Craft3 Site Visit Summary Report

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Visit Dates: August 5-August 10, 2019

Interviewees:

Jeff Baker, Business Lender, Craft3 (Bend, OR)
Bruce Brooks, Senior Vice President, General Counsel, Craft3 (Seattle, WA)
Natalie Charley, Executive Director, Taala Fund (Seattle, WA)
Ed Davis, Indian Country Regional Strategist, Craft3 (Seattle, WA)
Mike Dickerson, Innovation and Evaluation Center, Craft3 (Astoria, OR)
Brandon Dorman, Learning and Evaluation Coordinator, Craft3 (Portland, OR)
Saif Hakim, Senior Business Lender, Craft3 (Seattle, WA)
Maggie Kirby, Senior Vice President, Development Director, Craft3 (Bend, OR)
Jamie Lee, Director of Community Initiatives, SCIDpda (Seattle, WA)
Roger Lee, CEO, Economic Development for Central Oregon (Bend, OR)
Tawny Reader, Assistant Vice President, Consumer Product Manager, Craft3 (Bend, OR)
Carl Seip, Vice President, Communications and External Affairs, Craft3 (Seattle, WA)
Turner Waskom, Senior Vice President, Commercial Lending Director, Craft3 (Bend, OR)
Che Wong, Business Development Specialist, Craft3 (Seattle, WA)
Adam Zimmerman, President & CEO, Craft3 (Portland, OR)

Background

- Shorebank Enterprise Pacific, an affiliate of the Shorebank Corporation out of Chicago IL, was founded in 1995 in Ilwaco, WA as a partnership with Ecotrust, a Portland-based nonprofit "working to create, social, economic, and environmental benefit across the Pacific Northwest." During the next ten years, Shorebank Enterprise Pacific opened offices in Astoria and Coos Bay in Oregon and Port Angeles in Washington, with a presence also in Port Townsend and Forks, and invested $30 million as a nonprofit community development financial institution (CDFI) in businesses and communities in coastal (mainly rural) Washington and Oregon.
- In 2006, Shorebank Enterprise Pacific merged with another CDFI, Cascadia Revolving Fund, which was founded in 1985 and had loaned over $35 million to entrepreneurs and nonprofits from their offices in Seattle, WA, and Portland and Bend OR. The new entity, Enterprise Cascadia, under the leadership of John Berdes, set out to tackle issues affecting the region's triple bottom line: social, economic, and environmental well-being, with a loan fund of $70 million making it the largest CDFI in the Pacific Northwest. In 2011, the organization rebranded itself as Craft3.
- Rural-urban connections are part of Craft3's DNA. Shorebank Corporation was an urban venture that sought to replicate its learning from investing in poor urban neighborhoods to rural regions in Arkansas (Southern Bancorp, 1986) and Michigan Upper Peninsula (Northern Initiatives, 1992), before entering the Washington and Oregon market (1995). Enterprise Cascadia was a merger of two CDFIs – a rural (Shorebank Enterprise Pacific) and an urban (Cascadia Revolving Loan Fund). Today, Craft3 describes its work as supporting strategies that strengthen regions and better link rural and urban communities of the Pacific Northwest.

Organization

- Craft3 is a nonprofit (501(c)(3)) community development financial institution that is Aeris-rated and certified by the U.S. Treasury. It has an 11-member Board of Directors (4 minority, 6 women) chaired by a former City Manager of Astoria, OR. There are 65 staff working from eight regional locations. By the end of December 2018, Craft3 had cumulatively made 6,885 loans (1,283 commercial and 5,602 consumer) to the value of over $510 million (83 percent commercial). Craft3's total assets are over $148 million, capitalized by banks (33.5 percent), state and local governments (23.1 percent), foundations (14.7 percent), the Federal government (11.6 percent), community impact investors (individuals)(10 percent), non-depository financial institutions (6.1 percent) and religious orders (1 percent).
- Craft3 has two product portfolios. The commercial portfolio, which accounts for 74 percent of the total, comprises business loans for working capital, inventory, equipment, and commercial real estate, as well as loans to nonprofits for real estate acquisition and development, and loans for clean energy and conservation projects. The consumer portfolio (17 percent of the total) is designed for a wide range of borrowers including low-income households and funds home energy and clean water loans (repair and replacement of failing septic systems). New products include manufactured home replacement and funding for accessory dwelling units.
- Craft3 is guided by its 2018-2022 Strategic Plan:
  > "Over the last five years Craft3 achieved regional scale and put feet on the ground in regional centers throughout Oregon and Washington. Our approach for the 2018–2022 Strategic Plan is based on deepening our impact and focusing our resources and energy on creating enhanced outcomes from our lending. Our priorities will emphasize getting better over getting bigger." (p.5)
- Each regional office has (or will have) an outreach strategy with a five-year time horizon, as does Craft3's work in Indian Country, in the Clean Tech and Food and Agriculture sectors and for community facilities. With the intention of connecting the dots between the Strategic Plan, the outreach plans, and annual progress reports, Craft3's Innovation and Evaluation Center is charged with implementing a learning and evaluation strategy to continuously improve the impact and efficiency of the organization's strategies, tactics, products and processes.

Context

- Two of Craft3's offices are in the major metropolitan centers of Seattle and Portland. Seattle has a city population of around 756,000 in a metropolitan area of nearly four million; Portland's city population is 667,000 in a metropolitan area of around 2.5 million. They have advanced economies based on technology, aerospace (Seattle), logistics (shipping and ports), manufacturing, financial and health services. Both areas struggle with gentrification pressures pushing low and moderate-income people to the suburbs, income and wealth disparities for communities of color, high cost of housing and homelessness, and service provision for low-income people. Much or most of their population growth is coming from immigrants and people of color.
- On the other hand, four of Craft3's offices are in small cities or towns (Astoria, Walla Walla, Klamath Falls, and Port Angeles) with populations between roughly 10,000 – 35,000, facing very different economic and social challenges. All four are historically natural resource-based economies (timber, fishing, agriculture) which are in different stages of reinventing their economies. The other two offices are in Spokane (population, 217,000) and Bend (98,000) are mid-sized cities surrounded by agricultural lands or outdoor recreation areas. Craft3 can be a "big fish" in a community the size of Astoria. It is much harder to exert comparable influence on the economies of Portland or Seattle.

- The interviews revealed some of the challenges of working across state lines, specifically the differences in attitudes of the state agencies in Washington and Oregon. Washington, which is almost twice as populous as Oregon, has more money and resources and a greater willingness to try new approaches despite the enormous wealth gap between Seattle and the rest of the state. Oregon, on the other hand, because of its smaller size and regional inequities (east and west of the Cascades), is observed to be more parochial, turf conscious, and "squeezes the life out of big ideas." To the extent that this is true, Craft3 has been challenged in expanding programs developed in one state into the other.
- Another feature of the Pacific Northwest that has importance to Craft3's operations is that there are 38 federally recognized Tribes in the region (29 in WA, 9 in OR), owning 4.2 million acres (4 percent of the total land area) with some 88,000 enrolled members. There are 11 Native community development financial institutions.

Collaboration

- Craft3 is primarily a lending institution for which collaboration and partnership are essential given its geographical spread across two states and its active engagement in social, economic, and environmental issues. It relies on collaborative relations to:
  - Foster trust and goodwill at the community and state levels to identify mission-supporting lending opportunities;
  - Gather community support from local governments, tribes, businesses and nonprofits;
  - Generate referrals from banks and other financial institutions;
  - Obtain access to sources of capital from banks, federal and state governments, and foundations; and
  - Pursue broad regional goals, including bridging the rural-urban divide, with like-minded organizations.
- Examples of collaboration include:
  - Craft3 has developed a longstanding and effective relationship with the State of Washington. This began with Craft3 creating a small business credit fund capitalized by $9 million from the State's Small Business Credit program, $2 million from Craft3, and over $30 million from Wells Fargo and other banks. Total lending under this initiative was in the order of $30-40 million.
  - Working with Oregon Department of Energy, using federal, Recovery Act funds, Craft3 developed a home energy product. Craft3 now partners with the Energy Trust of Oregon, utility companies, and community organizations to provide home energy loans repaid through the utility bill. The product became available in Washington supported by state funding a few years later. To date, 4,000 families in Washington and Oregon have taken loans amounting to $50 million to reduce energy use and create local jobs.
  - Craft3 entered into a memorandum of understanding with 22 Washington counties to use state funds to repair and replace septic systems to clean groundwater and waterways that flow into shellfish harvest areas. 1,500 loans have been made totaling $33 million, keeping 1,400 families (40 percent low income) in their homes.
  - Craft3 partnered with the Shoalwater Bay Tribe in southwest Washington to make the one of the first-in-the-nation New Markets Tax Credit investments in Indian Country for a wellness center. The facility offers medical, dental, drug, and alcohol counseling and mental health services in an area remote from adequate medical care.
- An important feature of Craft3's approach is use of outreach strategies for each of the eight places in which it has a presence and Indian Country. These are assessments of the sub-regional economic status and trends, the small business financing ecosystem, and key community stakeholders and

potential partners. The result is a set of priority areas for engagement, a sub-regional vision for Craft3, outcomes, tactics, and metrics. These strategies are the basis for developing or strengthening collaboration with the community and region.

- The model for these strategies is Astoria OR. Craft3 began work in 1997 in the city of Astoria with two projects. One was a real estate initiative to redevelop former fairgrounds and a defunct plywood mill for mixed-income housing, the other was focused on interventions in the seafood industry. The redevelopment project was a critical part of the City's revitalization plans for downtown Astoria, which not only led to housing and other development (such as an aquatic center, a movie theater, medical facilities, commercial space, and a park) but a long-term and still continuing relationship with the City on other real estate projects. The seafood project was a partnership with the Oregon State University's Seafood Lab and the Coastal Oregon Marine Experiment Station to create the Community Seafood Initiative to support new product development, value-added processing and innovation in the seafood industry. Craft3's work in Astoria combines a place strategy, investing in the economic center of a rural region, and a natural resources strategy that had regional impact across state lines on the Lower Columbia River.

Rural-Urban Relationships

- Rural-urban relationships are core to Craft3's history and mission and essential for getting to scale and achieving regional impact. The Astoria project was an early example of combining place and sector investments to connect rural and urban economies and communities. A Craft3 strategy document from 2012 on regional resilience notes that the organization works in regions that frequently have rural and urban places near each other. Such places, it argues, mutually contribute to regional resilience through a wide range of economic exchanges.
- The 2018-2022 introduces a subtle change in emphasis termed 'regional amplification.' This refers to translating innovation and experience in specific places and sectors into opportunities to amplify Craft3's work throughout the region. This implies both a strong emphasis on learning from what works, whether originating from urban or rural places, and ensuring a balance of activities and investments across Craft3's regional footprint.
- Of the 112 current loans, there is an equal split between Seattle/Portland and the rest of the two states. Much of the back-office functions are in the two cities to make lending more efficient in the rural locations. A point made many times in the interviews was that keeping a rural-urban balance across Craft3's activities requires intentionality through its mission, organizational structure and operations, and strategies and priorities.
- Examples of intentional efforts to ensure that Craft3 maintains this balance, include:
  - Craft3 has eight sub-regional offices: Olympic Peninsula (Port Angeles, WA), Eastern Washington (Spokane, WA), Lower Columbia (Astoria, WA), Puget Sound (Seattle, WA), Mid-Columbia Basin (Walla Walla, WA), Central Oregon (Bend, OR), Columbia-Willamette (Portland, OR), and Southern Oregon (Klamath Falls, OR). There is no headquarters, with senior management located across the network offices (Commercial Lending Director, Bend; Consumer Lending Director, Seattle; Development Director, Bend; Innovation & Evaluation Center, Astoria; IT Director, Seattle; Chief Financial Officer, Portland; President & CEO, Portland); Chief Operating Officer, Port Angeles.) This geographic distribution of staff and functions helps to promote a network rather than a hub-and-spoke, center-periphery structure, which would normally favor the urban centers.
  - Craft3 identifies capital needs along three dimensions – people, place, and sector – which tends to preclude hard-and-fast distinctions between rural and urban. Priority is given to underserved populations, including entrepreneurs of color, women, immigrants, and veterans. Craft3's focus

on places is supported by outreach strategies in each of eight sub-regions), and its work in sectors is focused on clean energy, food and agriculture, and community facilities.

Equity

- Equity, collaboration, and regionalism are interconnected and reinforcing components of Craft3's strategies and operations. The following examples illustrate its approach to addressing barriers to capital and knowledge faced by minority and under-served businesses and communities in city neighborhoods and in Indian Country.
- **Minority Business Development.** Craft3 Business Development Specialist, Che Wong is working in King County building long-run relationships and understanding community needs for capital. Her focus is on nine neighborhoods, mainly in Seattle, where there are barriers to entrepreneurship for minority residents. She is developing a simplified loan application process and finding partners to provide technical assistance and training. Craft3's intention is, once the new process has been tested, to replicate or adapt it in other locations to make access easier for rural and minority entrepreneurs.
- Craft3 partners with the University of Washington School of Business, the Minority Business Development Agency, and the Northwest Mountain Minority Supplier Development Council, with funding from the Chase Foundation and Wells Fargo, to provide training and capital to minority businesses in selected Seattle and King County neighborhoods. The goal is to connect new minority businesses to buyers and to each other and currently 60 businesses organized in two tracks, food and beverage and clean energy, are in the program.
- The combination of the simplified loan application process and targeted technical assistance is intended to bring more potential minority borrowers through the door while reducing lending risk but rolling this approach in the more rural sub-regions will be challenged by lack of technical assistance capacity.
- **Sharia-Compliant Lending.** Sharia Law regards the practice of paying interest on loans as usury. This presents challenges for obtaining financing from the mainstream financial system. Craft3 worked with the Islamic community to find a way to fund the creation of a mosque in Seattle that would be Sharia compliant. This entailed a Craft3 LLC purchasing a commercial property for conversion to a mosque, of which Craft3 owned 70 percent and the partners 30 percent, with the partners making quarterly payments of rent and dividends until they own the property.
- **Lending in Indian Country.** Lending to businesses on the reservations is made more difficult as land cannot be used as collateral (held in trust by the Tribes, not by individuals) and there is limited technical assistance capacity. Nevertheless, Craft3 has invested $18 million in Indian Country, and is now managing a recent $50 million New Markets Tax Credit allocation, a proportion of which will also be targeted at projects in Indian Country. The eventual aim is to build the capacity of Native Americans to build their own capital and control their own investment decisions. There are five Native CDFIs in the region and these have established a peer learning group through which Craft3 provides back office services, loan processes and documentation, and mentoring and coaching. According to one interviewee, Craft3 is regarded by the Tribes as trustworthy and business-oriented, operating as a peer within a network of tribes.

Commentary

- Craft3 shows how regional, collaborative, and equitable sensibilities guide its activities as a high-performing community development financial institution. These are evident in its overarching and sub-regional strategies, its collaboration with state agencies, tribes, and local communities, and the development of new products. They are also reflected in its performance metrics and in its management structure and operations.

- A study recently published by the Aspen Institute's Community Strategies Group highlights the importance of certain types of rural and regional intermediaries, known as "rural development hubs." A number of criteria are proposed, including regional thinking and action, deep knowledge and understanding of their region, a long-term view and commitment, a bridge across issues and silos, systems thinking and efforts to address gaps, creation of structures, products and tools for effective solutions, collaboration, spanning local, state, and national connections, innovation and adaptability, and willingness to tolerate risks. All of these describe well the approach and track record of Craft3.
- 'Intentionality' is a key word for describing Craft3. Bridging the rural-urban divide, working collaboratively, and tackling social and economic inequities were baked in from the beginning, and every new development is assessed according to these principles. For example, Craft3's Strategy-Risk-Complexity Matrix is a tool used to guide commercial investment and lending decisions. It requires projects to be assessed firstly according to the extent to which they align with sub-regional (place-based) or sectoral plans and will lead to measurable outputs in terms of under-represented populations and businesses, as well as other social, economic, and environmental metrics. Then, the projects are assessed according a set of indicators of financial risk and project complexity.
- Now with more than $150 million of assets under management, Craft3 can be said to have achieved significant scale in its operations. Leadership have indicated that they have a goal to grow to $500 million in assets within the same geographical footprint in order to have real regional impact. To date, impact through growth has been balanced with an essentially bottom-up approach from the sub-regional offices and outreach strategies to the varied needs of communities and businesses across the Pacific Northwest.
- Craft3's unusual distributed organizational structure, with its eight sub-regional offices and no headquarters, is maintained through the extensive use of communications technology, a largely distributed leadership across the offices, an embedded culture and common language, and a powerful mission of getting capital to where it is most needed.
- Craft3's mission can only be achieved through effective collaboration with financial institutions, businesses, governments, foundations, and communities, and this is only possible through building trust and confidence over the long haul. Trust and confidence are based on competence and performance, and on developing relationships through the sub-regional offices and outreach strategies. Nowhere is this more important than in Indian Country and Craft3 has responded by having a targeted outreach strategy led by an on-staff tribal leader and businessman to work with Native CDFIs across the region.
- Knowledge transfer across the organization happens organically but is now being formalized through the Innovation and Evaluation Center and the work underway to integrate the various strategies and plans. The development work in Seattle neighborhoods to simplify lending processes and support minority entrepreneurship is fully expected to be applied in some form to the other sub-regions.
- Craft3 will be hard to replicate as it is born out of its geographical context and the vision of its founders and has had 25 years of intentional learning and development to bring it to its current state. But there are principles and approaches referred to above that can be applied in other contexts.
- One challenge that faces Craft3 as it looks forward is how to engage with state (and Federal) policy insofar as it impacts the social, economic, and environmental well-being of the region. Policy engagement requires building alliances and coalitions with advocacy groups, many of which are

Seattle- or Portland-based and liberal leaning. These are regarded with suspicion in rural communities which tend to be more conservative. Craft3 must pick its alliances carefully to ensure that it does not lose its credibility with its rural partners and customers. The cap and trade proposals in Oregon showed how differing perspectives among rural and urban actors can be exploited for party political gain. To date, Craft3's approach has been "to show up, be patient, provide expertise when asked for, and keep strengthening regional networks."

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