The True Cost of Capital

Assessing the true cost of borrowing from Opportunity Fund and marketplace alternatives

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Presenters

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Agenda

Introduction and Key Findings
PRO Neighborhoods
Research Methods
Findings
Looking Ahead
Q&A
Prior Research
The True Cost of Capital

• The true cost of a small business loan is not easily discernable nor understood by most borrowers

• After calculating true cost, Opportunity Fund saves considerable sums:
  • Our trucking loans cost 21% less than typical equipment loans*
  • Our online loans cost 40% less than typical short-term online loans and 76% less than typical merchant cash advances (MCAs)
  • Our microloans cost 89% less than typical auto title loans and 91% less than typical personal installment loans

*For borrowers with credit scores <650
PRO Neighborhoods
PRO Neighborhoods: Neighborhood Revitalization

Promote neighborhoods of opportunity where diverse individuals and families at all income levels can thrive

Focus Areas

- Forward-looking data and planning tools
- Market-based housing models
- Innovative collaboration models

$125 MM over 5 Years
PRO Neighborhoods: CDFI Collaborative Competition

- Encourage CDFIs to advance comprehensive solutions, increase community support, and deepen outcomes.
- Deploy capital to LMI neighborhoods and serve LMI individuals and small businesses.
- Share best practices and models to improve conditions in distressed neighborhoods.
- Address persistent community development challenges through creative problem solving.
- Create capital access and improved service delivery for local CDFIs by pooling balance sheets, technology, and talent.
PRO Neighborhoods: Impact in Communities

**Competition Impact To-Date**
Five competitions, awarding more than $98 million to 25 CDFI Collaboratives (more than 70 CDFIs)

Winners of the first three competitions raised an additional $713 million in outside capital to issue 21,000+ loans to LMI customers and create or preserve 3,000+ affordable housing units and 11,000+ quality jobs

**2019 Competition Insights**
1. Majority are responding to catalytic community event
2. Strong representation of asset classes
3. Strong gender and diversity representation at executive level
PRO Neighborhoods: Competition Lessons Learned

- Capital Products
- Accelerating Neighborhood-Level Plans
- Responding to Catalytic Events
- Equitable Development
- People and Place Focused Strategies
Research Methods
Methodology

1. Select Opportunity Fund products
2. Develop borrower and product profiles
3. Identify plausible alternatives
4. Compute and compare true costs for Opportunity Fund products and alternatives
Analyzed 2,216 California loans between July 1, 2016 and September 30, 2018

- **Trucking**
  - Equipment Finance Loans

- **Online**
  - Short-term Online Loans and Merchant Cash Advances (MCAs)

- **Micro**
  - Personal Installment and Auto Title Loans
Defining “True Cost”

*Actual* Total Amount Repaid Over Life of Loan
– Initial Principal

True Cost of a Loan
### Characteristics of True Cost of Capital

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<tr>
<th></th>
<th>Annual Interest Rate</th>
<th>Total Payment*</th>
<th>APR*</th>
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<tbody>
<tr>
<td>Finance Charge</td>
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<td>Origination Fees</td>
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<td>Income Volatility</td>
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<td>Late Fees</td>
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<td>Accrued Interest on Delinquent Balances</td>
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<td>Restructuring, Reborrowing, and Other Borrower Action</td>
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<td>Comparability Across Credit Products</td>
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#### True Cost of Capital

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*Online payment calculators will often provide these two figures.

**Origination fees will only appear in monthly payments if they are folded into the repayment amount.*
Incorporating Cash Flow Volatility in Loan Repayment

1x = Late Fee and Accrued Interest
>3x in a row = Default
Incorporating Cash Flow Volatility in MCA Repayment

Accumulated expense deficit at month end

Days

$ Amount

- Accumulated Missed Expenses
- MCA Payment Due
- MCA-eligible CFADS
Assumptions and Limitations

• Utilized a typical borrower in quantifying the cost differences, individual borrowers with different characteristics will see different costs

• Model results are conservative estimates

• Estimates do not account for variability across industries and business types

• Alternative product information is indicative, but data sources on small business loan pricing are scarce
Findings
Trucking Loans

Santos, Commercial Truck Driver

394 trucking loans issued to borrowers with a <650 credit score

1,124 trucking loans issued to borrowers with a ≥650 credit score

Compared to: Equipment finance loans for borrowers with <650 and ≥650 credit scores
Opportunity Fund Saves Truckers Over 20%

21% less than a typical equipment finance loan

$24,812 $25,492

$19,734 $20,238

$21,566 $22,204

$21,524 $22,141

$47,387 Loan for Borrowers with <650 Credit Scores

$54,446 Loan for Borrowers with ≥650 Credit Scores
Online Loans

265 LendingClub referral loans

Compared to:
Short-term online loans and merchant cash advances (MCAs)
# True Cost of MCA Towers Over Cost of Opportunity Fund

$29,186 loan

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<th>Full Repayment</th>
<th>True Cost</th>
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<tr>
<td>Short-Term Online Loan</td>
<td>$11,922</td>
<td>$12,199</td>
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<tr>
<td>MCA</td>
<td>$8,610</td>
<td>$30,433</td>
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<tr>
<td>Opportunity Fund</td>
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<td>$7,335</td>
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- **76% less** than a typical MCA
- **40% less** than a typical short-term online alternative
433 working capital loans (≤$21,000) issued to borrowers with:
• No credit score
• Credit score <620 or
• Less than four tradelines in credit history

Compared to: Personal installment and auto title loans

Alejandra, Ale’s Bissu Makeup Store
Microloan Borrowers Save Substantially

$4,620 loan

- $7,645 Full Repayment for Personal Installment Loan
- $7,658 True Cost for Personal Installment Loan
- $6,339 Full Repayment for Auto Title Loan
- $6,354 True Cost for Auto Title Loan

- $674 Full Repayment for Opportunity Fund
- $681 True Cost for Opportunity Fund

89% less than a typical auto title loan
91% less than a typical personal installment loan
Looking Ahead
Where Do We Go From Here?

• Innovate lending practices – $87 billion capital gap for underserved businesses
• Bolster research – industry-wide data for small business lending
• Enact borrower protections – federal truth-in-lending act
Imagine what would happen if every entrepreneur had access to affordable credit.

*Shannen, Enos CPR*
Q&A

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