African Development Center of Minnesota

African Development Center

Economic Impact of Financial Coaching and Loan Programs

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Background

The mission of the African Development Center (ADC) is to grow businesses, build wealth, and increase reinvestment in the African communities in Minnesota. ADC helps African immigrants and refugees in Minnesota overcome barriers to financial security and success. ADC helps emerging entrepreneurs develop successful businesses that serve their community, and to help community groups build a stronger neighborhood economy.

ADC achieves its mission by providing services in four areas: financial literacy, home ownership education, business education, and financing.

ADC is a leader in micro-lending to small businesses, outperforming even the largest banking institutions in the state of Minnesota. With the help of nine dedicated full-time employees, and our Executive and Finance Committee and Board of Directors, ADC provides services in six languages to communities throughout Minnesota.

Purposes of the evaluation

The purposes of this evaluation are to document ADC's impacts on alumni as well as on the local economies where alumni live and/or operate businesses. The results of this research will assist in ADC's strategic planning, implementation, and fundraising. In addition, the research will provide ADC's stakeholders and the community with an objective assessment of the impacts of the organization that will contribute to the understanding of ADC's social and economic value.

The evaluation covers two of ADC's main service programs: business lending and financial coaching.[1]

The key evaluation questions are:

- What is the impact of ADC's financial coaching on personal finances?
- What is the impact of ADC's business financing on job creation?
- What is the impact of ADC's business financing on business revenues?

Evaluation methods

The overall goal of this research is to assess the economic impact of ADC's services. The economic impact of each program depends on the effectiveness of ADC's strategy on achieving the expected outcomes. Therefore, a necessary preliminary step is to determine whether ADC's activities are generating any positive change in the economic situation of its participants. To achieve this, we rely on a combination of output data from participants and evidence from the literature on the impact of comparable interventions. The evaluation only includes outcomes for which sufficient data and evidence are available. Detailed methods and computations are summarized by outcome in their respective sections.

The evaluation is based on information from ADC's client records from 2014, 2015, and 2016. Client records include data from program application and intake forms, loan applications, records of one-on-one consultations, and follow up meetings with clients. The number of clients in the samples used in the analysis varies by year and outcome. Throughout the analysis, we assume that the information from the observed clients is representative of all participants with regard to gender, race/ethnicity, education, and income at onset of ADC assistance. Detailed sample sizes are summarized in the outcomes section.

1 ADC also offers homeownership coaching. At the time this research was conducted, there was not sufficient data on clients' outcomes to perform an economic analysis of the impact of the program. Note, however, that improved homeownership is expected to generate positive outcomes for families and society, including improved educational achievement of children and increased financial and job stability. Wilder Research will work with ADC to devise a research plan to assess these benefits in future evaluations.

Economic impact of services

Financial coaching

The personal financial coaching service at ADC targets Minnesota's African immigrants who are struggling to manage their finances. The service includes group sessions as well as some one-on-one coaching. The program covers money management, budget counseling, debt management, and review of credit reports. In many cases, the financial coaching is the first step for housing counseling, as these services are closely related.

The expected positive outcomes of financial coaching include:

- Financial stability
- Improved credit score
- Improved repayment of formal debts (with financial institutions, landlords, and other debtors)
- Lower interest rates
- Increased credit access and limits
- Increased disposable income because of reduced debt payments
- Ultimately increasing consumption since people will have more money in long run
- Potential benefits from investments made with loans including homeownership, access to a vehicle, and business investments
- Increased balance of banking accounts
- Improved preparedness for emergencies from increased savings

As noted before, we only assess outcomes for which sufficient data and evidence are available. Under these constraints, we focus the analysis on the impact on *increased balance of accounts* and *reduction of debt*. These two outcomes are the initial steps to achieve many of the other outcomes listed above and are the most commonly researched outcomes in the academic and evaluation literature.

Impact on account balances

The first outcome we assess is the increase in account balances associated with receiving financial coaching at ADC. We analyze increases in balances of transaction accounts (e.g. checking) and savings accounts. Previous research conducted by The Urban Institute (Theodos et al., 2015) shows that individuals who participate in financial coaching experience an increase in their account balances of more than three times (170% increase). There is no information on the average account balance of ADC's participants. However, we do know that the mean balance in transaction accounts in the United States for non-white individuals is $1,854 (Federal Reserve, 2016), while the average balance in savings accounts for participants in financial coaching observed by Theodos, et al. (2015) is $1,015. Using these parameters as benchmarks for a typical ADC participant, we estimate that participants in financial coaching increase their account balances in checking and savings accounts by $3,144 and $1,721 respectively.

1. Changes in account balance

	Initial balance[1]	Estimated increase in account balance per participant (170% increase)[2]
Median value of holdings in transaction accounts	$1,854	$3,144
Mean savings account balance	$1,015	$1,721

[1] Non-white individuals in the U.S., 2016. Federal Reserve. Survey of Consumer Finances.
[2] Average per participant from Theodos et al., (2015).

Aggregate value of increase in account balances

To assess the aggregated impact of the financial coaching for all ADC's participants, we used information from 204 participants who received financial coaching during 2015 and 2016.[2] The total value generated by these participants was $641,454 in transactional accounts and $351,084 in savings accounts.

2. Total additional value of account balances (2015-2016) (N=204)

	2015 (N=98)	2016 (N=106)	Total (N=204)
Total value of additional balance in accounts	$308,150	$333,305	$641,454
Total value of additional savings	$168,658	$182,426	$351,084

[2] These participation totals are estimates based on intake records and recall from program leaders. However, actual participation may vary from these estimates. Therefore, total outcomes and benefits may include a small and unknown margin for error. Also, note that we assume that in average, all participants have a checking and a savings account.

Future and indirect benefits of increased balances

As mentioned earlier, other positive outcomes derived from these additional funds will materialize in the future, and go beyond the nominal value of the balances. For instance, the increased balances could lead to more consumption of goods and services in the future, or saved to pay for unplanned expenses such as medical emergencies or unemployment, reducing the financial risk of catastrophic emergencies.

Furthermore, the money could be used to invest in a business or education. These investments are likely to increase the income of participants, and generate other positive outcomes associated with increased education and entrepreneurial activities. For instance, increased education is correlated with improved health care, reduced crime, and a reduced need for public assistance. Potential positive outcomes of increased entrepreneurial activities include future job creation, increased tax revenues, and potential diversification of local economies.

Impact on personal debt

A second positive effect of financial coaching is the reduction of personal debt. Financial education helps participants improve the administration of their income by promoting the use of budgets and increase savings; these tools allow the allocation of more income to pay existing debts. Researchers at the Urban Institute (Theodos et al., 2015) find that participants in financial coaching programs tend to experience a reduction of 18 percent in the balances from all debts. We assume that about 72 percent of participants hold any type of debt (Federal Reserve, 2016). The average value of holdings for families with any debt is estimated at $89,800, including mortgages and other types of loans.

Based on these parameters, we estimate that an average participant in ADC's financial coaching is likely to reduce their debt by $11,396. Since, it's likely that only a fraction of participants may own a home, we also estimate the reduction in other debts excluding mortgages.

3. Debt reduction for an average participant

	Impact of financial coaching	Average holdings[1]	Average reduction in debt
All debts	-18%	$89,800	$11,396
Other debt (excluding-mortgages)	-18%	$6,400	$75

[1] 72 % of families hold any type of debt in the U.S., (Federal Reserve, 2016)

Aggregate value of reduced debt

We analyze the change in debt balances in current accounts, such as credit card or personal loans and long-term debt such as mortgages. In 2015 and 2016, ADC participants reduced their collective debt by $2.3 million, including $15,354 in non-mortgage debt.

4. Collective debt reduction (2015-2016) (N=204)

	2015 (N=98)	2016 (N=106)	Total (N=204)
All debts	$1,116,773	$1,207,938	$2,324,711
Other debt (excluding-mortgages)	$7,376	$7,978	$15,354

Business lending

The ADC business lending program is a comprehensive service to help clients to plan, start, or expand their businesses. The program covers two aspects: education and funding. The education aspect of the program includes one-on-one advising and group sessions, while the funding aspect consists of a small business loan program and assistance finding funding sources that fit the business plan and characteristics of the entrepreneur.

For the analysis of this program, we included 62 clients who received at least one loan from ADC or from an external source with the help of ADC between 2014 and 2016. The number of clients is duplicated since some participants received more than one loan during the observed period.

Figure 5 shows a summary of statistics related to the loans received by these clients. The number of clients receiving loans has increased over the past three years and almost doubled the initial 15 clients in 2014. Most clients received more than one business loan; ADC distributed 100 loans over the three-year period. The total value of all loans was $1.7 million, with an average loan around $17,000.

5. Business loans summary statistics (2014-2016)

	2014	2015	2016	3-year total
Number of clients (duplicated)	15	19	28	62
Number of loans (multiple sources)	28	29	44	100
Value of loans	$480,000	$414,000	$775,281	$1,669,281
Average value per loan	$18,299	$14,536	$19,318	$17,384
Total value of projects	$847,347	$877,983	$1,470,500	$3,195,830
Average value of project	$56,490	$46,210	$52,518	$51,739
Leverage (loans/project value)	32%	31%	37%	34%

Over the three-year period, the average value of a project was $51,739. This value includes the amount to be invested in assets, working capital, or other items related to the business. From this value the average leverage of the loans is 34 percent ($Loan/$Project). This leverage ratio indicates the relative importance of the loans. In other words, the loans account for nearly one third of the value of the projects.

Impact on business performance

The ultimate goal of the loans is to increase the profitability of the businesses. This impact usually comes from investing the loan funds in assets such as machinery or equipment, increasing labor, working capital, or technology. However, we do not count with profit information from the businesses. Instead, we will assess the impact of loans on business revenues.

All businesses that received loans also experienced an increase in reported revenues. In 2014, the 27 businesses with loans had additional revenues of $67,370, almost doubling the initial level of revenues (92% increase). By 2016, the average increase in revenues was about $17,000 (57% increase). On average, revenues grew 62 percent.

6. Increase in revenues (2014-2016)

Year	N (loans)	Average revenues before loan	Average revenues after loan	Average additional revenues created	% increase in revenues
2014	28	$72,872	$140,242	$67,370	92%
2015	29	$126,517	$183,036	$56,519	45%
2016	44	$30,358	$47,806	$17,448	57%
3-year average	-	$76,582	$123,695	$47,112	62%

When we compare the additional revenues with the value of loans, on average, every dollar borrowed from ADC generates $2.70 dollars in additional revenues.[3] This implies about $42,257 in additional revenues per loan.

Every dollar lent by ADC generates $2.70 in additional revenues

This return reaches $5 for new businesses

[3] Return on loans (ROL) = Average increase in revenues / Average value of loans. From Figures 5 and 6, ROL = $47,112/$17,384 = $2.70.

One factor determining the growth in revenues is the age of the business receiving the loan. For instance, new businesses tend to show a relatively higher increase in revenues since their initial revenues are low or zero. Startup businesses experience a growth in revenues of nearly $5.24 per each dollar borrowed from or with the help of ADC.

Impact on the community

The impact of the loans goes beyond the benefits accrued by the entrepreneurs. For instance, it can be presumed that a portion of the loans and the additional revenue and profit associated with the loans would be spent on other goods and services from local businesses. This increased economic activity is a multiple of the original value of the loans and includes additional revenues, salaries, and taxes from third party business providers and workers.

Another benefit for the community is the additional jobs directly generated from the investments made with the loans. We estimate that each loan provided or facilitated by ADC is associated with about 1.8 additional jobs created within the clients' businesses. With a total of 100 loans, about 180 new jobs were generated by ADC's clients between 2014 and 2016. These jobs imply approximately $288,000 in additional income and benefits for the employees.[4] As noted above, we can assume that most of this income was spent in the community to purchase goods and services and pay taxes, thus they contribute to the indirect benefits to the community generated by ADC.

[4] Assuming an hourly wage of $8, an average of .75 full time equivalent average for each new job, and benefits with value of about 25 percent of wages.

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