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Community investing in peril?

SJF Ventures was recognized for helping create jobs in low-income areas. Now it may face federal budget cuts.

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SJF Ventures, an investment firm with offices in Philadelphia and Durham, N.C., garnered an unusual trifecta last month at the annual conference of the Community Development Venture Capital Alliance.

One of SJF's founders, David Kirkpatrick, was honored for innovation; one of its portfolio companies, HDS Cosmetics Lab Inc., for its performance; and one of its investors, Citibank, for its commitment to markets often underserved by banks.

The alliance is an industry association of funds that invest in small, unglamorous, job-producing businesses in low-income neighborhoods.

But if budget cuts proposed by the Bush administration and bank regulatory changes go through, fund-raising could become harder for member firms such as SJF that depend in large part on banks and federal funds for their activities.

So during the two days of the alliance's conference in Arlington, Va., Dan Hoversten, who heads SJF's Philadelphia operations, accepted one of the awards one afternoon - then spent the next day lobbying members of Congress.

The message: Reject the program cuts and prevent the potential retreat of another key source of funds: money banks contribute to fulfill their obligations under the federal Community Reinvestment Act.

Rule changes being considered by the Federal Reserve and other banking regulators could reduce pressure on banks to commit money toward business ventures in distressed neighborhoods, Hoversten and others fear. Some banks, though not Citibank, have resented the requirement.

The lobbying by Hoversten and other participants at the conference was unusual, he said. The alliance does not even meet routinely in the Washington area.

Citing efficiency, the Bush administration proposed to consolidate and cut the budgets of 18 federal programs that assist small businesses and community economic development.

The consolidation would reduce spending from \$5.31 billion this year to \$3.71 billion next year, according to a Commerce Department summary. The "unified" program would "better target assistance" and simplify access to the federal system, Commerce says.

For instance, the administration has asked Congress to appropriate \$8 million for the Community Development Financial Institutions Fund, which last year had \$80 million.

Since its creation in 1994, the fund has distributed more than \$500 million among small financial institutions, including SJF, that serve low-income communities.

Although the outcome of the proposed budget cuts and Reinvestment Act changes is unclear, "it's certainly something to be concerned about," said Bonny Moellenbrock, finance director at SJF in its Durham office.

Two-thirds of SJF's investment funds come from two sources: banks fulfilling their Reinvestment Act obligations and federal programs, including CDFI.

Each of these dollars draws several more in private investment, Moellenbrock noted.

The money given away is expected to bring financial returns, Kerwin Tesdell, alliance president, said.

"We use markets, which Republicans think highly of, to accomplish things that Democrats traditionally have been concerned about," Tesdell said.

After half a dozen years of investing, SJF is raising its return expectations from around 10 percent to "more of a market rate of 12 percent to 15 percent," Hoversten said.

"We don't want to invest in companies that just promise to create jobs. They must also show a good financial reason for us to invest," he said.

Not all of its ventures have panned out. It invested \$709,000 in the former Allegheny Child Care Academy, a chain of urban day-care centers that recently emerged from bankruptcy reorganization as Brightside Academy. "We didn't get totally wiped out," Hoversten said.

Still, SJF portfolio companies have won the community venture-capital industry's recognition two years in a row.

HDS, a maker of skin-care products in Yonkers, N.Y., increased its workforce from 75 to 135 during the 2 1/2 years that SJF had a stake in the company. During that time, the company's revenue rose from \$6 million to \$20 million, and is now close to \$30 million.

SJF, which had invested more than \$200,000 in HDS, sold its share last year for three times that amount, Hoversten said.

In 2003, another of Hoversten's companies, Salvage Direct, of Titusville, Pa., won top honors. It facilitates a Web-based auction of cars and boats wrecked in accidents and written off by insurance companies but coveted by salvagers.

In the three years SJF has been involved, Salvage Direct has grown from 27 to 70 workers and from \$3 million to \$11 million in revenue.

Hoversten noted that SJF stands for his firm's former name - Sustainable Jobs Fund - which emphasized its mission.

"We changed it because people thought we were from the government," he said.

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