**W.K. Kellogg Foundation**

**Mission Driven Investments**

**Bank Deposit Strategy**

**Overview**

The following outlines the W.K. Kellogg Foundation’s (WKKF) process for identifying and making just under $22 million in cash deposits in community development banks across the U.S. as an early “fast start” strategy for its Mission Driven Investment (MDI) program. The deposits were made for the most part in late 2008 and are all federally insured with the CDARS program.[[1]](#footnote-1)

To segment depository opportunities, MDI organized banks into two categories:

* *Geographic*: Top tier institutions in the WKKF priority geographies of Michigan, Mississippi, New Mexico, and New Orleans
* *Innovators*: Top tier institutions in the areas of race/gender, rural, and innovation in programs/models

**Geographic Institutions**

After scoring institutions across multiple quantitative and qualitative criteria, MDI made deposits in the following geographic focused banks:

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Institution** | **Geography** | **Assets** | **Description** | **Deposit** |
|  |  |  |  |  |
| Liberty Bank Detroit | Michigan | $290 mm | Founded in 1972, Liberty Bank’s primary focus is bringing financial services to d minority communities in Detroit. | $1.75mm |
| Southern Bancorp Mississippi | Mississippi | $145 mm | Southern Bancorp Mississippi is a member of Southern Bancorp, America’s largest rural development bank holding company. Since 2001, Southern Bancorp has made over $1.7 bn in development loans in the Delta. | $4 mm |
| Liberty Bank | New Orleans | $290 mm | Founded in 1972, Liberty Bank's primary focus is bringing financial services to d minority communities in New Orleans. | $4 mm |
| New Mexico Bank & Trust | New Mexico | $638 mm | New Mexico Bank & Trust is a member of Heartland Financial USA, a diversified financial services company dedicated to the preservation and growth of community banking. New Mexico Bank & Trust agreed to link MDI’s deposit to a branch located in a low-income community in Albuquerque. | $4 mm |

Please refer to the *Geographic Institution Selection* section for the criteria used in the selection of these banks.

**Innovative Institutions**

Innovative institutions were identified through MDI’s network and research as well as via partners such as the F.B Heron Foundation and NCIF. These banks were considered top tier in the areas of race/gender equity, rural, and program/model innovations.

|  |  |  |  |
| --- | --- | --- | --- |
| **Institution** | **Innovation** | **Description** | **Deposit** |
|  |  |  |  |
| National Cooperative Bank (NCB) | Program – Healthy Food | In August of 1978, Congress passed legislation creating the National Consumer Cooperative Bank (NCCB), a financial institution dedicated to consumer and small business cooperatives. The Bank Act also calls for the creation of the Office of Self-Help Development and Technical Assistance to provide start-up and development aid to new cooperatives. In its first year, NCB originated slightly less than $10 million in loans to a customer base composed largely of natural food cooperatives and a handful of New York City housing cooperatives. NCB has grown to over $1.6 bn in assets.  NCB is dedicated to strengthening communities nationwide through the delivery of banking and financial services, complemented by a unique focus on cooperatives and economic development. Despite its moderate size, NCB plays an important financing role within the cooperative and non-profit community.  As part of this investment, NCB agreed to link MDI’s deposit to its $200 mm food cooperative program. | $3 mm |
| Promerica Bank | Minority led/ownership  - Hispanic | Promerica is a de novo, Latino-owned bank founded in 2006 that operates in underserved areas in and around Los Angles. It currently has $100 mm in assets and takes a consultative approach that helps entrepreneurs grow their small businesses. Although not a CDFI, Promerica is focused on creating jobs and empowering communities overlooked by traditional financial institutions. | $2 mm |
|  |  |  |  |
| OneCalifornia Bank | Product Innovation  and  Ownership/  Structure Model | OneCalifornia founded in June 2007 in Oakland as one of the first chartered banks to be wholly owned by a philanthropic foundation. This innovative ownership structure enables the OneCalifornia Bank to engage in community programs in partnership with the OneCalifornia Foundation. The bank is focused on serving women and minority owned small businesses, social service organizations, and environmental programs in underserved communities. | $1 mm |
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Please refer to the *Innovative Institution Selection* section for the criteria used in the selection of these banks.

**Geographic Institution Selection**

The goal in executing the geographic deposit strategy was to identify top performing banks on both mission and financial criteria in WKKF’s areas of interest. To mitigate risk, bank deposits were also required to be fully FDIC insured. To meet these criteria, the following three-step process was applied:

1. Screened for geography, size, and participation in the Certificate of Deposit Account Registry Services (CDARS) Program
2. Screened for community development impact, commitment to racial/gender equity and financial health
3. Verified safety and soundness, determined how capital was going to be deployed, determined interest rates, and solicited input from WKKF program officers

**Step 1**

To be considered, banks had to meet the following basic criteria:

1. *Location*: Operated in one of the four targeted places
2. *Risk Mitigation*: Full FDIC insurance coverage via participation in the CDARS program
3. *Size*: $50 mm or more in assets to ensure sufficient capacity for WKKF’s deposits

As outlined below, a total of 80 banks passed these three initial screens:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **Target** |  | **CDARS Participant** |  | **$50 mm +** |
| **Place** |  |  | **in Assets** |
|  |  |  |  |  |  |
| Michigan | 170 |  | 23 |  | 19 |
| Mississippi | 97 | **+** | 29 | **+** | 24 |
| Louisiana Gulf Coast | 163 |  | 40 |  | 33 |
| New Mexico | 54 |  | 8 |  | 4 |
|  | **484** |  | **100** |  | **80** |

**Step 2**

To further screen the 80 eligible banks for development impact and financial health, MDI utilized available performance data - a standardized set of metrics to measure and compare the development impact and focus of different financial institutions. The following metric criteria was applied in the second phase of screening:

Racial/Gender Equity – Minority Depository Institutions

FDIC Minority Depository Institutions are minority owned and focused institutions that often play a unique role in promoting the economic viability of under-served communities. The FDIC created a definition to identify these institutions and to focus resources and activity towards these banks.[[2]](#footnote-2) Of the approximately 8,600 banks in the U.S., 200 are certified minority institutions.

Community Development – Certified Community Development Financial Institution (CDFI)

CDFI’s are unique entities established to provide credit, financial services, and other services to underserved markets or populations. Under the general definition of a community development financial institution as set forth by the Community Development Financial Institutions Fund at the U.S. Department of the Treasury, a CDFI has a primary mission of community development, serves a target market, is a financing entity, also provides development services, remains accountable to its community, and is a nongovernment entity. Of the approximately 8,600 banks in the U.S., 62 are certified community development financial institutions.

While there are numerous organizations certified as CDFIs by the CDFI Fund, it is believed that there are 200-300 financial institutions serving the needs of low-income people or communities in the U.S., but either have not applied for CDFI status or have otherwise not been able to fulfill all of the requirements for formal CDFI certification. NCIF has coined a term – Community Development Banking Institutions (CDBI) to denote any of the 8625 banks and thrifts in the country that “walk, talk or act” like CDFIs but may or may not be certified by the CDFI Fund.

Lending Impact –Development Lending Intensity – HMDA

The percentage of an institution’s single and multi-family *housing loan originations and purchases* that is located in CDFI Fund Investment Area census tracts. Census tracts are defined as Investment Areas if they have a poverty rate greater than 20%, an unemployment rate greater than 1.5 times the national average, or a median family income that is less than 80% of the relevant statistical area. All information is based on the 2006 HMDA database and 2000 Census data. NCIF has information on all banks in the country going back to 1996 that can be used for a detailed analysis inter-temporally and across a peer group.

*Adjusted* Development Lending Intensity excludes the “high rate loans in Low to Moderate Income Communities” from the total DLI – HMDA. Note: HMDA classifies loans that are priced at 3.0% or more above the relative rate benchmark, as “high rate loans”. This is a proxy for the “quality of lending in the targeted communities.”

Deposit Impact – Development Deposit Intensity

The percentage of an institution’s *branch locations* that are located in CDFI Fund Investment Area census tracts. NCIF calculated the DDI for every institution that reported a recognizable address. In case the branch locations are not geocodable, NCIF used the ZIP code and created a DDI value based on the center of the ZIP code. All information is based on the Summary of Deposits, a database maintained by the Federal Deposit Insurance Corporation.

Financial Health – Return on Assets

Return on Assets (ROA) is a number that shows how profitable a company's assets are in generating revenue. ROA is generally computed by dividing net income by total assets.

This number tells you "what the company can do with what it's got", i.e. how many dollars of earnings they derive from each dollar of assets they control. Return on assets is a common figure used for comparing performance of financial institutions (such as banks).

To effectively apply these criteria, we used the following criteria for ROA, Adjusted DLI, and DDI

* ROA > 0.50% - represents minimum standard of financial health;
* Adjusted DLI > 40% - the proposed NCIF threshold - is equivalent to over 2 times the average DLI for *all* banks in the country; and
* DDI > 50% - the proposed NCIF threshold – indicates “High DDI” and therefore makes a statement about low income service orientation

The following provides the number of banks that met the criteria by place. (Please note that the criterion was applied independently to each bank.)

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | Total |  | Minority | Certified | Return on | Adjusted |  |
|  | Banks |  | Institution | CDFI | Assets 0.5% + | DLI 40% + | DDI 50% + |
|  |  |  |  |  |  |  |  |
| Michigan | 19 |  | 1 | 1 | 15 | 1 | 4 |
| Mississippi | 24 |  | 0 | 2 | 23 | 6 | 16 |
| Louisiana Gulf Coast | 33 |  | 1 | 1 | 31 | 3 | 21 |
| New Mexico | 4 |  | 0 | 0 | 4 | 0 | 4 |
|  | **80** |  | **2** | **4** | **73** | **10** | **45** |

In summary, out of the pool of 80 pre-screened banks, 2 were FDIC minority institutions, 4 were certified CDFI’s, 73 had return on assets greater than 0.50%, 10 had adjusted DLI’s greater than 40%, and 45 had DDI’s greater than 50%.

A simple scoring system was then utilized to identify the top performing banks per the above criteria in each targeted geography. For each criterion met, banks received 1 point. What follows are the three highest scoring banks by geography (in 2008).

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Michigan** | **Score** | **Minority** | **CDFI** | **ROA** | **DLI** | **DDI** |
|  |  |  |  |  |  |  |
| 1. ShoreBank Detroit[[3]](#footnote-3) | 4 | no | yes | 0.60% | 85.06% | 85.00% |
| 2. First Independence | 3 | yes | yes | 0.27% | 23.00% | 75.00% |
| 3. United Bank & Trust | 2 | no | no | 1.38% | 30.15% | 50.00% |
|  |  |  |  |  |  |  |
| Michigan Peer Group (avg) |  | 5.26% | 5.26% | 0.87% | 21.37% | 18.75% |

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Mississippi** | **Score** | **Minority** | **CDFI** | **ROA** | **DLI** | **DDI** |
|  |  |  |  |  |  |  |
| 1. Southern Bancorp Mississippi | 3 | no | yes | 0.64% | N/A[[4]](#footnote-4) | 100.00% |
| 2. Guaranty Bank & Trust | 3 | no | yes | 1.48% | N/A | 83.00% |
| 3. BankFirst Financial Services | 3 | no | no | 0.93% | 44.18% | 70.00% |
|  |  |  |  |  |  |  |
| Mississippi Peer Group (avg) |  | 0% | 8.33% | 1.18% | 22.13% | 55.88% |

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| --- | --- | --- | --- | --- | --- | --- |
| **New Orleans** | **Score** | **Minority** | **CDFI** | **ROA** | **DLI** | **DDI** |
|  |  |  |  |  |  |  |
| 1. Liberty Bank, New Orleans | 4 | yes | yes | 1.37% | 27.30% | 69.00% |
| 2. Omni Bank | 3 | no | no | 1.12% | 40.05% | 55.00% |
| 3. First National Bank of Louisiana | 2 | no | no | 1.38% | 36.84% | 50.00% |
|  |  |  |  |  |  |  |
| New Orleans Peer Group (avg) |  | 3.00% | 3.00% | 1.34% | 25.50% | 53.67% |

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **New Mexico** | **Score** | **Minority** | **CDFI** | **ROA** | **DLI** | **DDI** |
|  |  |  |  |  |  |  |
| 1. New Mexico Bank & Trust | 2 | no | no | 1.19% | 13.13% | 60.00% |
| 2. First Community Bank | 2 | no | no | 1.04% | 17.51% | 54.00% |
| 3. Lee County State Bank | 2 | no | no | 1.40% | N/A | 66.00% |
|  |  |  |  |  |  |  |
| New Mexico Peer Group (avg) |  | 0.00% | 0.00% | 1.50% | 15.32% | 57.50% |

Based on these scores, we selected the highest scoring bank in each state for further diligence:

|  |  |  |
| --- | --- | --- |
| **Institution** | **Geography** | **Score** |
|  |  |  |
| Shore Bank Detroit | Michigan | 4 out of 5 |
| Southern Bancorp Mississippi | Mississippi | 3 out of 5 |
| Liberty Bank | Gulf Coast | 4 out of 5 |
| New Mexico Bank & Trust | New Mexico | 2 out of 5 |

**Step 3**

Once selected, we needed to ensure that the banks met minimum safety and soundness criteria, would effectively deploy our capital, offered market or near market rates, and were aligned with WKKF program officer goals.

Safety & Soundness

To determine safety and soundness, we utilized Bankrat.com’s CAEL ratings: [[5]](#footnote-5)

|  |  |
| --- | --- |
| **Institution** | **Star Rating** |
|  |  |
| Shore Bank | 2 out of 5 |
| Southern Bancorp Mississippi | 4 out of 5 |
| Liberty Bank | 4 out of 5 |
| New Mexico Bank & Trust | 4 out of 5 |

Of the selected banks, only Shore Bank failed to meet minimum safety and soundness criteria. According to Bankrate.com’s memorandum of findings:

Banking institutions are subject to regulatory assessments of profitability, asset quality, capitalization, and liquidity. We are of the opinion that, as of September 30, 2007, this bank exhibited a below average condition, characterized by lower than normal overall, sustainable profitability, questionable asset quality, below standard capitalization, and lower than normal liquidity.

Capital Deployment

We determined how the selected banks would deploy our deposit via their loan to deposit ratio. The banks with low loan/deposit ratios were lending less in their communities than their peers (e.g. using a greater share of their deposits to purchase securities versus making loans).

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| --- | --- | --- |
| **Institution** | **Loan/Deposit** | **Avg Peer Loan/Deposit** |
|  |  |  |
|  |  |  |
| Southern Bancorp Mississippi | 57% | 85% |
| Liberty Bank | 53% | 80% |
| New Mexico Bank & Trust | 96% | 71% |

Please note that both Southern Bancorp Mississippi and Liberty Bank had loan/deposit ratios considerably below peer group averages.

Offered Rates

We contacted selected banks to get rate information and compare to the average national rate for jumbo CDs provided by Bankrate.com.

WKKF Program Officer Input

We further provided the final list of selected institutions for review by relevant WKKF program officers.

**Innovative Institution Selection**

The selection process for the below institutions relied more heavily on a qualitative assessment of race/gender, rural, and program/model innovations. Please note that all institutions had more than $50 mm in assets and participated in CDARS.

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Institution** | **Innovation** | **Minority** | **CDFI** | **ROA** | **DLI** | **DDI** |
|  |  |  |  |  |  |  |
| NCB Bank | Program | No | No | 0.7% | 29% | 33% |
| Southern Bancorp National | Rural | No | Yes | 1.1% | 21% | 25% |
| Promerica Bank | Minority | Yes | Yes | (4.1%)[[6]](#footnote-6) | N/A | 100% |
| OneCalifornia Bank | Model | No | Yes | (7.6%)[[7]](#footnote-7) | N/A | 100% |
|  |  |  |  |  |  |  |
|  |  |  |  |  |  |  |
|  |  |  |  |  |  |  |

Safety & Soundness

To determine safety and soundness, we utilized Bankrat.com’s CAEL ratings:

|  |  |
| --- | --- |
| **Institution** | **Star Rating** |
|  |  |
|  |  |
| Southern Bancorp National | 4 out of 5 |
| Promerica Bank | 4 out of 5 |
| OneCalifornia Bank | 3 out of 5 |
|  |  |
|  |  |
|  |  |

Offered Rates

We contacted selected banks to get rate information and compare to the average national rate for jumbo CDs provided by Bankrate.com.

1. Certificate of Deposit Account Registry Service (CDARS®) allows depositors access to full FDIC insurance on deposits of up to $50 million. When an investor places a large deposit with a CDARS network member, that institution uses CDARS to place the funds into certificates of deposit issued by banks in the CDARS network. This occurs in increments of less than the FDIC insurance maximum to ensure that both principal and interest are eligible for full FDIC insurance. [↑](#footnote-ref-1)
2. Section 308 of FIRREA defines the term "minority depository institution" as any depository institution where 51 percent or more of the stock is owned by one or more "socially and economically disadvantaged individuals." Given the ambiguous nature of the phrase "socially and economically disadvantaged individuals," the FDIC's Policy Statement defines "minority depository institution" as any Federally insured depository institution where 51 percent or more of the voting stock is owned by minority individuals. "Minority" as defined by Section 308 of FIRREA means any "Black American, Asian American, Hispanic American, or Native American." The voting stock must be held by U.S. citizens or permanent legal U.S. residents to be counted in determining minority ownership. [↑](#footnote-ref-2)
3. Assumes same ROA, DLI, and DDI as Shore Bank (parent company) [↑](#footnote-ref-3)
4. Rural banks are not required to submit this information, indicated here as N/A [↑](#footnote-ref-4)
5. CAEL stands for Capitalization, Asset quality, Earnings and Liquidity. These are the measures of an institution's safety and soundness used in this model. It is an abbreviated version of the industry standard ratings known as CAMEL. Incorporated into these measures are more than 20 tests applied on a quarterly basis to the results reported by each institution. Using this data from the Federal Deposit Insurance Corporation and Office of Thrift Supervision, the program assigns a value to each of the CAEL categories and calculates a composite rating for the institution. More than 10,000 FDIC-Insured banks and thrifts are analyzed.

   The most desirable Safe & Sound CAEL rating is one, the least desirable is five, in accordance with industry standards. Bankrate.com has reversed this order in its graphic rankings for easy visual recognition. The top star rating is five, the lowest star rating is one. Performing institutions will generally receive a rating of 3 or better stars with the majority of banks falling into the 3-4 star range. By contrast, the performing Safe & Sound CAEL range would be 1, 2 and 3 with the majority of institutions falling into the 2 range. [↑](#footnote-ref-5)
6. As a de novo bank, OneCal is expected to have a negative ROA as it takes a number of years to become profitable. Please note that OneCal’s ROA was higher than peer banks that were formed in the same year. [↑](#footnote-ref-6)
7. [↑](#footnote-ref-7)