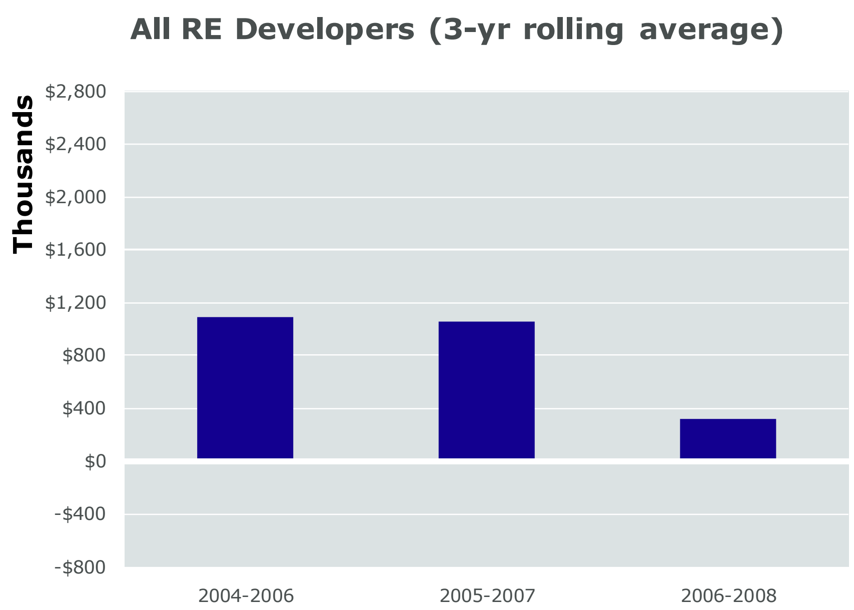


Large CDCs (3-yr rolling average)



On Average, Real Estate Developer CDCs' Historically Strong, If Erratic, Working Capital Level Went to Zero in 2008





Working Capital Levels Among Problem Solver CDCs Has Historically Been Thin

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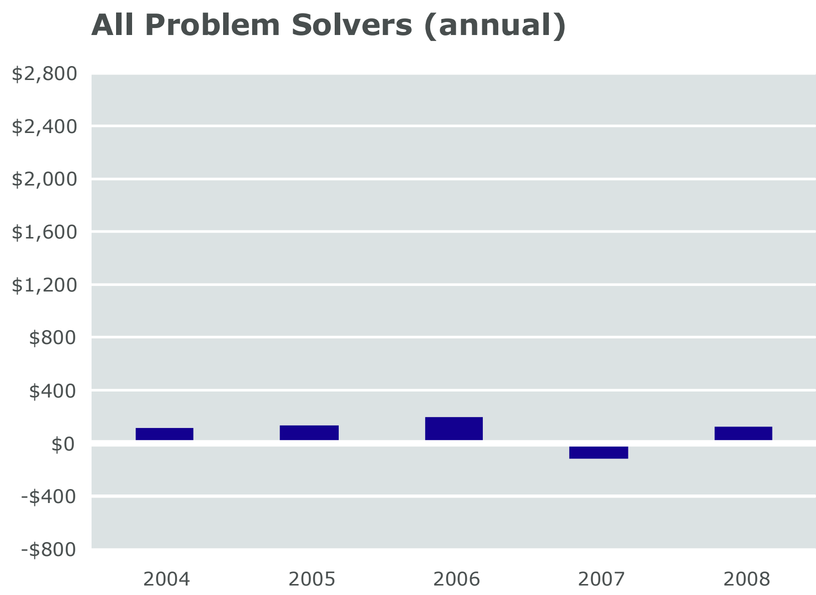
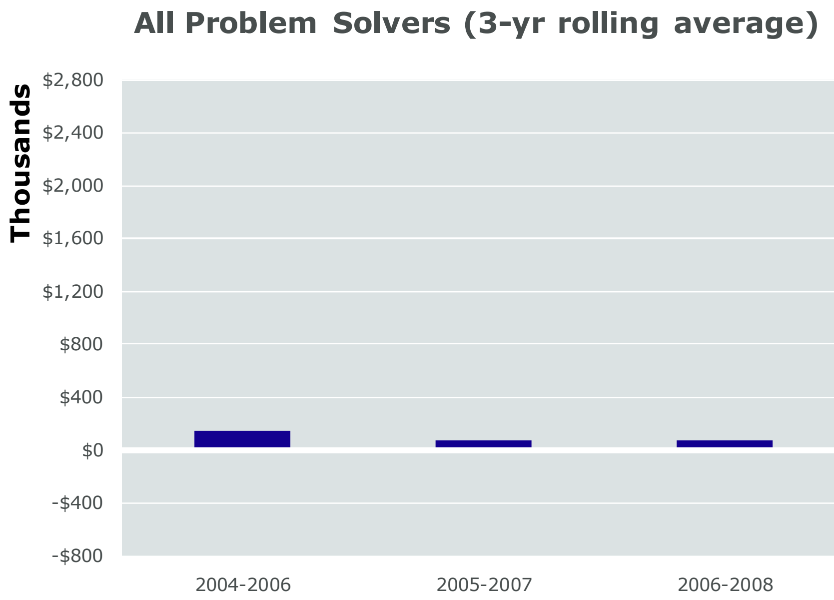
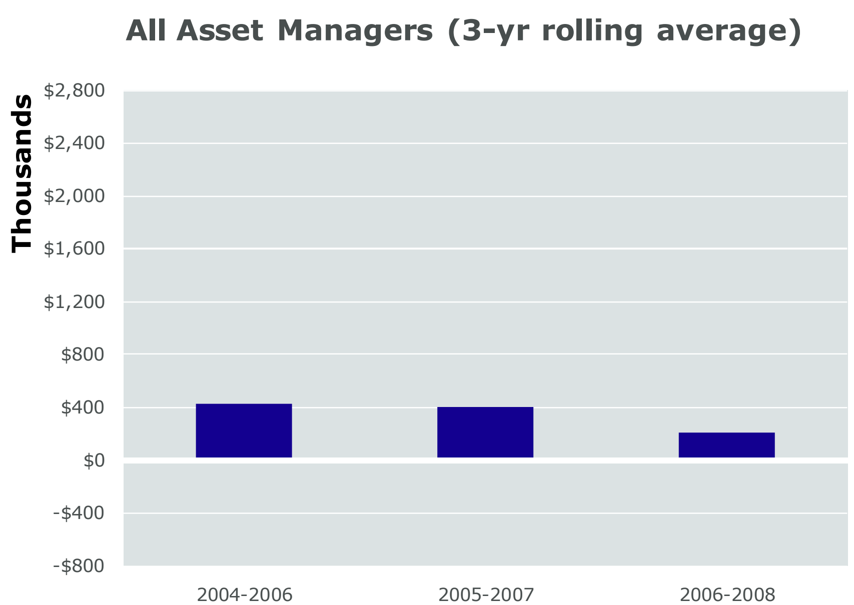




The Historically Stable Working Capital Levels of Asset Manager CDCs Turned Negative in 2008



Anecdotal CDC Commentary on Liquidity

- Risk taking and program offerings among CDCs are down and efforts to preserve cash are up
- CDCs are engaging in capacity reductions and operational and financial engineering to preserve cash
- CDC anecdotal commentary indicates a high priority on cash generation and preservation

Business Model Considerations

- Several factors limit profitability for CDC Sector real estate transactions – some factors are out of CDCs' direct control
  - Externally imposed caps on funding and revenues
  - Unlimited property acquisition and construction costs
- Business model economies of scale <u>by themselves</u> do not materially differentiate the financial situations of CDCs
- A balance between (i) community presence and support and (ii) building financial durability and sustainability is key

Future Considerations For Further Analysis

- Sector-wide use of consolidating schedules and the separation of operating and non-operating activities are recommended
- Revenue recognition practices may also be contributing to reduced visibility into true operating performance
- Improved financial reporting consistency and visibility = better informed management, planning and governance

Future Considerations For Further Analysis

- Obtaining funding support for pressing liquidity needs is a critically important challenge for the CDC Sector
- Funding support for pressing liquidity needs may require a commitment to restructuring at both the individual CDC and CDC Sector levels
- For the funding case, it may help to leverage work on CDC business model restructuring options currently under consideration

