S&P Global Ratings

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BlueHub Loan Fund, Inc., Massachusetts; General Obligation

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Table Of Contents

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Credit Profile		
US$75.0 mil rev bnds (taxable sustainability bnds) ser 2020 dtd 01/23/2020		
Long Term Rating	A-/Stable	New
US$0.0 mil ICR due 12/31/2099		
Long Term Rating	A-/Stable	New

Rationale

S&P Global Ratings assigned its 'A-' issuer credit rating to BlueHub Loan Fund, Inc. (BHLF), Mass. At the same time, we assigned our 'A-' long-term rating to BHLF's series 2020 taxable sustainability bonds. The outlook is stable.

The rating reflects our view of BHLF's:

- Very strong profitability, as measured by a higher return on assets (ROA) and net interest margin (NIM) than other rated community development financial institutions (CDFIs), resulting from operating under a lean business model;
- Stable total equity ratio (total net assets over total assets) between fiscal years 2014 and 2018, even as its loan portfolio nearly doubled in size within the past two years, through controlling its costs of capital and with support from grant sources;
- Strong history of loan performance, evidenced by minimal-to-no nonperforming assets (NPAs) over the past five years; and
- Proactive management of its loan portfolio, with thorough underwriting guidelines and a strong internal culture around risk mitigation.

Partially offsetting these strengths, in our view, are the following weaknesses:

- A less capitalized lending program than other rated CDFIs, with a total equity ratio averaging 27.9% between fiscal years 2014 and 2018, and a weaker net equity-to-assets ratio of 7.7% in fiscal 2018, reflecting more limited coverage for unexpected market changes, funding delays, or revenue reductions, compared with CDFI median ratios of 36.1% and 12.0%, respectively;
- BHLF's relatively small geographic footprint, which could present challenges in overseeing loan performance and local-level information for its loans in market areas outside of the Northeast and Mid-Atlantic regions; and
- Exposure to a balance of unenhanced early-financing loans, although these are comparable with those of industry peers.

The series 2020 taxable sustainability bonds (expected par amount of $75 million), will be fixed-rate, maturing in 2030, and with interest-only payments until 2027. BHLF expects to use $74 million in bond proceeds to refinance previously issued fixed- and floating-rate debt obligations that were used to finance 33 loans, most of which were for affordable housing properties, commercial and manufacturing projects, or education facilities. About $1 million of bond proceeds will pay costs of issuance. The bonds are interest-only until 2027, and will mature in 2030.

The 2020 bonds are unsecured general obligations of BHLF, and are therefore supported by the corporation's credit pledge. The bonds are payable from all legally available revenue and assets of the corporation and are not secured by a reserve fund, mortgage lien, or security interest on or in any funds or other revenue or assets of BHLF.

Outlook

The stable outlook reflects S&P Global Ratings' opinion that BHLF's profitability and asset quality will remain strong over the next two years, as net assets remain consistent with recent years' performance. Based on our review of unaudited financials as of September 2019 and the fiscal 2020 budget, we believe BHLF's strategy of growth and expansion will result in a stronger net position and lower capital costs. This strategy is also expected to continue the strong track record of loan performance during the outlook period, attributable to BHLF's diligent portfolio monitoring and management's intention to maintain a similar composition of diverse loans. We consider BHLF's debt and loan portfolio management critical to its rating stability.

Downside scenario

Increases in loan balances outstanding, with loan characteristics consistent with those we analyzed as of June 2019, could result in our assumption of additional projected loan losses. Should growth in net assets prove insufficient to absorb these additional loan losses, our calculated net equity ratio could decline below levels consistent with this rating level, and could lead us to take a negative rating action. If BHLF were to experience a significant reduction in capital adequacy as a result of increased debt, weakening loan performance, or fewer net assets, this would demonstrate volatility and impede its capitalization and debt positions. This could also lead to a potential negative rating action.

Upside scenario

We could raise the rating or revise the outlook to positive if BHLF were to demonstrate consistent and steady growth in its net equity ratios compared with its peers, while maintaining very strong profitability and asset quality. Exceptional loan performance and the preservation of sufficient capital available to absorb potential loan losses, in conjunction with a strong balance sheet following this bond issue, could also result in our raising the rating or revising the outlook to positive. We would also expect upward movement if projects with early financing loans were to stabilize and begin generating cash flow, or if the net cash flow for permanent loans were to become stronger, potentially lowering our assumed loan losses.

Issuer Description

BHLF is a 501(c)(3) nonprofit corporation based in Boston, Massachusetts and was certified as a CDFI by the U.S. Department of the Treasury in 1997. It was initially formed in 1984 as Boston Community Loan Fund, Inc., with an initial mission to provide below-market-rate capital to community-based organizations to develop affordable housing. By 1994, this mission had expanded to include broader community development lending. In 1997, the organization changed its name to Boston Community Capital, Inc. to reflect an expanded portfolio of financing it could provide to various communities. Most recently, in 2018, Boston Community Capital became BlueHub Capital Inc., with the intention of embracing a "blue economy," which promotes creativity, innovation, and entrepreneurship as a route to the creation of a sustainable and inclusive economy. BHLF is an affiliate of BlueHub Capital, and remains its core line of business. BHLF operates with a staff of 12 full-time employees and receives supporting services from an additional 15 staff members from BlueHub Capital; all BlueHub Capital employees are based in the Boston headquarters office.

Since 1985, BHLF has invested more than $1.3 billion in support of organizations and businesses that benefit underserved communities. BHLF participates in a variety of programs that further its mission of helping to build healthy communities where low-income people live and work:

- Affordable Housing: Produce and preserve affordable housing, emphasizing deeply affordable, supportive, and elderly housing;
- Early Education and Child Care: Increase access for low-income families to high-quality early-education care and child care;
- Education: Increase access for low-income families to high-quality public charter schools and out-of-school learning opportunities;
- Community Health Care: Improve access to primary health care, dental care, and mental health care for underserved patients;
- Healthy Foods: Expand affordable healthy food options in low-wealth communities, creating jobs and transforming neighborhoods with commercial investments;
- Sustainability: Collaboration with BlueHub Energy to bring energy resilience and cost savings to low-income communities; and
- Commercial and Manufacturing: Renovate commercial real estate in disadvantaged neighborhoods to create job opportunities and stimulate additional investment.

Equity And Capital Adequacy

As part of BlueHub Capital's most recent five-year strategic plan that began in 2017, BHLF was tasked with doubling in size. As a result, its loan balance outstanding grew 99% between fiscal years 2016 and 2018, to $172.4 million, and $220 million by September 2019, with a focus on acquisition loans, construction lending, and permanent financing in existing and new geographic markets. Financing for this loan growth has come from loans payable from individual and institutional investors, unsecured bank lines of credit, loan participations, and permanent capital (including grants from the CDFI Fund and equity equivalent investments (EQ2s)).

During this period of loan growth, BHLF has managed to control its cost of capital, grow its net position, and maintain a relatively stable total equity ratio (total net assets over total assets). BHLF has received credit enhancements from the U.S. Department of Education to support lending in the charter-school sector, and grants from the Capital Magnet Fund to help finance affordable housing loans. Historically, BHLF had not received funds from these capital sources. In fiscal 2018, its total equity was about 28%, matching its five-year average. Based on our review of unaudited fiscal

2019 financials as of September 2019, as well as the fiscal 2020 budget, it appears BHLF's total equity ratio could remain stable over the next two years. We view this stability as a credit strength.

Our analysis places the highest emphasis on net equity or adjusted unrestricted net assets (UNA), after projected losses, because this indicates resources available to sustain operations during difficult circumstances; it also indicates BHLF' capacity to fund programs that further its mission.

We think BHLF's financial support is sufficient to warrant an 'A-' rating, which, in our view, reflects its overall asset quality, debt profile, liquidity, and sufficient net assets to cover potential losses at the 'A-' stress scenario. Using our commercial mortgage-backed-securities model, we assess the risk associated with BHLF's loan portfolio based on loan characteristics as of June 2019. About 47% of the BHLF's loan balance that was secured by real estate was for cash-flowing projects, and 36% contained an interest reserve as part of the loan agreement. We factor a loan's potential default during its lifetime into our loss assumptions.

We estimate credit enhancement required for its existing loans, as of June 2019, was approximately 27% at the 'A-' stress level. After application of our loan loss assumptions, BHLF's total net assets over total assets ratio of 28% as of fiscal 2018 is reduced to 7.7%. We believe BHLF has sufficient net assets to cover potential losses at this 'A-' stress scenario. This is below the median net equity-to-total assets ratio for other rated CDFIs, due partially to the relatively limited UNA available to absorb loan losses, compared with other CDFIs.

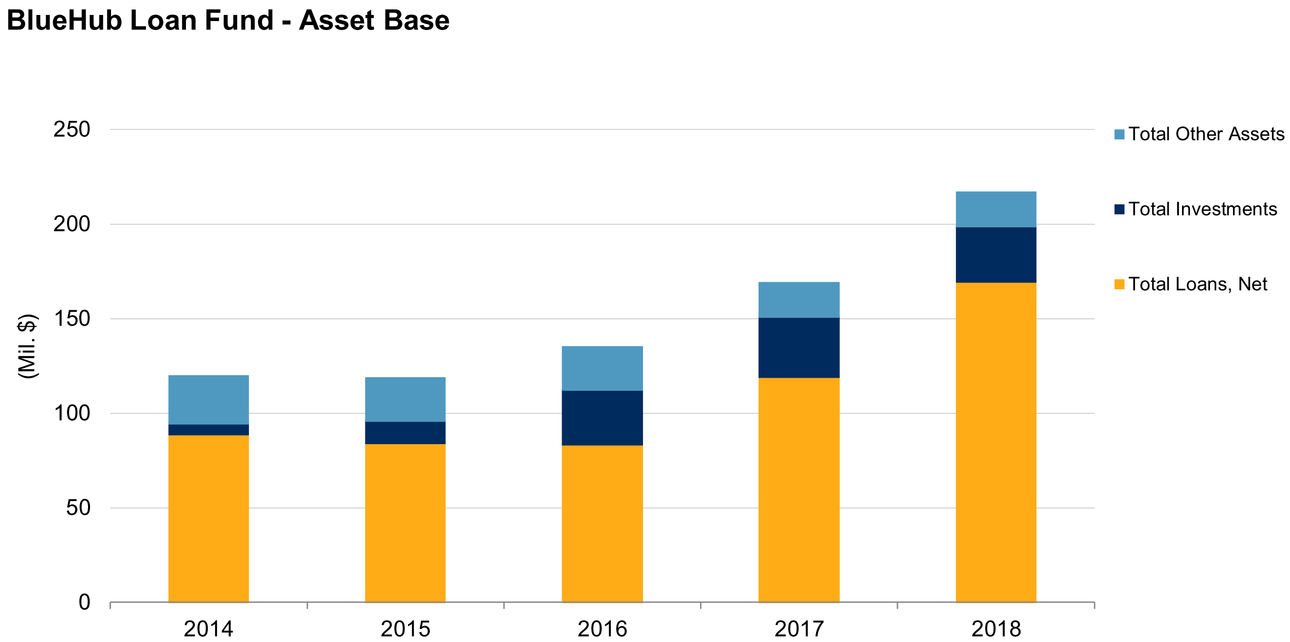
At the same time, BHLF maintains access to external liquidity. In fiscal 2019, BHLF had about $37.5 million in committed, and $15 million in outstanding, lines of credit, which were two- to three-year revolving facilities intended for short-term liquidity needs. Each line of credit carried a floating interest rate priced at LIBOR plus a range of 150-225 basis points.

Asset Quality

BHLF's strategic plan calls for the geographic expansion of lending activities to fill unmet capital needs in underserved markets. During this period of growth, BHLF has focused on six strategic impact areas: housing, education, health care, healthy food, economic development, and energy investment. As of June 30, 2019, about half of the loan balance outstanding was for projects based in Massachusetts, Connecticut, Rhode Island, or Maine, and 25% were located in New York or New Jersey. The remaining portfolio spanned 10 other states. The net loan portfolio reached $218.6 million by June 2019, a significant 162% increase since fiscal 2016.

At Dec. 31, 2018, about 78% of total assets were loans, up from 62% in fiscal 2016, a percentage we expect will increase over the next two years. The remaining assets include mostly short-term investments (see Chart 1). BHLF's annual lending target of $100 million, which it surpassed in fiscal 2018 and is expected to achieve in fiscal 2019, is up from the $42.6 million in closed loans in fiscal 2016, while reaching an expected high of 24 new borrowers in fiscal 2019.

Chart 1



BHLF has been more active in financing construction and permanent loans in recent years, more so than acquisition or predevelopment loans. Construction loans comprised approximately 38% of the total outstanding balance as of September 2019, most of which maintain an interest reserve, or upon completion of construction, will become cash-flowing and convert to amortizing, permanent financing. Permanent loans represented 32% of the loan balance as of September 2019, up from 16% in fiscal 2014. Many of these loans finance cash-flowing multifamily housing developments and community facilities (e.g., charter schools, health care centers). Credit enhancement from the U.S. Department of Education has helped support this increase in permanent loan financing. There has also been a shift to diversify asset classes to include more loans for education facilities (e.g., charter schools) and healthy food options. By September 2019, loans for housing projects totaled 40% of the balance outstanding, education-related facilities represented 27%, and commercial or manufacturing projects totaled 14%.

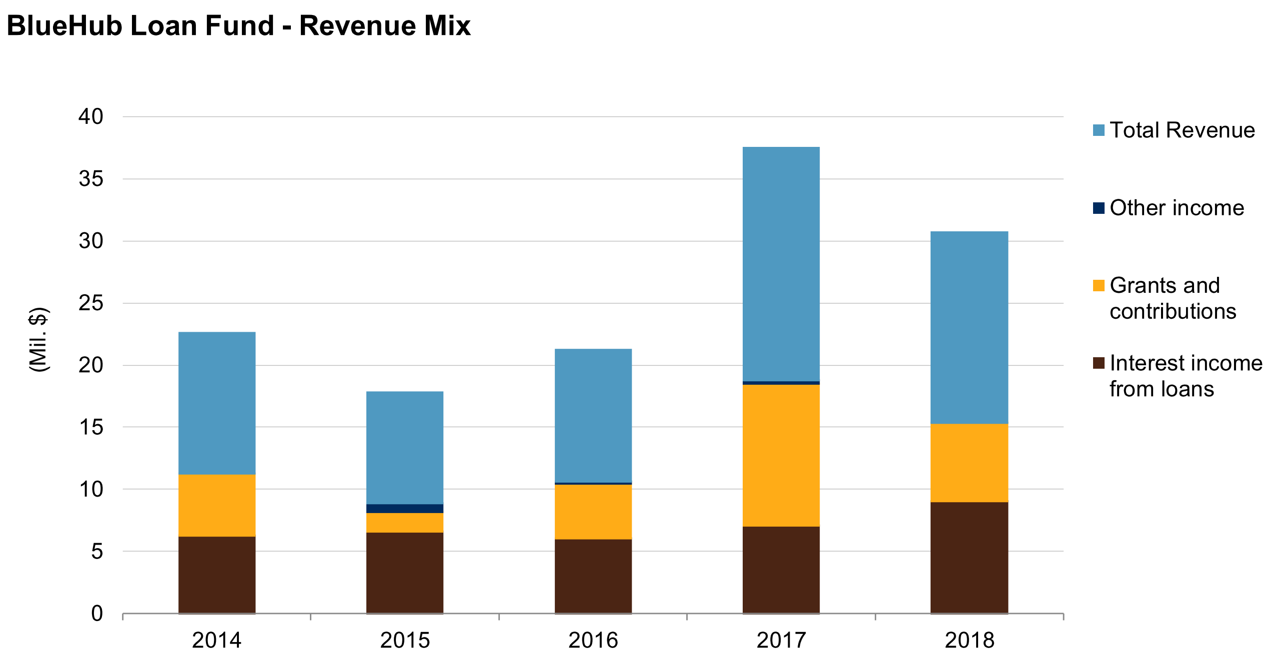
In our opinion, BHLF's loans perform strongly, with minimal-to-no NPAs over the past five years. While other rated CDFIs exhibit strong asset quality, with median NPAs of 0.7% of total loans, BHLF's portfolio's five-year average NPAs were an even stronger 0.01%, and 0.1% as of June 2019. Behind BHLF's loan performance is its active loan and portfolio management. This includes management reviews of weekly delinquency, maturity, and conversion date reports as well as quarterly portfolio reviews. Active loan monitoring involves annual reviews and site visits as needed, typically every three years. Staff also perform loan-level monitoring that involves high-touch relationships with borrowers, ongoing reviews of project progress, financial reports, and risk ratings (assigned at approval and reviewed over the life of the loan). Risk ratings drive the allowance for loan losses, based on a range of loan characteristics.

As loan performance has remained strong, and its portfolio has grown into new markets, BHLF's loan loss reserves have declined as a percent of total loans. In fiscal 2018, reserves were about 1.7% of total loans, trailing its five-year average of 3.6%, below the level of other rated CDFIs. We do not view BHLF's loan loss reserves as a credit weakness.

Operating Performance

BHLF has very strong profitability, in our opinion. Operating with a staff of 12 full-time employees and a loan portfolio that has grown by 84% during the past five years, to $172.4 million in fiscal 2018, BHLF keeps capital costs as low as possible and operates under a nimble, self-sufficient business model. This has led to a higher ROA and NIM than other rated CDFIs. BHLF's five-year ROA is 5.2%, more than twice the median ROA of 2.5% for other rated CDFIs. Interest income from loans increased by 45% between 2014 and 2018, with annual increases in all but one year. During these five years, BHLF's NIM averaged 3.6%, while the NIM for its loan business averaged 4.2%. At $9.1 million in fiscal 2018, interest income from loans was 59% of the $15.3 million in total revenue (see Chart 2).

Chart 2



BHLF's interest spread declined slightly in fiscal 2019 with increases on senior debt, particularly on variable debt indexed to LIBOR, and rate pressures on housing loans tied to projects funded through the Capital Magnet Fund grant. The series 2020 bonds are expected to lower BHLF's cost of funds as it replaces higher-cost, shorter-term debt from banks. BHLF has budgeted a savings of at least $500,000 in fiscal 2020. BHLF monitors the interest spread on loans both historically and forecast out at least 12 months. The target percentage to cover operating costs is between 2.5% and 3.0%. The cost of funds as of September 2019 was about 2.6%.

In our view, BHLF is less reliant on grants and contributions than other rated peers, and does not rely on grant income for operations. BHLF maintains a self-sufficient loan business, even without including revenue from grants and contributions. Interest income from loans and investments has covered total operating expenses for at least the past five years. We believe this mitigates, but does not eliminate, the risk of volatile grant revenue.

Debt Obligations

BHLF has managed its debt profile well, in our opinion. Net assets were near 41% of total debt in fiscal 2018, and its five-year average of 40%. While this is weaker than the median ratio for all other rated CDFIs (61%), about 18% of BHLF's debt outstanding ($27 million) was fully subordinate with indeterminate maturity dates in the form of EQ2s from local banks and institutions as of fiscal 2018. This debt typically carries an interest rate of 3%, with a 10-year rolling maturity date. Initial maturity dates automatically extend by one year at the end of each of the first five years of the loans' terms; thereafter, they are extended annually on their anniversary dates, indefinitely, provided the investor does not call the loan. These investments are fully subordinated to the right of payment of all other creditors.

Capital to support the lending activity of BHLF comes from four primary sources: investor funds lent to BHLF; bank debt, such as lines of credit; loan participations; and secondary market sales. Total debt outstanding rose 69% between fiscal 2014 and 2018, but the balance sheet's total equity has remained stable. BHLF has focused on matching the duration of assets with lending capital, managing interest rate risk, avoiding negative arbitrage, and maintaining flexible capital to meet borrowers' needs. For the loan fund, BlueHub Capital uses an internal tool, provided monthly, called the Portfolio/Liquidity Management Report to ensure appropriate matching of liabilities and assets. This tool is designed to identify in one report all of the information around liquidity, interest spread, and overall credit exposure.

Market Position: Strategy And Management

In our opinion, BlueHub's senior leadership has a clear vision, which is reflected in the organization's strategic plan. Implemented in 2017, the plan challenged BHLF in three particular areas, each aligned with the organization's broader goals:

- Grow lending to $100 million annually by 2021, focusing on six strategic impact areas: housing, education, health care, healthy food, economic development, and energy investment;
- Build a national lending footprint, expanding geographically to fill unmet capital needs in underserved markets; and
- Support innovation by BlueHub Capital affiliates to develop new strategies to improve the lives of low-income individuals and to strengthen communities.

As the CDFI lending arm of BlueHub Capital, BHLF concentrates on raising low-cost and flexible capital to lend in communities across the country. This concentration has led to a profitable and lean business model. Given the concentration of employees in its Boston office, and with it having no intentions of opening any satellite offices, BHLF relies on partners nationwide. As BHLF has expanded its loan portfolio beyond the New England region, staff works closely with trusted local partners (e.g., developers, local organizations and CDFIs, and real estate development consultants) in focused markets who know the landscape and support BHLF's management of loans from origination through repayment. We believe this presents some geographic limitations. While this partnership strategy has proven to work for BHLF, resulting in strong asset quality, there remains the potential for knowledge gaps in loan performance and local-level information.

We view BHLF's commitment to affordable housing and community development, in relation to its core values, mission, and overall strategy, as very strong. We base this on the financial ratios outlined above, and the effects of more than $1.3 billion deployed in low-income communities nationwide since 1985. This financing has supported:

- The creation or preservation of 23,500 units of affordable housing;
- The creation of 13,800 jobs;
- Health care services for more than 197,000 patients;
- Education and day care for more than 59,000 children; and
- Commercial real estate and community facilities totaling 5.9 million square feet, including healthy food retail businesses that serve more than 128,000 customers annually.

A 12-member board of directors, with an average tenure of service of more than 21 years, oversees BlueHub Capital. This includes the CEO of BlueHub Capital, the president of BHLF, and the president of BlueHub Managed Assets, all of whom are ex-officio members. To ensure that all affiliates are working toward shared financial and mission-driven goals, BlueHub Capital and each of its affiliates, including BHLF, have distinct boards of directors with identical members. The board represents a variety of business sectors and geographic locations. Directors are senior executives with experience at leading financial institutions and community organizations such as Bank of America, Citizens Bank, YouthBuild, Mercy Housing, Fannie Mae, and UNC Partners.

The loan committee has lending authority and oversight over BHLF. The eleven-member committee is chaired by a board member and includes both board members and non-board members with real estate, community development, nonprofit management, and lending expertise.

Table 1

BlueHub Loan Fund--Financial Ratio Analysis

FY Ending: 12/31	2014	2015	2016	2017	2018
Asset Quality (%)					
Total assets ($)	$119,486,939	$118,291,861	$134,792,526	$168,847,195	$216,547,675
NPAs/total loans + REO	0.0%	0.0%	0.0%	0.0%	0.0%
Loan loss reserves/total loans	5.4%	4.8%	3.9%	2.4%	1.7%
Liquidity (%)					
Total loans/total assets	74.4%	71.1%	61.9%	70.5%	78.3%
Short-term investments/total assets	4.7%	10.0%	21.5%	18.9%	13.5%
Other assets/total assets	20.9%	18.8%	16.6%	10.6%	8.2%
Profitability (%)					
Return on average assets	5.2%	3.1%	4.5%	8.7%	4.5%
Return on assets before loan loss prov. & extraordinary items	5.2%	3.1%	4.2%	7.9%	4.0%
Return on average equity	23.7%	12.0%	15.9%	29.4%	15.6%

Table 1

BlueHub Loan Fund--Financial Ratio Analysis (cont.)

FY Ending: 12/31	2014	2015	2016	2017	2018
Net interest margin	3.6%	4.2%	3.4%	3.3%	3.4%
Net interest margin (loans)	3.9%	4.6%	4.3%	4.3%	4.1%
Capitalization & Leverage (%)					
Total equity/total assets	24.4%	27.7%	28.6%	30.7%	28.0%
Net equity/total assets					7.7%
Total equity + reserves/total loans	38.1%	43.8%	50.0%	45.9%	37.4%
Total equity/total debt	33.1%	40.2%	41.0%	46.0%	40.8%
Net equity/total debt					11.3%

NPA--Non-performing assets. REO--Real estate owned.