Unit I–Core Principles: An Introduction to Community Development Finance

Learning Objective

To define several core principles of community development and investment and to analyze some of the factors that influence community development finance.

The Vocabulary of Community Development Finance

Community Development: What It Means

The definition of "community development" seems to vary from person to person, group to group. Some will define it all too narrowly. For example, they think it encompasses only beautification or only projects that can be financed with federal Community Development Block Grant money. Others think it's synonymous with affordable housing. Banks and thrifts take a somewhat different view, given their obligations under the Community Reinvestment Act to help meet the credit needs of their low- and moderate-income communities. Besides housing, banks and thrifts will often consider financing such community development as job creation programs for small businesses and small farms; redevelopment of industrial sites; environmental cleanup; and any project that will revitalize or stabilize a low- or moderate-income neighborhood, whether that project be a supermarket or a day-care center.

Community development can be all of these things, but also much more. Your community is free to come up with its own definition. Keep in mind that community development usually requires four elements:

- Attention to the desires of the people involved and to the areas where they live and work.
- Control by community members, who become active participants.
- The concept of self-help, which is vitally important to the community development process.
- A holistic view of the community, in which groups take into account one another's goals and actions, as opposed to operating as if each were in a vacuum.

■ ***Exercise:*** Depending upon our backgrounds and experiences, community development may mean a variety of things. What does it mean to you? Use the space provided to write down your definition of community development.

(Examples: Community Development Block Grant program, neighborhood beautification, solutions to wastewater problems, small-business development, industrial development, job creation, better public works.)

Community Development Finance

Community development finance involves economic growth in which people come together and make the decisions to organize and pool assets and resources for the purpose of addressing unmet needs and opportunities.

In order to do this, you must be familiar with some basic terms:

Financing: To raise money in any way. The list of sources could include grants, loans, sale of "stock" in the project, tax breaks, fund-raising, pooling money with partners, income from the project (rent, admission fees, etc.) and so on.

Capital: It's not just money, but anything you have that can be used to obtain your goals. The list includes equipment, property, other goods, services and even knowledge.

Subsidy: Financial assistance granted by a government to an individual or organization in order to fill a financing gap.

Debt: Any money, goods or services owed to someone else. Debt can take the form of mortgages, other kinds of loans and notes, bonds, etc.

Equity: Ownership interest in a project or company after liabilities are deducted.

(See the Glossary for more terms.)

Unmet Needs

"Unmet needs" aren't just the needs that leaders identify for a community. Rather, "unmet needs" are the needs as defined by those who have them. The difference can be important. For example, in the not-too-distant past, leaders across the country promoted youth centers as a top need for their communities. Many were built. And many went unused. Why? Because the youth themselves didn't really want them. Market research must be undertaken to prove that a project that has been suggested by community developers is really wanted and needed by the target audience—and will be used.

■ ***Exercise:*** What are some of the unmet needs in your community?

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(Examples: Lack of jobs, skilled laborers, industry, community park, senior citizen center, assisted living center for disabled or senior citizens, indoor community/athletic center, affordable housing, community-wide Internet access.)

Assets

When we talk about assets, we are referring to any advantages, resources, talents, goods or services in your community that might be available to help you with your project

■ ***Exercise:*** What assets do you and your group bring to the table?

(Examples: You have worked as an accountant or your group includes people with expertise in architecture, construction, job training, etc.)

■ ***Exercise:*** What assets exist elsewhere in your community or are available to your community?

(Examples: Schools, colleges and universities; banks; highways; airports; natural resources such as lakes, rivers or mountains; skilled labor force; leadership; affordable housing stock; history; etc.)

Opportunities

An unmet need becomes a community development opportunity when assets can be found that can be used as tools to address that need.

■ ***Exercise:*** What are some of the development opportunities in your community?

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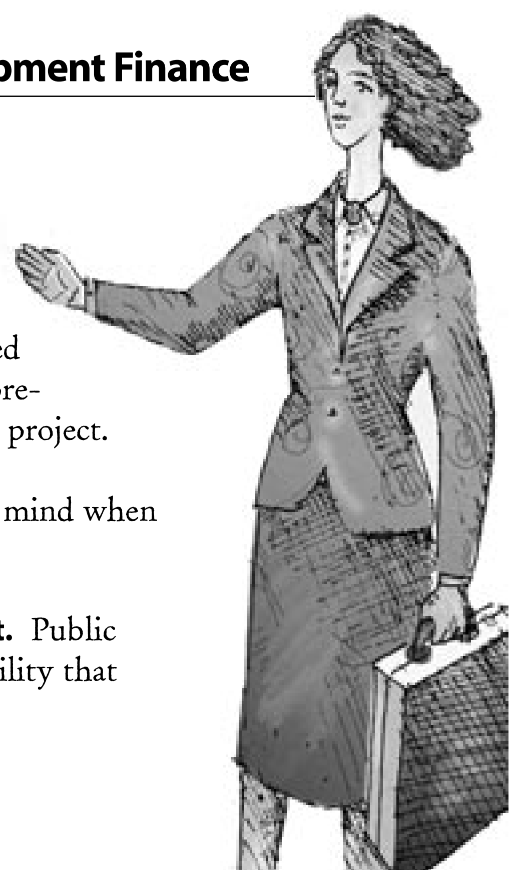
(Examples: Local university helps sponsor a senior citizen center. A bank and nonprofit group team up to provide affordable housing.)

Fundamentals of Community Development Finance



The Value of Good Design

Builders design a blueprint before constructing a house, and athletic teams draw up a game plan before going out on the field. For the same reasons, community development players also need to create a design to finance their projects. This predevelopment work is often the key to a successful project.

Some of the elements that you must keep in mind when designing a financing package:

Collaboration and community involvement. Public and private partnerships increase the probability that the project will reach its intended goal.

Mitigation. In finance, subsidies and enhancements are used to diminish risk.

Customization. Services and products are customized to take into account the community's characteristics, such as its predominant lifestyle, income range, amenities and housing.

Flexibility. The community development finance plan must be elastic so that it can be changed to accommodate growth and/or changing conditions. For example, a developer might ask to allow the value of in-kind contributions of professional services to satisfy the local match requirement for receiving grant funds from a national foundation.

Recognition and use of cycles. Timing is critical to community development, as every community development project is a small part of a larger cycle. Entering a market with a project at the wrong time can spell disaster. An example of poor timing would be to open a grocery store in an "on its way back" neighborhood that is still years away from being repopulated.

Trends in Community Development

Understanding why and how community development finance has evolved helps to predict what the future holds, improves planning and strategic responses, and heightens our ability to improve decisions that can result in better performance in the economy of our communities.

Current trends in community development include:

Dwindling government funds. Money for community development has come primarily from government sources, which account for more than one-third of all nonprofits' revenue. However, the growth of funding from government is declining. Government agencies are raising expectations for those who receive assistance. Some levels of government are allowing community developers to tap into more than one government program for money for the same project; such layering was not usually allowed in the past. Meanwhile, private contributions are increasing, but not at a rate that can completely replace government sources.

Shift from piecemeal approach to holistic approach. Community developers and the sources of money are becoming more concerned about how a project fits in with and is affected by other projects at work in the same community.

Shift from a single funding source to multiple funding sources. We have heard that the average number of funding sources is seven. This may have begun in its simplest form—with the requirement for matched funding.

Performance-based or outcome-based funding. Money from many sources is contingent upon completion of work described in performance contracts. And the bar is being raised on what sort of outcome is acceptable. In job training programs, for example, it's no longer good enough to show how many people graduated or how many got jobs. Rather, the program's success might be pegged to the number of graduates still on the job six months later and whether they are receiving a living wage.

Return on investment. Gone are the days when backers of community development projects didn't expect anything in return for their support besides recognition. Today, they want a return—sometimes financial, other times social or moral. And you must find a way to provide and measure these returns.

■ ***Exercise:*** What trends are affecting the community development field in your community?

(Examples: Banks are no longer locally controlled, nonprofit groups are becoming increasingly sophisticated, viable low-income markets, niche banks, less emphasis on agriculture.)

Partnerships: Why They Are Necessary and Why They Work

We form partnerships because we cannot accomplish community development projects single-handedly. Some of the benefits that partnerships bring:

Resolution of complex problems. Most organizations do not have the resources or the capabilities to address problems such as inadequate housing and downtown revitalization. However, many complex problems can be addressed when organizations work together. When several organizations are involved, more resources are available and more people are represented.

Fresh solutions to old problems. Contributions from differing organizations can provide new perspectives on persistent problems.

Making the best use of limited resources. Federal, state and private funding sources emphasize cooperation and collaboration among community developers. More often than not, the partnership approach is being mandated by these sources of money, who realize that strong interorganizational relations eliminate duplication of efforts and maximize the use of limited resources. Many funding sources require that their investments be matched by other sources.

Public relations strategies. Some industries see the chance to partner with a community developer as a chance to garner good public relations. The industries realize that if they are perceived as being socially responsible, politically savvy or connected, they will gain credibility among consumers and will win cooperation from various groups.

Synergies. Partnerships are able to accomplish more by working together than any of the individual entities can by working alone.

Special expertise. The partners can pool information and knowledge about community development.

Sometimes, Partnerships Can Be Difficult

Partnerships mean collaborating to accomplish a common mission. Financial collaboration for community development requires a commitment to share decisions and to share resources for needs that are mutually important.

■ ***Exercise:*** List some of the things that make partnership deals difficult, based on your experience or on your learning.

(Examples: time it takes; personnel changes; cash flow problems; risk—real and perceived; competing projects and programs; lack of consensus or agreements; NIMBY—not in my back yard; lack of business planning; lack of communication; government regulation and politics; egos.)

Whom Do You Need on Your Project Team?

Before you look for partners, be sure of what you bring to the table.

■ ***Exercise:*** What is your role in community development or what roles have you played in the past? What expertise do you bring to the project?

(Examples: visionary, lender or another kind of intermediary who provides credit or capital, developer, organizer, government enhancement provider such as the Department of Housing and Urban Development or the Small Business Administration, technical expert, political leader, community organization, national supporter, architect, contractor, project manager, accountant, lawyer, entrepreneur/owner, public relations, marketing and champion for the project.)

■ ***Exercise:*** Who might be a partner for you or your group?

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(Examples: Traditional partners have included banks; nonprofit institutions, churches and other faith-based groups; local, state or federal government agencies; and philanthropic arms of major businesses. Today's partners are just as likely to include pension funds, insurance companies, large corporations, private developers, community development financial institutions, housing trust funds, revolving loan funds, etc.)

Partnerships: A Final Thought

Similarities. All partners share a common vision but recognize and accept that each party has different, and possibly competing, agendas.

Differences. Each partner wants something different out of the deal, such as quality of life, social objectives or financial return on investment. Watch out for partners whose philosophies or goals can't be reconciled with your own. Consider the track record of others before aligning with them. Be ready to compromise.

Applying What We've Learned So Far

Let's start to put this information to work. Think of a potential community development opportunity in your area. Use the following worksheet to assess the current community development environment and to clarify your role in leading this opportunity.

Worksheet

Step 1: Assess the current situation

■ Describe the potential community development opportunity (unmet need).

■ List the assets that you have or that are available to your community to help fulfill this opportunity.

■ How can you take advantage of these assets?

Step 2: Assess collaboration opportunities

■ List all of your potential partners who could help you meet your community's unmet need.

■ List the expertise that each potential partner can bring to the table.

■ What problems might they bring as well?

■ Constructuct your team from your list and assign roles to each, including yourself.

Summary

Community development consists of three important elements: people, process and money. In this Unit, we discussed partnerships (people). In Unit II, we'll explore business plans (process), and in Unit III we'll show you different ways of coming up with the money.

Notes: