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Economic Development Revolving Loan Funds (ED-RLFs)

Revolving loan funds (RLFs) are instruments frequently used to finance water, wastewater, infrastructure, disaster recovery, and community development activities. RLFs can also be used for economic development purposes. Federally funded economic development RLFs (ED-RLFs) are one of many tools that public agencies and non-profit organizations use to make loans to finance small business growth, deploy capital to underserved markets, and incentivize development activity. The main advantage of using an RLF compared to other program design options is that the RLF can be configured in a way to be "self-replenishing," thereby reducing the need for annual appropriations or up-front federal credit subsidies. This In Focus provides an overview of how ED-RLFs work, a summary of federal support for ED-RLFs, and a brief review of current issues.

How Does an ED-RLF Work?

Initial funding for the ED-RLF capital base and administrative expenses may come from a variety of sources, such as government agencies, foundations, or private financial markets. Federal programs support ED-RLFs by providing grants or loans to capitalize the fund and cover administrative expenses. The initial funds can be combined with additional capital from other public and private sources. For comparison, some researchers note that banks and other financial institutions may use deposit accounts to capitalize loan funds. The repayment of principal, interest payments, and fees replenish RLFs so that future loans can be made to eligible borrowers and the loan fund can eventually be sustained or "revolved" without subsidy.

ED-RLFs borrowers include for-profit businesses, non-profit organizations, or government entities. ED-RLFs are often designed to target businesses in specific industries, geographic areas, or distressed communities, or to target the unmet needs of borrowers for products and services such as micro-loans or gap financing. ED-RLFs are also designed to finance development initiatives, such as infrastructure and revitalization projects sponsored by local government or other entities.

Many ED-RLFs report that they create some form of direct or indirect economic benefit to the region served. Directly, the ED-RLFs may increase the number of jobs created or retained, businesses expanded, or business startups created. Indirectly, ED-RLFs that finance public infrastructure or community development projects facilitate growth by supporting entrepreneurs, encouraging investment, and improving the conditions that expand facilities or amenities. The purpose of ED-RLFs typically is to supplement—not replace—conventional lending activity where business and development credit needs are not fully addressed. ED-RLF programs can provide credit to businesses and markets that may be underserved by commercial lenders, including small or nontraditional businesses and minority-owned businesses. Participating in an ED-RLF program may help small or new businesses build credit and receive additional services, like technical assistance or business coaching. Some ED-RLFs serve businesses that need gap financing or micro-loans that may be unavailable from traditional banks. As a development tool, ED-RLFs can often be sustained without requiring ongoing grant support because they have the capacity to grow over time as funds "revolve" and ED-RLF administrators collect interest and loan repayments.

Issues and Considerations Related to RLFs

There are limitations and challenges associated with the creation, expansion, and maintenance of RLFs. Both borrowers and intermediaries may need technical assistance and "hand-holding" to get started and to remain sustainable. Thus, ED-RLFs might need to be paired with technical assistance to borrowers (often at an additional cost to the funder, lender, or borrower) to promote maximum effectiveness of the fund's proceeds. Loan losses are a risk to ED-RLFs and may decrease the capital base over time. Interest rates and fees have to be sufficient to cover loan losses, administrative expenses, and inflation. ED-RLF administrators must balance the demand for services and the need to meet social goals while also assessing and managing risk. According to some researchers, the demand for ED-RLF loans can be episodic and depend on economic factors that are outside the control of ED-RLF administrators at the local, state, and regional level. High-performing ED-RLFs may need additional funds to recapitalize the fund when an ED-RLF has an active base of borrowers. ED-RLFs that receive federal support may face constraints related to program regulations. Reviewing the performance of ED-RLF programs is challenging because of insufficient data and other limitations.

Federal Programs That Support ED-RLFs

Table 1 provides a summary of selected federal programs that support ED-RLFs. The terms, eligibility requirements, and other conditions of federally-supported ED-RLFs vary based on the agency's program objectives and statutory requirements. The federal agency's regulations may specify that the ED-RLF programs or loans contribute matching funds or meet other requirements. Some ED-RLFs are administered by the federal agency directly; others are administered by an intermediary. ED-RLF intermediaries include local governments, non-profit organizations, utilities, universities, and economic development agencies, including economic development districts and councils of governments. Some ED-RLF programs, such as the ones supported by the Appalachian Regional Commission and EDA, are awarded through existing grant programs with specific guidelines for the use of funds as ED-RLFs. Through the Department of Housing and Urban Development's (HUD's) Community Development Block Grant (CDBG) program, grantees may opt to use CDBG funds to capitalize an ED-RLF. The Department of Agriculture programs offer stand-alone RLF programs designed for targeted lending activities or specific types of rural borrowers. The Department of the Treasury, Community Development Financial Institutions (CDFI) Fund's Financial Assistance awards program and its Small Business Credit Initiative (SBCI) program (which is no longer providing states with additional funding) are not included in this summary. Both offer or formerly offered loan or guarantee programs for businesses—usually through intermediaries such as community banks, CDFIs, and state economic development agencies.

The ED-RLFs described above often complement the business capital provided by financial institutions, the Small Business Administration, and Treasury programs. For more information, see CRS Report RL33243, *Small Business Administration: A Primer on Programs and Funding*.

Table 1. Summary of Selected Federal Programs That Support the Creation and Operation of ED-RLFs

Federal Program (CFDA No.[a])	Administering Federal Agency/Authorizing Statute	Brief Description
Economic Adjustment Assistance (EAA RLF) (11.307)	Department of Commerce, Economic Development Administration (EDA) Public Works and Economic Development Act of 1965, as amended, Section 209 (42 U.S.C. 3149)	EAA grant funds can be used to establish an RLF to make loans to businesses that cannot obtain traditional bank financing and to governmental entities for public infrastructure. The loans enable small businesses to expand and create and maintain jobs. EAA RLF loan programs must leverage private investment.
Community Development Block Grants (CDBG) (14.218)	Department of Housing and Urban Development Housing and Community Development Act of 1974, Title I (42 U.S.C 5301-5321)	CDBG funding may be used for grants or loans, including ED-RLFs. The award process is established by each state and entitlement community. Administration of ED-RLF funds must be consistent with rules governing the federal CDBG program, including the ability to meet one of HUD's National Objectives, and the grantee's Consolidated Plan.
Appalachian Regional Commission (ARC) Business Development RLF Grants (23.001)	Appalachian Regional Commission Appalachian Regional Development Act of 1965 (40 U.S.C. 14101-14704)	ARC provides grants to eligible recipients, which include states, local development districts, and other non-profit multicounty organizations to operate a lending program to support the creation and retention of private-sector jobs. Eligible borrowers include private, for-profit firms that do business within the Appalachian Region and government entities. Loans using ARC RLF sources may not be made in ARC-designated attainment counties.
Rural Economic Development Grant Program (REDG RLF) (10.854)	U.S. Department of Agriculture (USDA), Rural Business-Cooperative Service Rural Electrification Act of 1936, as amended, Title III (7 U.S.C. 930-940c)	USDA provides grants to qualified intermediaries for the purpose of establishing a RLF. Grants require a 20% match from an intermediary. The ultimate recipients repay the intermediary directly. The program serves rural areas with populations of 50,000 or fewer. Loans made from the RLF to the ultimate recipient may cover up to 80% of the project's cost.
Intermediary Relending Program (IRP RLF) (10.767)	USDA Rural Business-Cooperative Service Consolidated Farm and Rural Development Act, Section 310H (7 U.S.C. 1936b)	The IRP provides low-interest loans at 1% to intermediaries that re-lend to businesses to improve economic conditions and create jobs in rural communities. Ultimate recipients may be individuals, public or private organizations or other legal entities in rural areas. Funds loaned to the ultimate recipient by an intermediary must not exceed 75% of the cost of the ultimate recipient's project.
Rural Business Development Grants (RBDG RLF) (10.351)	USDA Rural Business-Cooperative Service Consolidated Farm and Rural Development Act, Section 310B (7 U.S.C. 1932)	The RBDG is designed to provide technical assistance and training for small rural businesses; i.e., fewer than 50 new workers and less than $1 million in gross revenue. Capitalization of RLFs is one of several categories of eligible activities that may be funded by the program. RBDG funds must be used for projects that benefit rural areas or towns with populations of 50,000 or fewer.
Rural Microentrepreneur Assistance Program (RMAP) (10.870)	USDA Rural Business-Cooperative Service Consolidated Farm and Rural Development Act, Section 379E (7 U.S.C. 2008s)	The RMAP provides loans and grants to Microenterprise Development Organizations (MDO) to help launch and grow microenterprises and provide training and technical assistance to microloan borrowers and microentrepreneurs. The program's loan element provides loans of $50,000 to $500,000 for establishing a microloan RLF, managed by the MDO. MDOs may make microloans for qualified business activities and expenses. This program serves rural areas with populations of 50,000 or fewer.

Source: Compiled by CRS based on information from agencies, including program regulations.

a. CFDA No. refers to the Catalog of Federal Domestic Assistance, a searchable database of federal domestic assistance programs. Each program is identified by name and a five-digit number.

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