

RatingsDirect®

Summary:

Reinvestment Fund, Inc [The], Pennsylvania; General Obligation

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Credit Profile

Reinvestment Fund, Inc [The] ICR		
<i>Long Term Rating</i>	A+/Stable	Downgraded
Reinvestment Fund, Inc [The] taxable rev bnds		
<i>Long Term Rating</i>	A+/Stable	Downgraded

Rationale

S&P Global Ratings has lowered its issuer credit rating (ICR) on Reinvestment Fund Inc. (Reinvestment Fund or RF), Pa., and its rating on RF's series 2017 and 2018 taxable impact investment bonds to 'A+' from 'AA-'. At the same time, S&P Global Ratings removed the rating from CreditWatch, where it was placed with negative implications on Nov. 1, 2019. The outlook on all ratings is stable.

The rating change is partially the result of a recalculation of net equity. Because of an analytical error regarding the treatment of undrawn lines of credit, Reinvestment Fund's net equity-to-assets ratio was overstated, and appeared to be comparable with those of similarly rated peers. The recalculation results in a net equity-to-assets ratio averaging 11.4% between fiscal years 2015 and 2018, which we view as in line with the current rating after considering this ratio in conjunction with other key analytical factors.

Further, Reinvestment Fund's total equity ratio (net assets-to-total assets) has declined significantly in recent years, as increases in its outstanding loan balance have exceeded increases in net assets as a result of a marked reliance on debt. Reinvestment Fund's strategy for meeting its mission and growing its loan portfolio (which increased 93% between fiscal years 2014 and 2018) included absorbing additional debt obligations (which increased more than 120% over that same five-year period). While net assets have increased in four of the last five years, there has been a steady decline in RF's total equity ratio, resulting in weaker capitalization and leverage ratios in absolute terms and relative to rated peers. Net assets were 44.4% of total assets in fiscal 2014, dropping to 30.7% in fiscal 2018, averaging 37.8% over these five years. This lower net assets ratio provides limited resources on RF's balance sheet to absorb potential loan losses, particularly compared with other rated community development financial institutions (CDFIs).

In addition to these credit factors, the rating reflects our opinion of Reinvestment Fund's:

- Continued weakening debt position, as the total net assets-to-total debt ratio significantly decreased to 47.7% in fiscal 2018 from 87.6% in fiscal 2014, reflecting increases in debt outstanding that exceed increases in net position;
- Susceptibility to fluctuations in funding from government and private grants that might not be recurring, which could lead to volatility in net asset growth and profitability, as measured by return on assets (ROA); and
- Exposure to early financing loans that is comparable with that of industry peers, which we view as carrying

inherently more risk than permanent loans secured by cash-flowing projects.

Partially offsetting these factors, in our view, are Reinvestment Fund's:

- Very strong asset quality, with nonperforming assets (NPAs) averaging close to 0% between fiscal years 2015 and 2018, and the conservative approach to loan-loss reserves that have remained above 5% of total loans over the same five-year period, compared with a median reserve level of 3.8% for other rated CDFIs;
- Experienced senior management team and prudent capitalization strategy for continuing to execute on its mission while producing a strong net position; and
- Diversified lending portfolio reaching across multiple geographic markets and a variety of sectors, including charter schools, commercial real estate, healthy food, housing, and other community facilities.

Headquartered in Philadelphia, with offices in Baltimore and Atlanta, Reinvestment Fund is a mission-driven financial institution that leverages capital, analytics and partnerships in an effort to build strong, healthy, and more equitable communities. RF has issued two series of impact investment bonds, amounting to approximately \$50 million in fiscal 2017 and \$75 million in fiscal 2018, to finance loans to borrowers with the mission of expanding economic opportunity in low-wealth communities, as well as to pay down existing debt.

The bonds are general obligations of RF; therefore, its credit pledge supports the bonds. Bonds are payable from all legally available revenue and RF's assets, and are not secured by a reserve fund, mortgage lien, or security interest on or in RF funds or other revenue or assets.

Outlook

The stable outlook reflects our view of Reinvestment Fund's current-year performance and strategy over the next two years. Based on unaudited financials as of September 2019, RF expects its loan portfolio growth to lighten somewhat, driven by issues that affect CDFIs more broadly; this includes potential changes in the demand for loans to charter schools and the lack of a New Markets Tax Credit (NMTC) allocation in 2019, which diminishes RF's capacity to offer certain loans. In addition, after realizing substantial declines in its total equity ratio as it expanded its loan portfolio using additional debt, RF's capitalization strategy to fiscal 2023 includes emphasizing off-balance sheet loan originations and minimizing the balance of loans on-balance sheet that we may view as containing higher repayment risk. We believe this strategy, combined with our review of September 2019 unaudited financials and loan portfolio quality as of June 2019, would stem the significant decline in its total equity ratio over the next two years, and lead to net equity that will remain sufficient to absorb potential loan losses at the current rating level.

Downside scenario

If RF were to experience a significant reduction in capital adequacy as a result of increased debt, declining loan performance, or fewer unrestricted net assets, this would demonstrate volatility and weakness in its capitalization and debt positions. In this scenario, we could lower the rating or revise the outlook to negative.

Should RF's total on-balance sheet loans receivable decline, we would expect to see a corresponding decline in interest income from loans, which could have negative implications for RF's profitability. A significant reduction in net income,

potentially from a decreasing interest spread, or continued high reliance on volatile grant income, could also lead to our lowering the rating or revising the outlook to negative.

In addition, if secured debt were to increase to amounts we no longer consider minimal, we could lower the rating on series 2017 and 2018 bonds based on the availability of unpledged assets to cover unsecured general obligation bonds.

Upside scenario

We could raise the rating or revise the outlook to positive if RF were to demonstrate consistent and steady growth in its net equity ratios compared with its peers, as well as very strong, consistent profitability metrics. In addition, exceptional loan performance and the preservation of sufficient capital available to absorb potential loan losses could also result in our raising the rating or revising the outlook to positive.

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

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