Capital and Collaboration: Strengthening Community Investment in Smaller, Postindustrial Cities

Katie Grace, Robin Hacke, and Carmen Panacopoulos

When stakeholders work together and think of community investment in terms of key functions rather than as a series of individual quests, smaller cities can benefit.

In 1850, Lowell was the second-largest city in Massachusetts[1] and America's largest industrial center, driven by the growth of a textile industry that helped launch the US Industrial Revolution. By the mid-1900s, textile manufacturing had moved to the more cost-competitive South, and the city was a shell of its former self, with a decaying urban core and fleeing population. Today, after a number of years of concentrated economic-development efforts, Lowell is facing significant demographic change and still lags the state in median family income, employment rates, and educational attainment.

Smaller, postindustrial cities like Lowell dot the landscape of New England. Often far from major metropolitan regions like Boston, these cities are struggling to build, or arrest the decline of, their economies and are home to sizeable communities of low- and moderate-income (LMI) individuals and families who are not well served by traditional economic-development activity that seeks to attract large-scale employers and prioritizes job volume over job quality. Community investment, which we define as financial investment to accomplish social, economic, and environmental goals in LMI areas, provides a foundation that can be built upon to support LMI communities and the cities where they live. By thinking in new ways about what it takes to strengthen community investment in a place, we hope to improve the ability of cities like Lowell to attract and deploy private capital to public purpose.

Community Investment and Capital Absorption

Community investment nurtures economic and neighborhood vitality and can help make cities more equitable and sustainable. It works in places and sectors where conventional market activity does not fully meet community needs. Community investment transactions are often complex, time-consuming, and politically fraught, requiring intense collaboration among stakeholders and relying on subsidies, tax credits, and grants to be financially viable.

Community investment transactions are often complex, time-consuming, and politically fraught.

Practitioners of community investment tend to view their work as a series of individual heroic quests, rather than as part of a system for conducting socially valuable activity. That viewpoint makes it difficult to address the challenges of coordination and build capacity for the long term.

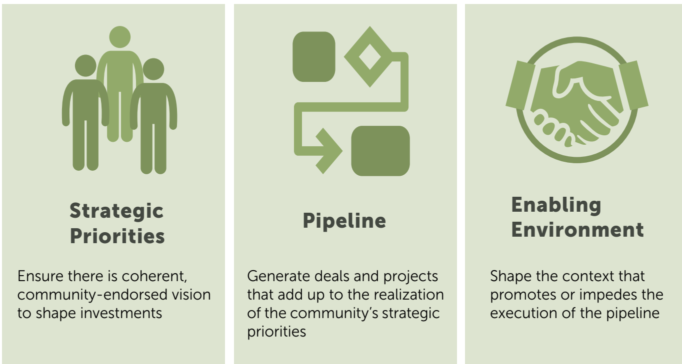
To better understand the system of community investment, and with the hope of developing interventions that would permit it to achieve greater scale, efficiency, and impact, we developed a framework we call "capital absorption."[2] The capital absorption capacity of a city or region is that place's ability to attract and make effective use of various forms of capital in support of underserved communities. The capital absorption framework goes beyond consideration of individual transactions to identify functions that support effective community investment in three areas: strategic priorities, project pipeline, and an enabling environment. (See "The Community Investment System.")

Application of this framework generally involves two sets of activities: assessment of the current system and effort to change it. These activities are carried out by a cross-sector group of stakeholders that may include public-sector leaders, investors, foundations, developers, small-business owners, nonprofit organizations, and others. During assessment, the cross-sector group examines the current system's strengths and gaps and evaluates how the three functions are currently being performed.[3] The assessment includes questions like the following:

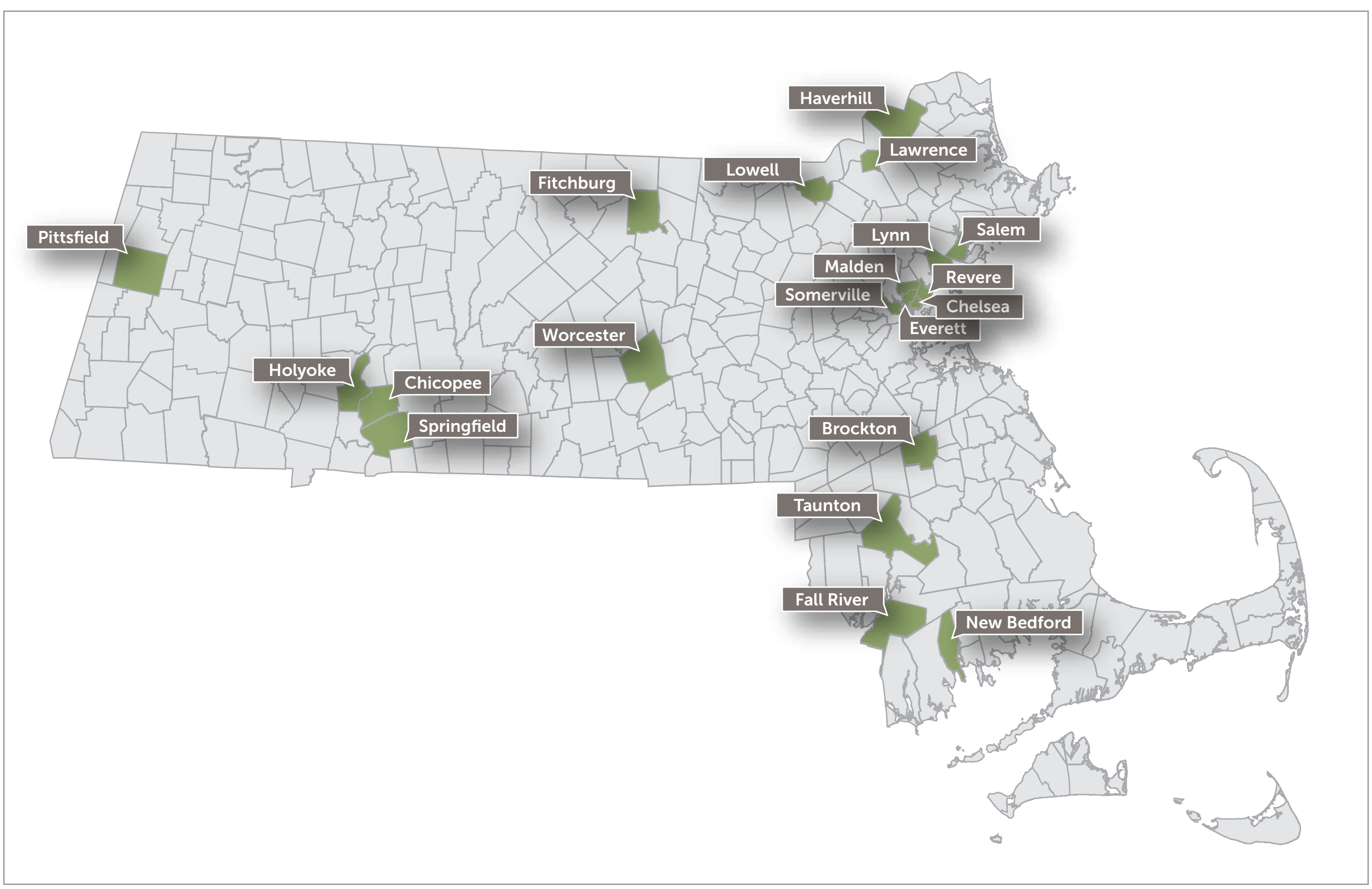
- Are there clear priorities guiding activity?
- How does the pipeline of investments match up with those priorities?
- Where does capital currently come from, and where is it going?
- What policies and practices foster or impede the execution of investments that align with priorities?

Then the cross-sector group considers how to change the existing system, identifying and then implementing interventions that will strengthen community investment. These interventions may include adopting new policies, bringing in new stakeholders, gathering data, or aligning resources and attention.

The Community Investment System



Locations of Massachusetts' Working Cities



Capital & Collaboration Initiative

In 2013, the Federal Reserve Bank of Boston launched the Working Cities Challenge,[4] a competition designed to incentivize cross-sector leadership and collaboration for transformative change in 21 postindustrial cities in Massachusetts. (See "Locations of Massachusetts' Working Cities.") In 2015, the Boston Fed partnered with the Initiative for Responsible Investment at the Harvard Kennedy School and Robin Hacke of the Kresge Foundation to look at the systemic issues that affect the flow of capital to these cities. The Capital & Collaboration project is using the capital absorption framework to understand the community investment system in the Working Cities as it pertains specifically to two types of investments: large-scale mixed-use and commercial real estate and small-business development.

The project is guided by a state-level, cross-sector working group of more than 25 individuals representing state and quasi-public agencies, banks and financial institutions, community development financial institutions, and other intermediaries and advocacy organizations. Over the past year, the project has conducted more than 50 interviews, convened five focus groups, and gathered and analyzed extensive data to learn how community investment operates in the Working Cities. We also held a workshop to which 11 of the Working Cities brought multisector teams to assess their own local capital absorption capacity. The Capital & Collaboration working group is now consolidating insights and formulating an action plan that identifies steps its members' institutions can take, individually and together, to strengthen the community investment system.

We have already gained several insights into the community investment system in the Working Cities:

- Practitioners believe that Working Cities are at a disadvantage because interest, focus, funding, and the ability to do deals are overconcentrated in the city of Boston. Boston's market size and strength, its density of opportunity, and the strong network of relationships among its developers, investors, and public-sector officials, among other factors, make it easier to do deals there than in the Working Cities.
- Both for-profit and nonprofit developers desire greater transparency and predictability in the allocations of tax credits and other state subsidies, which they said would reduce risk and the time it takes to execute a transaction, potentially resulting in more deals.
- Stakeholders also emphasized the importance of another type of certainty: a clear expression of a city's plans and priorities. Developers and bankers agreed that resources flow more readily when cities put forth actionable plans, especially ones that are bolstered by visible investment of municipal resources.
- Mixed-use and commercial projects are hampered by the siloing of housing and commercial/industrial development. The distinct actors, policies, and funding flows associated with each type of development create fragmentation and complexity that make these deals incredibly challenging to execute, with many projects requiring a decade to complete. In addition, many developers of mixed-use spaces struggle to develop attractive ground-floor spaces and to find tenants for these spaces who would contribute to street-level vitality and meet the needs of residents.
- To support small-business development, investors must consider the distinct needs of different types of businesses. Segmenting by size of business, sector, and growth potential is necessary in order to provide appropriately targeted capital and technical assistance. In many cases, availability of capital is not the constraining factor: what small businesses in these communities often need are small-dollar loans, help with accounting and operational issues, and assistance finding and finishing spaces.

Lessons Learned to Date

The Capital & Collaboration initiative is the first statewide application of the capital absorption framework in the nation. Although the work is ongoing, we are already learning some interesting lessons about the interaction between the local, regional, and statewide scale in the community investment context.

Developers and bankers agreed that resources flow more readily when cities put forth actionable plans.

Given the magnetic pull exerted by a major metropolis like Boston, getting capital to flow to projects further afield requires intentional measures. Cities can help attract capital by clearly defining their plans and priorities, thereby reducing uncertainty for developers and investors. State actors can identify policies that may unintentionally penalize smaller jurisdictions and can then work to counteract their effect. When stakeholders from the public, private, and philanthropic sectors work together, it becomes easier to assess how the community investment system is performing and how its performance can be strengthened. This work offers potential routes forward for understanding and addressing need in LMI communities in postindustrial cities throughout New England.

Katie Grace *is the assistant director of the Initiative for Responsible Investment.* **Robin Hacke** *is a senior fellow at the Kresge Foundation.* **Carmen Panacopoulos** *is a senior relationship manager in the Regional & Community Outreach department of the Federal Reserve Bank of Boston. Contact them at katie_grace@hks.harvard.edu, RLHacke@kresge.org, and Carmen.Panacopoulos@bos.frb.org, respectively.*

Endnotes

1 "Population of the 100 Largest Urban Places: 1850," US Bureau of the Census, https://www.census.gov/population/www/documentation/twps0027/tab08.txt.

2 This work is the result of a partnership between Robin Hacke, senior fellow at the Kresge Foundation, David Wood and Katie Grace at the Initiative for Responsible Investment at Harvard University's Kennedy School of Government, and Marian Urquilla, from the consulting practice Strategy Lift. An overview of our framework can be found in "Community Investment: Focusing on the System" (working paper, Kresge Foundation, March 2015), http://kresge.org/sites/default/files/Kresge-Community-Investment-Focusing-on-the%20System-March%202015_0.pdf.

3 Useful tools for conducting such an assessment may be found here: http://kresge.org/library/community-investment-focusing-system-worksheets.

4 For more information, see www.bostonfed.org/WorkingCities/.