

SBA Loan Fund Reaches 100 Investors and \$400 million in Assets

The Solomon Hess SBA Loan Fund reached a key milestone in its development with 100 funded investors and \$400 million in assets. Investors currently represent 34 different states and range from large diversified financial institutions to regional and super-regional banks to small community banks. The expansion of our investor base has enabled us to build a diversified portfolio mainly consisting of the federally guaranteed portion of variable rate SBA 7(a) loans where the underlying borrower is located in a low or moderate income area in investor assessment areas. The Fund currently has over 780 loans in the portfolio. The Fund was founded in December 2004 with three investors for \$5 million. Since inception, all of our investors who sought CRA credit have received positive consideration for CRA from their regulators. Investment in the Fund does not guarantee positive consideration for CRA. ■



Founding partners Gino Heilizer and Bill Einstein would like to thank investors for their continued support as the Solomon Hess SBA Loan Fund reaches 100 investors and \$400 million in gross assets under management.

Unique CRA Strategies Discussed at First Solomon Hess Investor CRA Virtual Roundtable

Following our investor road show in 2015 we learned that there is a desire among bank CRA professionals to come together with industry peers to share ideas, ask questions and exchange experiences. To address this desire, we invited the CRA Officers and Compliance Professionals of our investor banks to participate in a CRA Virtual Roundtable Conference Call on May 18. Over 45 attendees representing 38 banks participated in the roundtable.

Prior to the call, we asked investors to submit discussion topics that they would like addressed by their peers. We received several requests for a discussion about unique CRA investment strategies which became the main topic on the agenda. We asked three of our investors to share their experiences in this area and provided attendees the opportunity to ask questions and share comments with our prepared speakers and other participants. *(continued on next page)*

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Social Impact Bonds Cristina Shapiro and John Olson of the Urban Investments Group of Goldman Sachs Bank (“GSB”) shared their knowledge of the use of social impact bonds (“SIBs”) as an innovative financing tool for CRA. In its 2012 CRA Exam, GSB received positive CRA credit as an innovative investment for its first SIB, a \$7.2 million loan to New York City to fund the project to reduce recidivism among the 3,000 16- to 18-year old males detained at Rikers Island jail.

A Social Impact Bond (“SIB”) is an innovative financing tool that has the ability to achieve a financial return with a social impact. SIBs are technically not bonds but are working capital loans where repayment of both principal and interest is through the proceeds of a government contract and the government pays only if the social program is deemed successful in achieving targeted outcomes.

From her experience, Ms. Shapiro shared that critical components of a successful SIB include: 1) party willing to reward investors if the program is successful, 2) the program being

funded has a proven track record and a strong service provider, 3) the transaction is supported by a strong intermediary that will manage the program, and 4) a financial structure that mitigates the risk of multi-year contract providing exit thresholds if the program is not working. For CRA, as with any other investment or financial structure, the ultimate beneficiary of the transaction will determine whether the SIB should qualify for CRA credit.

EQ2 Eric Fuiten, Asset Manager in the Community Investments Group for BMO Harris Bank, continued the discussion of unique CRA strategies by sharing his experiences with Equity Equivalent (“EQ2”) investments. An EQ2 is a long-term deeply subordinated loan with features that make it function like equity.

Mr. Fuiten shared that EQ2s account for a portion of BMO Harris’s total portfolio and typically these structures are used to backfill CRA needs in smaller communities where it can be difficult to find CRA investments. He also mentioned that they tend to specify that their funds be earmarked to benefit a target area.

Guaranty Bank Nina Johnson, CRA Officer of Guaranty Bank, then shared

that partnerships with CDFIs and credit unions are a key component of Guaranty Bank’s CRA strategy. Ms. Johnson said that Guaranty Bank partners with credit unions that are community focused by investing in a 12-month jumbo Certificate of Deposit at a negotiated rate at par or above. She mentioned that Guaranty Bank received positive CRA consideration for these investments at their last exam. Ms. Johnson referred to community banker roundtables as a significant value-add that are positively supported by the interagencies.

CRA Virtual Roundtable Takeaways

- Banks are moving to short duration CRA investment structures
- CDFIs offer partnership and investment opportunities for banks seeing CRA
- Relationship building with CRA industry peers continues to be a priority for all CRA professionals

Next Virtual Roundtable We will continue to provide this value-add to our existing investors and plan to host another virtual roundtable conference call following the release of the new CRA Interagency Q&A. ■

Manager’s Mailbag SBA Loan Fund Operating Reserve

QUESTION: What is the purpose of the Solomon Hess SBA Loan Fund’s Operating Reserve?

ANSWER: The SBA Loan Fund maintains an operating reserve which stood at \$10.2 million as of Q1 2016. This reserve has been built over the life of the Fund. The structure of the Fund is such that investors are paid a preferred return that is annualized and net of all fees and expenses. The preferred return is set at the beginning of each quarter based on the Fund Manager’s forecast of how the portfolio will perform.

The purpose of the Fund’s Operating Reserve is to shield investors against unpredicted increases in the prepayment speeds of the Fund’s assets. The majority of the Fund’s assets consist of the federally guaranteed portion of floating rate SBA 7(a) loans where the underlying borrower is located in a low or moderate income area in investor assessment areas. The low and stable interest rate environment over the past six years has resulted in low and stable prepayment speeds. As interest rates rise, prepayment speeds are expected to rise as more borrowers may choose to refinance their small business loans.

In effect, the operating reserve acts as an “allowance for prepayment” for the Fund. For Q1 2016, the preferred return was 1.375%. The Fund has paid investors the preferred return each quarter since inception. Past performance is no guarantee of future results. ■

Manager’s Mailbag provides an opportunity for CRA professionals to ask the managers of Solomon Hess Capital Management a question relating to the SBA Loan Fund or current CRA landscape. Have a question you’d like us to address? Email us at questions@solomonhess.com and we’ll try to include it in a future newsletter!

Small Business Loan Profiles: Carolina Kitchen and Feedlogic Corporation



Carolina Kitchen serves southern cuisine with welcoming hospitality. Impact of Solomon Hess SBA Loan Fund investment in Carolina Kitchen's SBA 7(a) loan was the creation and retention of 90 jobs in Hyattsville, Maryland.

Carolina Kitchen in Hyattsville, Maryland The Carolina Kitchen ("CK") is a popular southern cuisine restaurant group which combines unique blends of Cajun and Creole spices with traditional savory and home-style cooking. Founded in 1996 by Lance London as a full service restaurant with a down home southern twist, CK offers a dining experience encompassing welcoming southern hospitality and home cooked fare based on London's grandmother's recipes. The restaurant in Hyattsville was established in 2008.

Impact Record

Including Carolina Kitchen and Feedlogic, the Solomon Hess SBA Loan Fund has invested in 2,464 US-based small business since inception resulting in the creation and retention of 29,250 jobs throughout investors' communities. "When we review small business loans for investment, we look for businesses that embody the spirit of the regulations and go beyond the CRA requirements." said Bill Einstein, Managing Director and Chief Financial Officer of Solomon Hess Capital Management.

London was honored in 2012 as a recipient of the Minority Business Leader Award by the Washington Business Journal for his entrepreneurial drive, creativity and success. In that same year CK received Best Soul Food Restaurant recognition by the Hoodie Awards. This award honors local businesses, religious and neighborhood leaders, churches and schools for excellence within their own communities. When he received this award, London said, "Communities need more financial heroes to teach the importance of entrepreneurship and the power of economics."ⁱ

On behalf of its CRA motivated investors, the SBA Loan Fund invested in CK's SBA 7 (a) loan which resulted in the creation and retention of 90 local jobs. ■

Sources:
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www.thecarolinakitchen.com
www.feedlogic.com

Feedlogic Corporation in Willmar, Minnesota Willmar, Minnesota-based Feedlogic Corporation ("Feedlogic") is a leader in the development of intelligent feeding and farm monitoring solutions for agricultural production. It was established in 2001 and since then has built its business designing, building and selling equipment and software targeted to farmers and farming operations. It offers a suite of products which combine patented hardware and software to measure production processes and execute more precisely. The Minnesota High Tech Association ("MHTA") named Feedlogic a finalist in the Ag and Food category for the Tenke Awards in 2014. The Tenke Awards annually recognize Minnesota companies and individuals who have demonstrated superior technology innovation and leadership. ■



10 jobs in Kandiyohi County, MN, were created and retained as a result of the SBA Loan Fund's investment in Feedlogic's SBA 7(a) loan.

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Capital Management
is proud to sponsor the
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27th Annual SRI Conference
Nov. 9-11, Denver, CO

**CRA & Fair Lending
Colloquium**
Nov. 13-16, Las Vegas, NV

Visit our booth in the exhibition hall

Contact Michelle Lai for information
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Managing Good Capital Well

Solomon Hess Capital Management is an Investment Advisor located in Falls Church, Virginia with over \$500 million of assets under management.

Solomon Hess specializes in the small business and community impact sectors. Our investors include Banking Institutions of all sizes that are seeking Community Development Investment or Lending test credit within the Community Reinvestment Act (CRA) rules via exposure to SBA 7(a) related assets.

The Solomon Hess SBA Loan Fund LLC attempts to provide its investors with CRA credit related to their participation in the Fund. Investment decisions are not always exclusively based on the economic characteristics or investment merit of a specific asset. Certain CRA eligible securities sought by the Fund in specific geographies may not provide as great an economic benefit to the Fund as the same securities located in non-CRA geographies. The Fund may engage in transactions at times for reasons related to CRA considerations that may not be desirable from an investment standpoint. If one or multiple federal banking regulators, such as the OCC, FDIC or the Federal Reserve Board, were to deem an investment in the Fund as not qualifying for CRA credit, the impact to Fund investors could be material.