FitchRatings

Public Finance
Community Development & Social Lending
United States

Capital Impact Partners

A Community Development Financial Institution (CDFI)

Rating

Long-Term IDR	A+

Outlooks

Long-Term IDR	Stable

Rating Outlook

Stable

Outstanding Debt

Capital Impact Investment Notes	A+

Applicable Criteria

Public Sector, Revenue-Supported Entities Rating Criteria (April 2023)

Related Research

Fitch Ratings Updates Public Sector, Revenue-Supported Entities Rating Criteria; Adds CDFI Guidance (April 2023)

Strong Financial Profiles and Loan Oversight Support CDFI Credit (May 2023)

U.S. Public Finance Rating Actions Report and Sector Updates: Second-Quarter 2023 (July 2023)

The 'A+' rating assigned to Capital Impact Partners (CIP) and CDC Small Business Finance Corp. (CDC), collectively known as Momentus Capital, reflects its strong revenue defensibility and financial performance, which are bolstered by ongoing demand for access to capital and community-focused lending. Momentus Capital exhibits a stable operating profile, reflecting its lending products, grants, and other sources of revenue. Fitch Ratings also affirmed the 'A+' rating on Capital Impact Partners Investment Notes (Investment Notes). The Rating Outlook is Stable.

Fitch affirmed the 'A+' Issuer Default Rating (IDR) under it recently updated Public Sector, Revenue-Supported Entities Ratings Criteria (Revenue Master Criteria), published on April 27, 2023, which now includes a new appendix that provides additional, transparency and guidance for assessing community development financial institutions (CDFIs) within the methodological framework of the Revenue Master Criteria.

Strong asset quality, a healthy capital base, profitability and a strong leverage profile, all key drivers, are stable with upward potential. Earned income and liquidity exposure are also factored into the rating. Further, Momentus Capital has prudently managed its operations, as evidenced by its strong management of finance and loan performance, as well as good standing with federal oversight provided by the Department of Treasury's CDFI Fund.

Fitch rated the Investment Notes in 2022. As of Dec. 31, 2022, noteholders held $203.7 million in total notes outstanding. Accordingly, an aggregate principal amount of $146.3 million of Investment Notes remains unsold. The amount of notes available for purchase varies depending on the amount of notes sold and that mature and are repaid during the offering period.

The leverage associated with the notes is factored into the rating and does not have a material impact on the financial profile. CIP primarily uses the notes to fund initiatives that meet critical needs in low-income communities across the U.S. Fitch's analysis is based on results of CIP and CDC combined, which comprise the designated obligated group, although only CIP is an obligor under the notes.

Security

The obligations are secured by CIP's full faith and credit pledge, payable from all legally available revenues and assets.

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Key Rating Drivers

Revenue Defensibility

Revenue Defensibility (aa): The revenue defensibility assessment of 'aa' reflects the organization's exposure to revenue disruption based on the asset quality of its loan portfolio, including loan performance, portfolio composition, net chargeoff rates and the availability of reserves to offset loan losses. Based on five years of audited financials for 2018 to 2022, Momentus Capital maintains strong portfolio performance, as measured by a non-performing loans ratio of less than 1% and a net chargeoff ratio of 0.1%, and has demonstrated minimal losses over multiple cycles.

Momentus Capital observes adequate loan loss provisions for impaired loans, in line with its internal financial covenants and loan performance monitoring. The CDFI's expanding lending program model, which has proven effective, as demonstrated by overall growth and strong loan performance, coupled with low exposure to concentration risk, is factored into the assessment.

Asset Quality

The loan portfolio has historically exhibited very strong and stable performance, with minimal losses over multiple cycles. Based on five years of audited financials for 2018 to 2022, the ratio of non-performing loans (defined as loans 90 days or more delinquent or in default, foreclosure or non-accrual status) to total loans was below 0.7% as of fiscal 2022 and has consistently remained below 1% year over year over multiple cycles.

Further, Momentus Capital maintains strong loan loss provisions for impaired loans that are in line with its internal financial covenants and loan performance monitoring. Momentus Capital employs a risk-based approach for estimating potential losses on its loan portfolio. Its allowance for loan losses averaged 3.7% of total loans outstanding for 2018-2022, far exceeding actual loan losses (as measured by net chargeoff rates), which averaged just 0.1% per year during the same period.

Adjustments to Revenue Defensibility

Momentus Capital's low concentration risk and strong diversification of its credit exposures are considered positive credit attributes and are reflected in the 'aa' revenue defensibility assessment. Momentus Capital's lending spans across several sectors and U.S. geographies. Primary lending segments include education, healthcare, affordable housing, community development, and small business financing. A significant portion of Momentus Capital's business loan portfolio benefits from federal guarantees from the U.S. Small Business Administration (SBA), which cover between 75% and 90% of the principal balance outstanding for each loan.

Further contributing to Momentus Capital's strong revenue defensibility assessment is its long track record of successful community development lending across multiple segments, resulting in competitive advantages that are likely to endure into the long term. Its net loan portfolio demonstrated an average annual growth rate of 0.04% for 2018-2022, with an average loan balance of $379 million. Fitch expects this growth to continue due to ongoing unmet demand for access to capital. Further, given the worsening macroeconomic environment forecast for late 2023 to early 2024, demand for the affordable housing and community development loans offered by CDFIs is expected to rise.

Operating Risk

Operating Risk (a): The 'a' operating risk profile assessment reflects Fitch's assessment of earnings and profitability. The impact on its borrower base and the overall demand for its loan products, which contribute to its growth and profitability, are also important factors. The average net interest spread (NIS), a key profitability metric supporting its mission, was 55.5% for 2018-2022. This demonstrates a strong nominal difference between its borrowing and lending rates. However, Momentus Capital has been heavily reliant on grant income, which is material to its operating performance.

The earned income ratio (EIR), a key operating risk factor, averaged 58.2% for 2018-2022, demonstrating a heavy reliance on contributed income to support operations. The 2022 audited financials demonstrate a higher EIR of 85.8%, representing an improving trend. Momentus Capital demonstrates a unique, sophisticated and conservative risk management approach to its overall lending activities while managing expense ratios. It has created a lending model to fulfill its mission, factoring in volatility and loss exposure, which does not impede its operating flexibility or financial position.

Operating Profitability

Momentus Capital has demonstrated solid profitability margins compared with historical trends. Its relatively manageable cost burden creates flexibility in operations, which contributes to a stable operating profile and strong loan profitability. NIS averaged 55.5% for 2018-2022, demonstrating the strong nominal difference between borrowing and lending rates. Momentus Capital's primary revenue source is interest income and fees generated from

its various lending products. Additional revenues are sourced from servicing and processing of its SBA loan portfolio. Interest income on loans has grown steadily to $27 million in fiscal 2022, averaging $24 million over the past five years.

Grant Funding

Momentus Capital has been heavily reliant on grant income, which is material to Fitch's operating risk assessment. The EIR averaged 58.2% for 2018-2022, demonstrating a heavy reliance on contributed income to support operations. Grants and contributions averaged $16.4 million per year for 2018-2022, and grant income will likely continue to increase. However, the fiscal 2022 audited financial statements demonstrated a higher EIR of 85.8%, reflecting still moderate dependence but an improving trend in the EIR. This primarily reflects an increase in operating revenues following CIP's alliance with CDC in 2021.

Adjustments to Operating Risk

Operational practices and policies that reduce operating risks are also factored into the operating risk assessment. Momentus Capital follows a sophisticated and conservative risk management approach to its overall lending activities while managing expense ratios. It has created a lending model that fulfills its mission while factoring in volatility and loss exposure that does not impede its operating flexibility or financial position.

Risk reporting tools are very robust. Risk limits are highly conservative, consistently adhered to and routinely monitored. Safeguards are in place to limit loss exposure, and prudent measures are followed to mitigate losses and ensure repayment. Asset reviews are conducted annually, including evaluations of borrower credit to determine if any loan adjustments are necessary.

Exposure to non-financial risks (e.g. operational, reputational, litigation, regulatory, cyber and event risks) is very low. Additionally, risk controls such as internal ratings, watchlists or other risk monitoring scales are consistently used to measure risk exposure. In line with its mission, Momentus Capital systemically adapts its control environment to meet higher business volumes, such that growth is unlikely to affect its overall ability to operate. With its strong capital position, healthy cash balances and limited debt burden, Momentus Capital is in a solid position to manage borrower-related pressures amid slowing economic growth and persistent inflation.

Financial Profile

Financial Profile (a): The 'a' financial profile assesses leverage and the impact that unreserved, unexpected losses may have on the organization's resources. Debt-to-equity (DTE), the core capital ratio (CCR) and liquidity are key drivers for evaluating financial flexibility. Factoring in both CIP and CDC debt, the leverage profile is very strong, averaging 2.0x DTE for 2018-2022. Fitch's calculated adjusted debt is approximately $411 million when accounting for short- and long-term borrowing. Of the debt outstanding, short-term debt, including the Investment Notes, totaled $56.9 million, while long-term notes payable totaled $328 million.

Additionally, capitalization levels are stable, with a CCR of 23.4% in 2022, favorable to the five-year average CCR of 20.1% for 2018-2022. This demonstrates that the capital base provides a strong cushion to absorb unexpected losses and further reflects exposure associated with a broad range of lending risk.

Liquidity, measured by the ratio of unrestricted cash, liquid assets, and undrawn committed facilities to short-term debt, averaged 6.2x, representing strong coverage for meeting short-term obligations and/or unexpected shortfalls.

Leverage

Primary borrowing includes notes and bonds payable, Investment Notes, revolving lines of credit, and subordinated debt. Fitch calculated adjusted debt of approximately $411 million when accounting for short- and long-term borrowing. Of total debt outstanding, short-term debt (including Investment Notes) totaled $56.9 million, while long-term notes payable totaled $328 million.

The Investment Notes are capped at $350 million. Proceeds are used to provide technical assistance to borrowers and other market participants to increase the likelihood that their projects will be successful and have a positive impact on the communities they serve. Proceeds may also be used for general corporate purposes and to purchase securities or other assets that will be leveraged to support lending and investment activities and general operations.

Fitch calculated an adjusted DTE ratio of 2.4x when accounting for projected debt associated with the Investment Notes for 2019-2023. This also includes outstanding bonds payable of $5 million as of 2022.

Additionally, capitalization levels are stable, with a CCR of 23.4% in 2022, favorable to the five-year average CCR of 20.1% for 2018-2022. This demonstrates that the capital base provides a strong cushion to absorb unexpected losses and incorporates exposure associated with a broad range of lending risk.

Liquidity, as measured by the ratio of unrestricted cash, liquid assets, and undrawn committed facilities to short-term debt, averaged 6.2x, representing strong coverage for meeting short-term obligations and/or unexpected shortfalls.

Adjustments to Financial Profile

Asymmetric Risk Factors (neutral): Risk factors such as management, debt and market risk characteristics, external support and regulatory mandate are considered neutral to the rating.

Management & Governance

Momentus Capital is a well-governed organization with strong credibility in the sector. The management team comprises a nine-member executive team, all of whom have a strong commitment to social mission lending. CIP and CDC have substantially overlapping management teams, with Ellis Carr serving as the president and chief executive officer for both organizations. Collectively, the two entities have an unparalleled depth of experience in lending and impact investing.

Furthermore, strategic objectives are transparent, well-articulated and consistent with operational and financial performance. Prudent asset, operational and financial management policies have contributed to positive growth trends and strong debt management. The organization continually monitors its borrowers and reports loan performance for all segments on a regular basis. Additionally, compliance with internal covenants is consistently reported in financial reports.

Debt and Market Risk Characteristics

Debt characteristics are also neutral to the rating. Market risk characteristics are captured in the core capital analysis. Risk-weighted assets include both loans and investments.

External Support and Regulatory Mandate

Momentus Capital has a long track record of stable government support and maintains strong relationships with all levels of government. CIP is a participant in the CDFI Bond Guarantee Program, which provides fixed-rate, long-term capital that can be used to finance eligible community and economic development loans for small businesses, charter schools, healthcare facilities, and affordable housing.

Rating Sensitivities

Factors that could, individually or collectively, lead to negative rating action/downgrade

- Weakened leverage position, with a DTE ratio trend increasing above 3.0x.
- A material decline in interest earnings and fees that negatively impacts overall operating flexibility.
- Although unlikely, high levels of delinquency, coupled with higher losses, leading to a spike in DTE ratios.

Factors that could, individually or collectively, lead to positive rating action/upgrade

- Strengthened operating performance reflected in positive trends in key ratios, including EIR, CCR and DTE, over a sustained period.
- Demonstrated trends of high profitability and reserve levels relative to loan program performance.

Profile

CIP is a mission-driven CDFI that finances affordable housing, education, health care and community development, serving Northern and Southern California, Michigan, northeast Ohio, the New York Tri-State Area, Texas, and the Washington, D.C. Metro area.

CDC is a California non-profit organization committed to serving the capital needs of small businesses in California, Nevada and Arizona. Its mission is to champion the growth of diverse small companies in its communities through lending and financial services and business advising. CDC arranges commercial real estate and commercial/business development loans for small businesses, primarily through loan programs of the SBA.

Effective July 15, 2021, CIP and CDC aligned their operations under one chief executive officer and a joint board of directors yet they remain as separate legal end tax entities. CIP and CDC cross-guarantee most of each other's debt and are co-borrowers on certain obligations, enabling each organization to benefit from their combined financial strength. Fitch's analysis is based on the results of Momentus Capital, which represents the designated obligated group, although only CIP is an obligor under the notes. Fitch will monitor Momentus Capital, its respective debt obligations, and any changes to the legal relationship between the parties.

Momentus Capital is managed by an experienced 18-member board of directors, each of whom serves both CIP and CDC but are technically on two separate boards. The boards are composed of cooperative development, philanthropy, education, health care, housing, small business and economic development sector experts.

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