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Investment intermediaries in economic development: Linking pension funds to urban revitalization

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Abstract.

Large institutional investors, such as public sector pension funds, invest in affordable housing, mixed-income and mixed-use real estate, and emerging growth companies under the rubric of urban revitalization or economic development. Investment intermediaries link institutional investors to urban revitalization. As a pension fund does not have urban investing expertise they turn to an investment intermediary, often referred to as an investment fund manager or termed "investment vehicle", to deploy large pools of capital into the community. The money managers are able to take large dollar amounts and parcel the funds into attractive urban investments. They have the expertise to structure a deal in a community partnership that delivers high financial returns to the investor and social returns to the community. An investment vehicle can have in-depth expertise investing in large-scale property development and mission-oriented companies. Community partners also act as an intermediary between the investment vehicle and the urban community. The community organization can ensure that the ancillary social goals are realized. We argue that without these intermediaries large institutional dollars could not be deployed in the underserved markets and could not achieve the targeted financial and social goals.

Keywords.
Economic development, investment vehicles, public sector pension funds.

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Executive Summary

- Investment intermediaries link pension funds to the revitalized economic development area. The investment vehicle and the institutional investor form a symbiotic relationship that allows for scale to effectively transform neighborhoods and yield financial returns to the institutional investor.

- Without these vehicles large pools of capital would not get placed in the economic development area. The institutional investor relies on the investment fund manager for their expertise in successfully deploying capital.

- Through an effective deal flow process and capital structure the investment vehicle sources deals and deploys capital into the community.

- The community partner also serves as an intermediary. In this case the community partner links the investment fund manager with the economic development area and the community. The community partner ensures that the social goals are realized.

- An investment vehicles' competitive advantage is in overcoming investment barriers typical to the underserved markets. Investment vehicles overcome market prejudice and work through restrictive government regulations. They are able to manage the inherent risk in these transactions through their ability to pool assets and spread risk across investors. As such they price transactions up to the associated risk.

- Greater transparency on returns is needed for more institutional dollars (e.g. public sector pension funds) to flow into the space of community based investing. Metrics to date include financial returns measured against industry benchmarks.

- The social metrics are slowly being tracked and will continue to be as institutional investors expect to see quantitative results on the ancillary benefits. Incorporating social goals into the investment criteria is essential for the growth of this industry.

- Environmental benefits are now being tracked. Buildings can be measured for their environmental impacts (brownfield redevelopment) and green building certification according to the Leadership in Energy and Environmental Design (LEED) Green Building Rating System. Investments in clean-tech and recycling companies also yield environmental returns.

Contents

List of Tables

List of Figures

1 Introduction

Investing in America's inner cities is an innovative practice in which large institutional investors can enjoy high financial and social returns on their investment. Public sector pension funds invest in urban areas spurring economic growth in underserved emerging domestic markets. These investments are made through traditional investments (fixed income) and alternatives (equity real estate and private equity). Contrary to market perception, targeted investments can produce above market-rate returns along with jobs, workforce housing, and an increased tax base as secondary social benefits.

Critics argue that these types of investments are prone to political interference (Romano, 1993) and can distract pension funds from their mission. Further skeptics contend that investment vehicles may not have the expertise to produce the above market-rate returns to the investor. Lessons learned from pension fund adopters in urban investing (California, New York, and Massachusetts) demonstrate that these investments yield both high financial and social returns. Public sector pension funds that have adopted economic development policies typically set aside two percent of their total portfolio to targeted investments and place the capital with an investment intermediary (Hagerman, Hebb, 2005).

We argue that investment vehicles provide these pension funds with the expertise to deliver the financial and social returns they seek. These vehicles have developed their own market niche and investment strategy. Often they are for-profit entities selected based on their investment expertise and past performance. Public pension funds seek out investment vehicles that meet the requirements of a rigorous investment philosophy chosen through a competitive bidding process (Hagerman 2006). Pension funds need these investment intermediaries to be able to make investments in economic development.

In this paper we will show that while pension funds provide broad geographic goals, it is investment vehicles that link the pension fund to a revitalized urban area. Bringing investments to scale so they are attractive to a large institutional investor (e.g. public sector pension fund) is a challenge. Public pension funds do not have the time or expertise to actively manage specialized urban investments. Investment vehicles intervene, using economic principles, and government subsidies to organize and produce scale. An investment intermediary can source deals and deploy capital into the community through limited partnership structures or fund-of-funds. The specialized investment fund, through their urban investing expertise, helps the institutional investor place large pools of capital in the underserved markets.

Several types of investment intermediaries and their business models are presented in this paper. Investment vehicles specialize in different asset classes such as fixed income, equity real estate, and private equity (early and later stage venture capital). Fixed income debt-based investments are usually the first of the asset classes for a pension fund to undertake investments in economic development. Fixed income investments in economic development are often backed by government guarantees and a conventional option for the large institutional investor. Equity real estate is a growing industry and the asset class through which investments can make the greatest impact in urban revitalization. Private equity investment vehicles make investments in early stage and later stage venture capital. Investments are made into mission-oriented companies across industry sectors. In private equity investment vehicles are successfully building funds, and fund-of-funds, that are investing in mission-oriented companies.

This paper examines a range of community groups that partner with the investment vehicles. The role and importance of the community partner as an integral part of the investment process is developed. In this discussion we will examine an economic development consultant, or "fund builder", and show how the not-for-profit community sponsor is built into the investment process. We argue that the partnership with the community ensures the social goals are realized.

The study examines the outcomes connecting the financial intermediaries, both investment vehicles and community partners, to the revitalized area. We will deconstruct the types of returns (financial, social, and environmental) that benefit the investors first and the community second. Competitive financial returns are being realized, in particular in equity real estate and fixed income investment products. In private equity (early and later stage venture capital) returns are negative in the first few years due to fund management fees and expenses incurred before the fund has exited on its investment (referred to as the J-Curve effect). Social returns (e.g. job and wealth creation) and the environmental returns (e.g. green construction and clean technology) are equally important and being tracked.

This paper is structured in the following way. Section two provides a roadmap for the reader with the different types of investment vehicles across the asset classes of fixed income, equity real estate, and private equity. Section three examines the role of the investment intermediary in the context of the economic principles of scale. Section four examines the structure of an investment intermediary. Section five highlights the types of investment intermediaries in the context of urban economic development. Section six examines the role of the community partner in economic development. Section seven examines capital structures and how deals are sourced. We conclude with arguments in favor of pension funds investing in urban revitalization through investment intermediaries with a discussion of the financial, social, and environmental outcomes.

2 Types of investment vehicles

Pension funds invest in urban revitalization through investment vehicles that act as a channel for large institutional dollars to flow into the urban economic development areas. Pension funds invest in investment vehicles through three asset classes: fixed income, equity real estate, and private equity (early and later stage venture capital) as follows:

1. Fixed Income is a debt based real estate and small business development finance product investing in affordable housing through construction loans and permanent loans, job creation programs and in mortgage backed securities. Additionally, in the case of the credit enhancement product a pension fund will loan its credit rating to a municipality or state agency for a fee. This allows the agency to access capital at a lower cost. Fixed income is generally the easiest option for a pension fund to take up as investing in mortgage-backed securities is often already a part of their fixed income strategy.

2. Equity Real Estate is a real estate finance product investing in the potential growth in market value of the investment property. Investments are made in mixed-use, mixed-income greyfields (urban infill development) and brownfields (clean-up of environmentally contaminated properties). Pension fund investing in equity real estate has seen the greatest impact on urban revitalization and a more established form of community based investing.

3. Private Equity (early and later stage venture capital, and often mezzanine capital) is the business finance product investing in mission-oriented companies (consumer products, healthcare, technology, women and minority-owned firms in or near low-moderate income areas) at the early stage of the company's development and the expansion stage of the company. Pension fund investing in urban revitalization through private equity (business finance) is an emerging vehicle for pension funds to invest in urban revitalization.

The funds listed are mission-oriented funds that seek to achieve first a high financial return and secondly ancillary benefits. In this sense they are often referred to as double bottom line funds. However, pension funds tend to more generally refer to them as funds that target economic development. A brief background on the fund, projects undertaken, and returns realized is outlined. Most funds listed are for-profit fund managers with, in some cases, a not-for-profit affiliate or sponsor. *The following text is simply to provide a roadmap for the reader with example funds listed in alphabetical order. The funds profiled are a small selection of a myriad of funds in this growing industry. The reader should keep in mind that the following description of the funds is not an offer or solicitation by the Funds and should not be construed as such. The following is merely for research purposes.*

Asset Class: Fixed Income

Access Capital Strategies LLC

Asset size**:** $600 million

History: Founded by Ron Homer and David Sand in 1997 because they identified the opportunity for a high credit quality market rate of return investment vehicle that supports community development in areas designated by investors. The principal focus is to create and purchase specialized economically targeted securities guaranteed by Fannie Mae, Freddie Mac Ginnie Mae, USDA,SBA and other government agencies. These securities can be managed in separate counts or held in the Access Capital Strategies Community Investment Fund, Inc. Inception Date: 6/30/98

Structure**:** Managed by the Registered Investment Advisor and for-profit fund manager, Access Capital Strategies LLC, sub-managed by Voyageur Asset Management, a subsidiary of Royal Bank of Canada

Pension Fund investors**:** MassPRIM (Fund) NYCERS (Separate Account)

Location of investments**:** National

Investment type**:** Economically targeted bond fund that invests in geographically-specific, debt securities located across the United States as designated by Fund investors. Financing low income housing, mortgages to low and moderate income borrowers, small businesses and healthcare facilities.

Example Projects: Industrial Bank, N.A. – Worked with Fannie Mae to enable Industrial Bank, N.A., a DC-based minority-owned CDFI, to securitize and sell a $15M mortgage pool made from 5 year balloon payment mortgages converted to 30 year fixed rate loans at prime mortgage rates.
Holyoke Health Center – Worked with the Massachusetts Housing Investment Corporation (MHIC) to provide the Holyoke Health Center – a community health center in a medically underserved area of Holyoke, MA – with a loan of $9.4M to enable the Center to expand health care and services while giving them a more efficient capital structure.
Community Reinvestment Fund (CRF) – Helped CRF create liquidity by investing $3M in their AAA-Rated Series 17 Class A-3 Notes which consist of 128 economic development loans including affordable multi-family housing units in 19 states.
Returns are gross, annualized, as of 12/31/06
1Yr: 5.43 3 Yr: 4.42 5 Yr: 5.06 Since Inception: 5.83
Over a 5 year period gross returns have consistently met or exceeded the Lehman aggregate.
Community Impact:
Since inception, the Fund has supported 8,408 low- to moderate-income homebuyers, 4,474 affordable rental housing units, 147 small business loans, and 1 community health center.
Ancillary objectives**:** Creates a reliable secondary market for community development loans and helps to extend the prime mortgage market in to underserved communities.
Community partners/Joint venture developers**:** Massachusetts Housing Investment Corporation, Fannie Mae American Communities Fund, and Community Development Financial Institutions;

Source: Senior management, http://accesscapitalfunds.com/index.html

Asset Class: Fixed Income

AFL-CIO Housing Investment Trust (AFL-CIO HIT)

Asset size: $3.6 billion in net assets
History: The AFL-CIO authorizes creation of the AFL-CIO Housing Investment Trust in 1981 to build on the work of the earlier Mortgage Investment Trust and expand the scope of investments in housing and mortgages.
Structure: Common Law Business Trust registered under the Investment Company Act of 1940. Approximately 94% of the non-cash investments are insured or guaranteed by the U.S. government or a government-sponsored enterprise.
Pension Fund investors: Taft-Hartley funds, public employee pension funds
Location of investments: National (e.g. New Orleans, NYC, Chicago, St. Louis, Minneapolis)
Investment type: financing for development, rehabilitation, or preservation of real estate, construction and permanent financing, fixed or floating rate forward commitments, secured bridge loans
Ancillary objectives: affordable housing, union construction jobs, permanent jobs, tax revenues, improved quality of life
Signature projects:
Victory Center of Roseland, Chicago, IL
Working with the Illinois Housing Development Authority (IHDA), the Trust made an $8 million financial commitment for construction of the $20.7 million Victory Center of Roseland Supportive Living Facility. Residents of the 124-unit facility are very low-, low- and moderate-income elderly who are able to take advantage of a wide array of services. The building's ground floor has 10,000 square feet of community space.
HIT Investment: $8.05 million

Community partners/Joint venture developers:
Illinois Housing Development Authority, local housing development offices such as the City of New York's Department of Housing Preservation and Development as well as national housing advocacy groups such as the National Low Income Housing Coalition, the National Housing Conference, the Enterprise Foundation and Local Initiatives Support Coalition.

The Trust has a long history of working closely with for-profit and non-profit developers, housing agencies, members of the mortgage banking community, labor unions, government-sponsored enterprises (GSEs) and others to identify and structure the financing needed for their real estate developments.

To protect its investors from a loss of principal and to provide the most attractive terms to developers, the Trust structures its financing with credit enhancements provided by a variety of sources, including the Federal Housing Administration (FHA), Ginnie Mae, government-sponsored enterprises such as Fannie Mae and Freddie Mac, and state and local agencies.

Returns: Annualized net returns for period ending 10/31/06 10yr: 6.57%, 5year: 4.8%, 3 yr: 4.02%, 1yr; 5.43% (consistently outperformed Lehman Aggregate Bond Index) Over past 10yrs created or preserved over 37,000 units of multifamily housing in 175 projects nationwide, 65% of which were affordable to low-moderate income households. 100% union labor construction on projects it financings.
Since inception: Since Inception:"80,000 housing units built through $5 billion in financing; creating 35 million hours of union construction work".
Source: Senior Management, http://www.aflcio-hit.com/

Asset Class: Fixed Income

Community Capital Management (formerly CRA Fund Advisors)

Asset size: $825 million in assets under management as of 9/30/2006; $1.85 billion of economically- and geographically-targeted investments made since 1999
History: Community Capital Management is a money management organization created in 1998 specifically to manage fixed-income community development investments on behalf of the nation's largest financial institutions. In 2001, it began managing separate accounts and currently manages fixed-income portfolios on behalf of public pensions, foundations and faith-based investors. Its unique economically-targeted investment approach has generated consistent returns ahead of the Lehman Brothers Aggregate Bond Index and benefited hundreds of thousands of underserved families and communities throughout the United States.
Structure: For-profit money manager / registered investment advisor
Location of investments: National

Investment type: Mutual fund (CRA Qualified Investment Fund; ticker symbol CRAIX; minimum investment $500,000) and fixed-income separate accounts (minimum investment $5 million). Community Capital Management approach involves the positive screening of new and outstanding bond issues in search of high credit quality securities that finance community development initiatives targeting: homeownership, affordable rental housing, affordable health care, job training, education, and environmental programs

Pension fund investors: Massachusetts PRIM; Pennsylvania State Workers Insurance Fund; Pennsylvania Treasury
Ancillary objectives: affordable housing, affordable healthcare, senior housing facilities, union construction jobs, permanent jobs, tax revenues, improved quality of life

Returns:
GIPS-compliant performance numbers for the *Community Investment Composite* (comprised of all actively managed fixed-income portfolios including mutual fund and separate accounts (through 4th Quarter 2006; inception date is 8/30/1999):

	Gross	Net	Lehman Aggregate
4Q2006	1.24%	1.12%	1.24%
1-Year	4.55%	4.05%	4.33%
3-Year	4.18%	3.67%	3.70%
5-Year	5.53%	5.02%	5.06%
7-Year	6.64%	6.11%	6.45%
Since Inception	6.35%	5.82%	6.29%

Social returns:
$2.0 billion resulting in the following measurable impact through December 31, 2006:

- 128,000 affordable rental housing units
- 4,600 home mortgages for low- to moderate-income individuals
- $30.5 million in affordable health care facilities
- $139 million in community development activities, including neighborhood revitalization and brownfield redevelopment
- $296 million in downpayment assistance and statewide homeownership programs
- $93 million in job creation and job training programs

Source: Community Capital Management Senior Management, http://www.crafund.com/about_crafund_advisors.asp?PageID=2

Asset Class: Fixed Income

Community Preservation Corporation (CPC)

Asset size: As of fiscal year ended 6/30/906: CPC closed $674M in new financings. Accumulated fund balance $65.3M (acts as FHA approved lender & seller/servicer for Fannie Mae & Freddie Mac)

History: Community Preservation Corporation (CPC), was founded in 1974 after David Rockefeller led a study with New York City officials and other leading commercial banks to address the lack of apartment building financing (construction/rehabilitation loans) from traditional savings banks. CPC owns their for-profit subsidiary, Community Preservation Corporation Resources (CPCR) founded in 1992.

Structure: Ownership model, the Community Preservation Corporation (CPC) is a not-for-profit community development lender. CPC owns a for-profit subsidiary, CPCR, founded in 1992.

Pension Fund investors: NYCERS, NYC Police, NYC Teachers, and New York State Common

Location of investments: 5 boroughs of NYC, Hudson Valley, upstate NY, and New Jersey.

Investment type: financing low-moderate income housing

Ancillary objectives: affordable housing, historic building restoration, construction jobs, permanent jobs, tax revenues, improved quality of life

Signature projects: The Imperial (Crown Heights, Brooklyn) is one of six buildings containing 72 units financed by CPC for $12.4 million. In addition to CPC's construction financing, HPD provided 1% funding. This restored building consists of 35 rental units, of which 25% will be affordable to households earning no more than 50% of area median income. 50% will be affordable to low-income households earning no more than 60% of area median income (CPC 2006 Annual Report).
Most Significant Bronx success stories: McKinley Square. CPC in partnership with HPD, financed over 500 units, investing more than $35 million in the immediate area.

Community partners/Joint venture developers: State housing agencies, NYC Department of Housing Preservation & Development (HPD)

Returns (financial, social and environmental): In 2006 financed preservation and development of over 6,700 housing units representing over $670 million in 317 separate transactions. In its 32-year history 117,000 units of housing representing over $5.3 billion in public-private debt to low and moderate income markets.

Source: Senior management, 2006 CPC Annual Report, http://www.communityp.com/

Asset class: Equity Real Estate

Bay Area Smart Growth Fund I - Pacific Coast Capital Partners (fund manager) (BASFG)

Asset Size: $66 million
History: Created in 2001 as part of the Bay Area Family of Funds and starting investing 2002 to realize community revitalization.
Structure: For-profit fund manager (Pacific Coast Capital Partners) contracts with the not-for-profit fund sponsor (Bay Area Council)
Pension Fund Investors: None
Location of investments: Nine-county Northern California Bay Area
Investment type: mixed-use mixed-income real estate such as community shopping centers, affordable homeownership opportunities, and commercial and office developments in priority neighborhoods
Ancillary objectives: construction jobs, permanent jobs, tax revenues, preservation of green space
Signature projects:
"The flagship project for SGF is Marin City Gateway Retail Center (GRC), a shopping center built about a decade ago in a lower-income area surrounded by more prosperous areas. GRC tenants are national chains and include a restaurant and drug store. The original ownership structure of the center paired a real estate group with a non-profit owner/manager, Marin City Community Land Corporation (MCCLC). But the deal wasn't working. The nonprofit had trouble accurately billing and collecting rents, there was a poor mix of tenants, and the nonprofit didn't have the expertise to fix GRC's problems SGF stepped in and invested $7.1 million in partnership with MCCLC which bought out the real estate partner. SGF became an equity partner, bringing along a plan to turn the property around over a seven-year time period through tenant repositioning, a full facelift of the buildings, and training so the community group's staff members learn how to effectively lease and manage commercial property. Revenues from the property now flow through MCCLC and profits are used to fund community projects such as the development of a garden, playgrounds, ball fields, and a library." OCC Report, "Bay Area Funds Focus on Double Bottom Line" (http://www.occ.treas.gov/cdd/ezine/summer05/doublebottom.html).

Community partners: Joint venture developers, Marin City Community Land Corporation

Returns: With 90% of the fund invested and a new fund proposed following are results as stated by the not-for-profit sponsor Bay Area Council (www.bayareacouncil.org):

- $61 million invested in 12 deals, exited from 3 deals with gains of $8.8 million (Total projected gross IRR of over 30%)
- 111 permanent jobs created, 930 jobs projected, and 1010 jobs preserved for a total of 2,051 permanent jobs – one job for every $29,750
- 809 for-sale homes being built or renovated, with at least 230 units affordable to purchasers at 80% of area median income or lower
- 585,554 sq. ft. of new or upgraded retail development and 577,000 sq. ft. of new or upgraded office/light industrial development
- 5 construction projects utilized green construction measures

Source: Bay Area Council, Pacific Coast Capital Senior Management, OCC Report Bay Area Funds Focus on Double Bottom Line.

Asset Class: Equity Real Estate

Cherokee Investment Partners, LLC (Cherokee)

Asset size: Fund I (1995): $50 million; Fund II (1998): $250 million; Fund III (2002): $620 million; Fund IV (2006): $1.2 billion

History: Originally in the brick manufacturing business, Cherokee founders turned to soil remediation after purchasing a brick plant site on petroleum-contaminated soil. By 1990, Cherokee Sanford Group was the largest soil remediator in the mid-Atlantic region of the United States. In 1993, Cherokee Investment Partners was formed when Tom Darden and John Mazzarino began to buy contaminated sites, remediate them and return them to productive use.

Structure: For-profit fund manager and nonprofit affiliate

Pension Fund Investors: Primarily large, public pension plans, university endowments and insurance companies.

Location of investments: North America and Western Europe

Investment type: Brownfield redevelopment, urban infill redevelopment

Ancillary objectives: Clean-up of contaminated sites, creation of new jobs, improved tax revenues, preservation of green space, sustainable (re)development, community building,

Signature projects:

1. Cherokee Denver is a 50-acre mixed-use revitalization of a 2.3 million square foot former rubber manufacturing complex located in Denver, Colorado on the South Platt River near I-25. Cherokee will create a world-class, transit-oriented urban village on the site, integrating with existing neighborhoods and Denver's citywide assets.
2. Cherokee Boisbriand is the redevelopment of a former General Motors automobile manufacturing plant encompassing 232 acres in the city of Boisbriand, Quebec, approximately 15 minutes north of Montreal. Cherokee is working with the city of Boisbriand to transform this industrial site into a productive mixed-use development for the rapidly growing community. This project will help revive the city economically, replacing jobs and tax dollars lost through the closing of the GM plant.
3. Cherokee Ashley is 450-acre redevelopment of contaminated property along the Ashley and Cooper rivers in North Charleston, S.C. For more than a century, this waterfront property was home to fertilizer processing plants, steel production facilities and wood-treating operations. Cherokee is cleaning up the property and working with the cities of Charleston and North Charleston to establish a new and vibrant mixed-use residential and commercial gateway district that includes a public square, a river walk and a botanical garden.

Community partners/joint venture developers: Municipalities, economic development organizations, city & regional planners, local & national developers, U.S. Conference of Mayors

Social Returns: Through its work on 4,680 acres in North America and Europe, Cherokee will create an estimated 28,600 homes, 3.8 million square feet of retail space, 1 million square feet of office space and almost 3 million square feet of industrial space on formerly contaminated, underutilized land. Cherokee uses its Environmental Management System to assess its performance against environmental policies, objectives, targets and other environmental criteria. Cherokee's Environmental Management System is ISO 14001:2004-certified by the International Organization for Standardization for environmental management. In addition, the company's annual Sustainability Report summarizes each year's progress on key environmental and social performance indicators. For example, in addition to the human health risks mitigated by cleaning up contaminated property, reclaiming a one-acre urban brownfield preserves 4.5 acres of green space[1]. Using this metric, Cherokee's brownfield redevelopment efforts have preserved approximately 20,000 greenfield acres to date. Source: Senior Management, www.cherokeefund.com

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[1] "Public Policies and Private Decisions Affecting the Redevelopment of Brownfields: An Analysis of Critical Factors, Relative Weights and Areal Differentials." U.S. Environmental Protection Agency, September 2001.

Asset Class: Equity Real Estate

Community Preservation Corporation Resources (CPCR)

Asset size: Opportunity Fund I $42.5 million, Opportunity Fund II $93million

History: CPC Resources, Inc. (CPCR) is a for-profit subsidiary of The Community Preservation Corporation (CPC). It was created in 1992 to develop affordable housing in underserved communities throughout New York and New Jersey. The not-for-profit manager of CPCR, Community Preservation Corporation (CPC), was founded in 1974 after David Rockefeller led a study with New York City officials and other leading commercial banks to address the lack of apartment building financing (construction/rehabilitation loans) from traditional savings banks

Structure: Ownership model, CPC Resources is a for-profit subsidiary of the Community Preservation Corporation (CPC nonprofit manager)

Pension Fund investors**:** None
Location of investments**:** 5 boroughs of NYC, Hudson Valley, upstate NY, and New Jersey.
Investment type**:** mixed-income, mixed-use projects infill construction
Ancillary objectives**:** construction jobs, permanent jobs, tax revenues

Signature projects**:**
Renovation and revitalization of the 12,271-unit Parkchester condominium (10-year project) joint venture was formed, Parkchester Preservation Company (PPC), to acquire 6,361 unsold residential units, 500,000 square feet of commercial space and five parking garages. Financing by CPC and member banks, permanent loan financing provided by Freddie Mac, with mortgage insurance by SONYMA. Real estate tax abatements (special New York City and State legislation) partially offset increased costs. Unit owners pay no real estate taxes for 15 years or longer. PPC subsidizes low-income senior and disabled residents in both condominiums (North and South).

Community partners/Joint venture developers**:** Parkchester Preservation Corporation, State Housing Agencies

Returns (financial, social and environmental): $6 million investment in former 11 acre Domino sugar processing plan in Williamsburg, Brooklyn (waterfront). Site to feature affordable housing, open public space, community facilities, and waterfront esplanade. Completed (10-year project): renovation and revitalization of the 12,271-unit Parkchester condominium joint venture was formed, Parkchester Preservation Company (PPC), to acquire 6,361 unsold residential units, 500,000 square feet of commercial space and five parking garages.

Asset Class: Equity Real Estate

Genesis LA Workforce Housing Fund II (Genesis II) managed by Phoenix Realty Group

Asset size: $150 million
History: Genesis LA Workforce Housing Fund II is being funded in 2006, managed by Phoenix Realty Group, is part of the *Genesis LA Family of Funds.*
The Genesis LA Family of Funds model was originally conceived in the office of former Los Angeles Mayor Richard Riordan in 1998, and established as a not-for-profit corporation in 2000. The Family of Funds model is an innovative market-driven real estate and business financing strategy to stimulate job-producing, development projects that create economic opportunities within Los Angeles County's low-income communities.
The Genesis La Family of Funds includes:

- Genesis LA Real Estate Fund I and II
- Genesis LA Workforce Housing Fund I and II
- Fulcrum Growth Capital Fund (private equity early and later stage venture capital),
- Community Investment Fund, and
- a New Markets Tax Credit Fund (U.S. Treasury Dept. tax credit allocation program that allows the fund to provide lower cost capital and make certain project financing feasible)

Structure: not-for-profit fund sponsor, Genesis LA Family of Funds contracts with a for-profit fund manager, Genesis LA Workforce Housing Fund II managed by Phoenix Realty Group

Pension Fund investors: $65 million investment in Los Angeles City Employees Retirement System (LACERS); Los Angeles County Employee Retirement Association (LACERA); Los Angeles Department of Fire and Police Pensions (LAFPP)

Location of investments: Greater Los Angeles area
Investment type: Infill mixed-income development, investments will target for-sale and rental housing affordable housing to Los Angeles' middle-income workforce, including teachers, firefighters, and nurses.

Ancillary objectives: supply 2,250 housing units valued at $750 million across greater Los Angeles. These homes are predominantly for first-time buyers making from 80 to 200 percent of the region's median income. Estimate of $27 million in increased sales tax revenue, annual property tax revenues of more than $1.3 million and more than 3,750 construction jobs.

Signature projects:
Puerta del Sol, a 165-unit condominium/loft community in Los Angeles that received a direct investment in 2004 from the first Genesis Workforce Housing Fund. Puerta del Sol opened November 11, 2006.
Community Partner/Joint venture developer: community based developers, public-private partnerships
Returns (financial, social and environmental): 2,250 housing units, estimate of $27 million in increased sales tax revenue, annual property tax revenues of more than $1.3 million and more than 3,750 construction jobs.

Source: http://www.phoenixrg.com/news/item.php?id=349,
http://www.genesisla.org/fund.php?nav=1,

Asset Class: Equity Real Estate

UrbanAmerica

Asset size: Fund I $120 million Fund II $400million

History: UrbanAmerica was founded in 1998 by Richmond McCoy and Hal Reiff to realize the market opportunities of the inner cities, they saw "urban center" where others saw inner city to serve as a conduit of institutional capital into urban centers nationwide. The founding partners are:

· John Utendahl, Chairman, UrbanAmerica LP; Chairman & CEO, Utendahl Capital Partners
· Joseph Flom, Esq, Partner, Skadden, Arps, Slate, Meagher & Flom LLP
· Joseph Elmaleh, Private Venture Capital Investor
· Richmond McCoy, President & CEO/CIO, UrbanAmerica LP
· Hal Reiff, Executive Vice President & CFO/COO, UrbanAmerica LP

Asset Class: Equity real estate

Structure: For-profit fund manager, registered investment advisor, value-added investment vehicle

Pension Fund investors: Undisclosed

Location of investments: Atlanta, California, Florida, New York Tri-State (excluding New York City), Philadelphia, Phoenix, Texas, and Washington, DC Metro National -- areas of concentrated purchasing power and mismatch between consumer demand and supply of goods & services

Investment type: Class A Development, office, retail and mixed use, including a residential component

Ancillary objectives: Social returns as represented by job creation and minority vendor services employed

Signature projects: Eastover Shopping Center, 10 Audrey Ln., Oxon Hill, MD, 249,047 SF shopping center acquired in 2000; Value add:

· Increased rent at lease expiration for several tenants-Foot Locker rent increased 325%, Rainbow rent increased 85%
· Consummated deal to bring full-service police station to site. Increased safety brings better tenants and more customers

Community Partner/Joint venture developer: Fisher Brothers

Returns: Undisclosed

Source: Senior Management, http://www.urbanamerica.com/

Asset Class: Equity Real Estate

Urban Strategy America Fund, L.P., a New Boston Real Estate Fund (USA Fund)

Asset size: $170 million
History: USA Fund was founded in 2004 by New Boston Fund and is led by Kirk Sykes to realize a double/triple bottom line return and had its first closing in 2005. New Boston Real Estate Fund was originally founded in 1993. Prior to 1993 and dating back to the 1950's the principals of New Boston Fund were active in urban redevelopment.
Structure: For-profit fund manager model, subsidiary of an established real estate company
Pension Fund investors: Massachusetts Pension Reserves Investment Management Board, Connecticut Retirement Plans and Trust Funds (CRPTF), City of Hartford,
Location of investments: Boston, MA, North Kingston, RI, Norfolk, VA, Rocky Hill, CT. Other markets include primary and secondary locations in the Mid-Atlantic and Southeast.
Investment type: mixed-use office, for sale and rental multi-family residential, retail, warehouse/distribution
Ancillary objectives: workforce housing, facilitation of low-income tax credit affordable housing rentals, community centers, construction jobs, back office administrative jobs, warehouse distribution and retail, community organizations, property management, job training, nursing, property management, minority & women-owned construction, energy efficient and environmentally sustainable green development

Signature projects: Olmsted Green, Parcel 24 and Quonset
Olmsted Green (former Boston State Hospital) will transform 42 acres in Boston, with the creation of homeownership opportunities, jobs, nursing care, training, and health and fitness facilities. Community partner is Lena Park Community Development Corporation. Project will be built in four phases over four years with an estimated total cost of $143.5 million. The infrastructure required for the project will be publicly financed, including $37 million of institutional development by others.

Community partners/Joint venture developers: Bonaventure Realty Group, Lena Park Community Development Corporation, Asian Community Development Corp.

Returns (financial, social and environmental):
1. Create housing for sale and for rent that address all levels of affordability. 2. Permanent and construction jobs created for local residents, women and minorities. 3. Ability to stimulate third party and economic development in an area, thereby creating a ripple effect for each development. 4. Project components that offer goods, services and amenities that are missing or underrepresented in a community. 5. Investments that lever the creation of infrastructure to benefit the broader community (i.e. transit, traffic, utility, recreation, etc. improvements). 6. Undertake projects of a scale that have a significant impact on the surrounding community. 7.Invest in projects that offer residents job and career advancement at all levels of employment and structure local partnerships to facilitate this goal. 8. Capitalize on institutional anchors in a community by offering supportive services that can benefit the community and the institutions (i.e. administrative back office or institutional housing). 9. Partner with local CDC's and developers to assure participation by the local community in all aspects of the project economics and approvals. 10. Create retail and office environments by blending local and national tenants to create stability and growth. 11. Empower local minority and women development entities by offering expertise and financing in a joint venture structure. 12. Develop and acquire "Green Buildings" that utilize sustainable and energy efficient technology.
Source: Senior Management, www.newbostonfund.com

Asset Class: Private Equity (Early and Later Stage Venture Capital)

Banc of America Capital Access Funds (BACAF)

Asset size: Not available

History: Formed in 1997 and currently operating as a division of the Bank of America Principal Investing Group, Banc of America Capital Access Funds manages a fund-of-funds investment vehicle that invests in private equity and venture capital funds that can provide market returns while also investing in underserved markets in the United States.

Structure: For-profit fund manager model, a fund of funds

Pension Fund investors: Refer to www.bacapitalaccessfunds.com

Location of investments: California, located in or employ residents of low to moderate-income geographies

Investment type: Investments are made in companies that are located in or employ residents of low to moderate income geographies, owned or managed by ethnic minorities, owned or managed by women focused on delivering products or services to an ethnically diverse customer base; or located in areas—urban or rural—with limited access to investment capital

Ancillary objectives: job growth, companies owned by women or ethnic minorities, percentage of employees with health insurance, aggregate payroll

Signature projects:

Community partners:

Returns: not publicly disclosed

Source: Senior Management, (http://www.bacapitalaccessfunds.com/index.asp)

Asset Class: Private Equity (Early & Later Stage Venture Capital)

CDVCA Central Fund

Asset size: $6 million
History: "CDVCA was formed in 1993 and incorporated as a not-for-profit in 1995, CDVCA promotes use of the tools of venture capital to create jobs, entrepreneurial capacity and wealth to advance the livelihoods of low-income people and the economies of distressed communities" (www.cdva.org).

Structure: CDVCA Central Fund is a for-profit fund subsidiary of the not-for-profit, Community Development Venture Capital Association (CDVCA).

Pension Fund Investors: none
Location of investments: National

Investment Type: venture capital (early and later stage) through a Fund of Funds and co-investments.
Fund of Funds investments are made in CDVCA member funds that have missions of creating high-quality jobs and wealth that improve the lives of low-income people and benefit distressed communities. Co-investment Fund investments, as direct equity investments made with other funds, are made in companies that meet CDVCA's financial and social criteria in any industry sector except real estate. Both types of investments have a minimum size of $250,000.

Ancillary objectives: Creating high-quality jobs and wealth that improve the lives of low-income people (less than 80% of area median) and benefit distressed communities. Investments are made in any industry sector except real estate. Fund encourages minority and women ownership, environmentally sustainable businesses, production of products useful to communities, and promotion of socially responsible business practices.

Signature projects:
Fund of Funds investment:
"Coastal Ventures II, LLC is one of CEI Ventures' two venture capital funds which have combined total commitments of $25.54 million. These funds make equity investments in companies exhibiting the potential to grow profitably and provide attractive financial returns. Portland, Maine-based CEI Community Ventures manages a $10M venture capital fund. The Fund invests from its own fund in amounts ranging from $100,000 to $500,000. Working with partner funds, we also help coordinate and/or lead larger financings (as much as $5 million) with investors that share our outlook and criteria" (www.cdvca.org).
Co-Investment:
Ricochet Manufacturing, Inc., a Philadelphia, Pennsylvania-based company, manufactures protective apparel for EMS and Fire Rescue Professionals.

Community partners: Community Development Financial Institutions Program, New Markets Tax Credit Program, Venture Capital Program, Community Reinvestment Act

Returns (financial, social, and environmental): The CDVCA industry as a whole has created 24,000 new jobs in underserved areas of the nation.

Source: CDVCA website: www.cdvca.org

Asset Class: Private Equity (Early & Later Stage Venture Capital)

JP Morgan Bay Area Equity Fund (BAEF)

Asset size: $75 million
History: JP Morgan Bay Area Equity Fund founded in 2003 as part of the Bay Area Family of Funds to realize double bottom line returns. The fund started investing in 2004.
Structure: Contractual model, for-profit fund manager (JP Morgan H&Q) contracts with the not-for-profit fund sponsors (Bay Area Council and the Alliance for Community Development)

Pension Fund investors: Contra Costa County Retirement System

Location of investments: Low and moderate income neighborhoods in the Nine-county Northern California Bay Area
Investment type: Investments are made in private, primarily mid-to-late stage growth companies across all industries, with a focus on technology, healthcare, clean tech and consumer products and services located in, or adjacent to low and moderate income neighborhoods.

Ancillary objectives: Local hiring, particularly qualified residents of low and moderate income communities employee development and training, employee education on healthcare, profit sharing etc., community workshops on financial literacy, contracting with women and minority-owned suppliers and contractors, energy conservation, and resource efficiency, green building design, construction and operation, training for advancement, and continuing education.

Signature projects:
$2.2 million in venture capital to Elephant Pharmacy, it has generated 70 new entry-level jobs for the local community. The pharmacy is an innovative, start-up business, combining traditional pharmaceutical products with complimentary and alternative products, such as food, flowers, and consulting health practitioners. This combination of merchandise and service is targeted to health conscious consumers. The business model for the pharmacy meets the requirements for BAEF's double bottom line because store is located in or near a low- and moderate-income geography in the Bay area; the majority of new jobs are entry-level positions with compensation that exceeds the livable wage ordinances in Berkeley, Oakland, and San Francisco; and staff benefits include health care, equity-sharing, and training.**"** OCC Report, "Bay Area Funds Focus on Double Bottom Line (http://www.occ.treas.gov/cdd/ezine/summer05/doublebottom.html).

Community partners: Bay Area Alliance for Community Development, Bay Area Community Investment Network (BACIN).
Returns: Results as stated by the not-for-profit sponsor (www.bayareacouncil.org):

- $11.8 million invested in 7 companies to date, producing 69 jobs
- Liquidity event for an investment in the health-services industry
- Launched a state, regional, and local effort to keep potential investment Solaicx, a solar company, in California to create over 350 jobs
- Joined with portfolio company, Five Prime Therapeutics, to convene meetings of corporate, government, and nonprofit entities to coordinate community engagement initiatives in Mission Bay
- Joined with portfolio company, Efficas, to highlight successful launch of a new high-value agricultural crop in Contra Costa County"

Source: BAEF senior management, www.jpmorgan.com, OCC Report "Bay Area Fund Focus on Double Bottom Line", http://www.bayareacouncil.org/site/pp.asp?c=dkLRK7MMIqG&b=995761

Asset Class: Private Equity (Early & Later Stage Venture Capital)

Massachusetts Capital Resource Company (MCRC)
Asset size: Committed capital over $500 million

History: "MCRC was formed by the Massachusetts-based life insurance industry in 1977 in response to a study of the region's economy produced for the Massachusetts Task Force for Economic Development. MCRC is a private company which promotes economic development by providing growth capital to established local businesses throughout the Commonwealth"

Structure: For-profit Limited Partnership Fund

Pension fund investors: None; the Fund is fully capitalized by the Massachusetts Life Insurance Industry

Location of investments: Massachusetts, with 2/3rds of the capital committed historically to disadvantaged areas

Investment type: "MCRC is a source of risk capital for Massachusetts business and invests across the entire range of business development financings. Although MCRC can make senior loans to mature companies on a fixed rate and long-term basis, MCRC focuses on making subordinated loans to rapidly growing profitable companies in need of equity type funds or to assist management buyouts and acquisition financings. MCRC also provides equity capital or convertible debt to young organizations which have outgrown initial capital infusions". MCRC generally seeks a current return through a debt instrument. When asked to take an equity risk, we will seek an open ended return through direct equity ownership, warrants to purchase common stock or convertible securities.

Ancillary objectives: Job creation: MCRC has created more than 18,000 jobs essential to the economic growth of the Commonwealth.

Signature projects: Wang Laboratories, at an early stage in its growth, would have failed without essential growth capital from MCRC. As a part of the transaction, Wang moved to Lowell, Massachusetts, a severely depressed community, which saw dramatic improvement from Wang's presence.

Community partners: Through its affiliate, the Mass Life Initiative, works closely with community development corporations and affordable housing organizations across the Commonwealth.

Returns: Over the past twenty years, MCRC has invested approximately $400 million in 219 companies located in 98 communities resulting in the creation of over 15,000 jobs.

Source: http://www.masscapital.com/Overview/overview.htm

Asset Class: Private Equity (Early & Later Stage Venture Capital)

Oregon Investment Fund, a Credit Suisse Fund of Funds (OIF)

Asset size: $105million

History: In July 2003, HB 3613 passed the Oregon State Legislature and enacted a mandate for the Oregon Investment Council ("OIC") to design a $100m program that encourages the growth of small businesses within the state of Oregon. To accomplish this mandate the OIC chose to develop a fund of funds, the Oregon Investment Fund ("OIF"). The fund (established in 2004), was capitalized with funds from the OIC, and has been committing capital to private equity and venture capital funds that will in turn invest in companies located primarily in the state of Oregon, as well as the Northwest region. In addition, a percentage of the assets of the OIF will be invested directly into operating companies alongside the OIF's private equity and venture capital managers. The OIC chose Credit Suisse's Customized Fund Investment Group to develop and manage this Fund on a discretionary basis.

Structure: For-profit fund manager model, a fund of funds, Delaware Limited Partnership

Pension fund investors: Oregon Public Employees Retirement Fund (as directed by HB 3613)

Location of investments: Oregon and the Pacific Northwest

Investment type: Growth of small and medium sized businesses in Oregon and the Pacific Northwest

Ancillary objectives: jobs, investments in start-up companies that come out of Oregon universities and colleges.

Signature projects: Sherbrooke Capital: focuses on the health and wellness sector. This fund invests in areas of both health (fitness and "wellness") and consumer products. Sherbrooke is designed to capitalize on these areas in Oregon as well as throughout the country.

Community partners: Oregon Economic and Community Development, Oregon Entrepreneur Forum and many others

Returns: Not publicly disclosed, proprietary fund and client information

Senior management, http://www.oregoninvestmentfund.com/about_oif.htm

Asset Class: Private Equity (Early & Later Stage Venture Capital)

SJF Ventures (SJF)

Asset size: Fund I: $ 17.1 million Fund II: target $30 million

History: SJF was founded in 1999 by Dave Kirkpatrick, an environmental entrepreneur, and Rick Defieux, a successful venture capitalist in the environmental sector. The original vision of SJF was to create quality jobs in low-income communities through equity investments in environmental businesses. SJF has made investments in 24 companies, which collectively have created over 1000 good paying jobs in the Eastern United States. SJF's second fund invests in clean technology, business services, and premium consumer products companies that use environmental or workforce innovation as a competitive advantage. SJF Advisory Services, an allied non-profit organization founded in 2001, assists SJF portfolio companies and hundreds of other companies annually with entrepreneurial assistance and workforce and sustainability services.

Structure: SJF has pioneered the combination of for-profit venture funds —SJF Ventures I and II, both structured as ten-year limited partnerships with a 501(c)(3) not-for-profit, SJF Advisory Services. Institutional capital received from the Bank of America Community Development Corporation.

Pension Fund investors: None to date. State of Pennsylvania has invested in Fund II through the Pennsylvania Department of Economic & Community Development. Institutional capital from a fund of funds, major banks, foundations, and development finance trade associations.

Location of investments: Primarily Eastern U.S though will invest nationwide.

Investment type: Investments are made in private, primarily mid-to-late stage growth companies. SJF invests in expansion stage companies with annual revenues of $1 - 20 MM that are at a growth inflection point. SJF's initial investment in a company ranges from $500,000 to $1M, usually in the form of preferred stock or subordinated debt with warrants.

Ancillary objectives: With its investments in clean technology and workforce innovators, SJF seeks to create quality entry-level employment and positive environmental benefits alongside risk-adjusted market rates of return for investors.

Signature projects: Representative companies include: Intechra (Jackson, MS), providing IT asset disposition services and electronics waste recycling nationwide (200 employees); Ryla Teleservices (Kennesaw, GA), a contact center using an engaged workforce to deliver quality call center services domestically (375 employees); Home Bistro (Plattsburgh, NY), direct mail gourmet frozen food (89 employees)

Community partners: SJF Advisory, CEI Ventures (Portland, ME), Boston Community Capital, Community Development Venture Capital Alliance, Opportunity Finance Network.

Returns (financial, social, environmental): SJF II is targeting a risk-adjusted market rate of return (high teens IRR) for investors; Social returns: Over 1,200 good paying jobs created since SJF investment, of which 67 % are from minority groups and 77 % are women. Seventy-one % of the jobs created by SJF portfolio companies are entry-level positions; 75% of SJF portfolio companies pay 50% or more of health care premium costs. Eight companies have implemented broad-based stock option plans. Environmental benefits include electronics waste recycling, energy efficiency consulting, solar energy installation, reduced water and fertilizer use by vegetable growers and nurseries. Source: SJF Management, http://www.sjfund.com

3 Importance of scale

Investment intermediaries and pension funds each need scale (size or magnitude) to make investing in the urban market viable and profitable. An institutional investor will only make an investment if it meets the minimum amount. Otherwise an investment is not worth pursuing given their need to place billions of dollars in the market and meet their return objectives. Similarly, investment intermediaries need scale to be able to organize and produce developments and ventures of size that yield the targeted returns.

Investment intermediaries serve the purpose of organizing and producing investments of scale in the emerging domestic markets. Intermediation between capital and the market is inherently needed. To better understand what we mean by an investment intermediary we refer to the academic literature. Davis and Steil (2001, 446) define intermediation in the *public markets* as:

> The process whereby end-providers and end-users of financial claims transact via a financial institution, rather than directly via a market. In securities trading, refers to execution of an investor's trade with the assistance of an intermediary, such as a broker-dealer.

Within the *private emerging domestic markets*[2], an investment intermediary is needed to broker deals between the massive institutional investor and the private urban investment community. Clark (2000, 192) narrows the definition noting that:

> …intermediaries are functionally located between pension funds and financial services markets offering expertise in project-based investment management and management of the flow of funds.

The investment vehicle intermediates in this transaction-driven process and facilitates the flow of pension fund money into the investment community. The investment vehicle reaches scale in their investments by pooling assets, reducing transaction costs, and partnering with community development corporations. Without an intermediary these investments could not successfully impact the community and achieve the targeted returns.

[2] The Milken Institute defines the Emerging Domestic Markets to a market that "refers to people, places or enterprises with growth potential that face capital constraints due to systematic undervaluation as a result of imperfect market information. These markets include ethnic- and women-owned firms, urban and rural communities, companies serving low-to-moderate-income populations, and other small- and medium-sized businesses" (http://www.milkeninstitute.org/research).

Barriers to reaching scale in the emerging domestic markets include access to accurate information and high transaction costs. Daniels (2005) has identified *market barriers* that help explain why capital does not easily flow to low-income neighborhoods that includes:

1. Inadequate risk management. Conventional investment vehicles do not adequately pool and spread risk among a range of sophisticated institutional investors;

2. Managers do not price the transaction up to the associated risk;

3. Information and transaction costs. Often it costs too much to find out who are the players and where the opportunities lie within the inner city;

4. Market prejudice. With "pre-judgement" and a lack of good information a conventional manager may see lack of growth, uncertainty, and no opportunity;

5. Government regulations that can deter development in the underserved markets. For example, inadvertent tax and regulatory policies, and transportation and infrastructure policies can have the unintended consequence of lowering the cost of greenfield development to developers, and place a hidden cost on potential underserved neighborhoods.

Allen and Gale (2000, 474) lay out that an investment intermediary plays a role in overcoming these informational barriers:

> … intermediaries assume the role of advisers, bridging the gap between the investors' lack of knowledge and the expertise required to get the most out of sophisticated markets…(w)ithout intermediaries, the informational barriers to participation would prevent investors from reaping the benefits of the new markets, and the markets themselves might not survive. At the same time, financial markets reduce costs for the intermediaries and their customers and allow them to hedge risks more effectively than they previously could.

To overcome imperfect information and high transaction costs (in which small size of deals means income cannot cover costs) the intermediary and the investor comes together in a symbiotic relationship. Each needs the other to make the investments work. In this sense they provide each other with scale—the crucial factor that make urban investments viable and profitable. The institutional investor provides the investment intermediary with scale—in terms of large amounts of capital. This institutional capital is fundamental in its ability to lock in scale as these are illiquid, high-risk, transactions with returns typically seen six to seven years out. The investment intermediary also provides scale to the investor in organizing and producing urban development projects of significant size that impact the community and produce financial returns. The later is the more difficult offering and one that we will deconstruct in subsequent sections.

An investment intermediary achieves scale through their product knowledge expertise and access to local information, something the institutional investor lacks. Arrow (1984,142) points out "information is not merely a good that is desired and acquired but is to some extent a commodity like others whose markets we study". It is this commodity that the intermediaries provide to the institutional investor— as a pension fund does not have the necessary expertise. An investment intermediaries' competitive advantage is in overcoming barriers by pooling assets, establishing a niche in the marketplace, and minimizing their transaction costs through experience.[3] An investment intermediary, with on the ground knowledge, can also help create a market that previously did not exist. Merton and Bodie (2004) refer to the "innovation spiral" and the role of intermediaries as providers of new financial markets.

An example of an investment intermediary that helped create a market is the Community Preservation Corporation (CPC), a not-for-profit community developer in New York City. CPC was created to fill the gap left by traditional bank lenders in the 1970's and has since expanded its base of capital providers with permanent financing from public sector pension funds such as the New York City Retirement System. CPC organizes and produces scale in their ability to nurture development specialists. Before CPC came into being no one thought of specializing in converting dilapidated buildings into rentals on a larger scale. With the help of CPC financing, relying on CPC's community development expertise and backing from institutional investors, subcontractors on rehabilitation jobs became general contractors and then owners through their value added in efficiently rehabilitating properties.

CPC helped create a market that previously did not exist, private businesses were now specializing in acquiring and rehabilitating run down buildings. CPC took advantage of smaller-scale construction projects on vacant lots in low-and moderate-income neighborhoods. This was a sector often of no interest to a larger conventional developer. However, in dense urban environments small buildings or lots are often the most abundant (CPC Corporate Overview 2005). CPC was able to organize and produce scale with their market knowledge—something the institutional investor relies on the investment vehicle to provide.

[3] Clark (2005) notes that money, like mercury, runs together to benefit from opportunities attainable through the transaction process. Similarly, investment vehicles benefit from pooling assets and limiting transaction costs.

Urban investments are higher risk given their location in the underserved markets. Investment vehicles with proven track records know how to manage and redistribute this risk. Investment vehicles that produce above average financial results, placing them in the top quartile against their peers, are those with proven track records in their ability to manage risk and return.

Gaining access to quality investment vehicles can be prone to *adverse selection*—when only the lower quartile managers (and unsophisticated investors) are left in the selection pool. The selection process is one that relies on reputation, trust, and information. Relationships are key in the fund manager selection process. Often the investment structure is not transparent to the institutional investor, and in the case of a commingled fund, can be formulated only after all investors are in the fund. In this scenario a pension fund chooses to invest with the intermediary based on their proven track record of assets under management, number of years in existence, and performance.

Investment intermediaries and institutional investors interconnect to achieve scale in urban investments. In this section we have drawn out the importance of scale and the role of intermediaries in that process. The institutional investor provides the intermediary with significant long term and patient capital that allows them to scale-up their investments. Without institutional capital to lock-in scale, these investments would not be viable. For-profit investment vehicles seek significant amounts of capital as fees generated are based on assets under management. Intermediaries can transform neighborhoods and companies, impact the community, and first and foremost, achieve targeted returns to the institutional investor. To better understand how scale is achieved in urban investments we now turn to the types and structures of the investment intermediary.

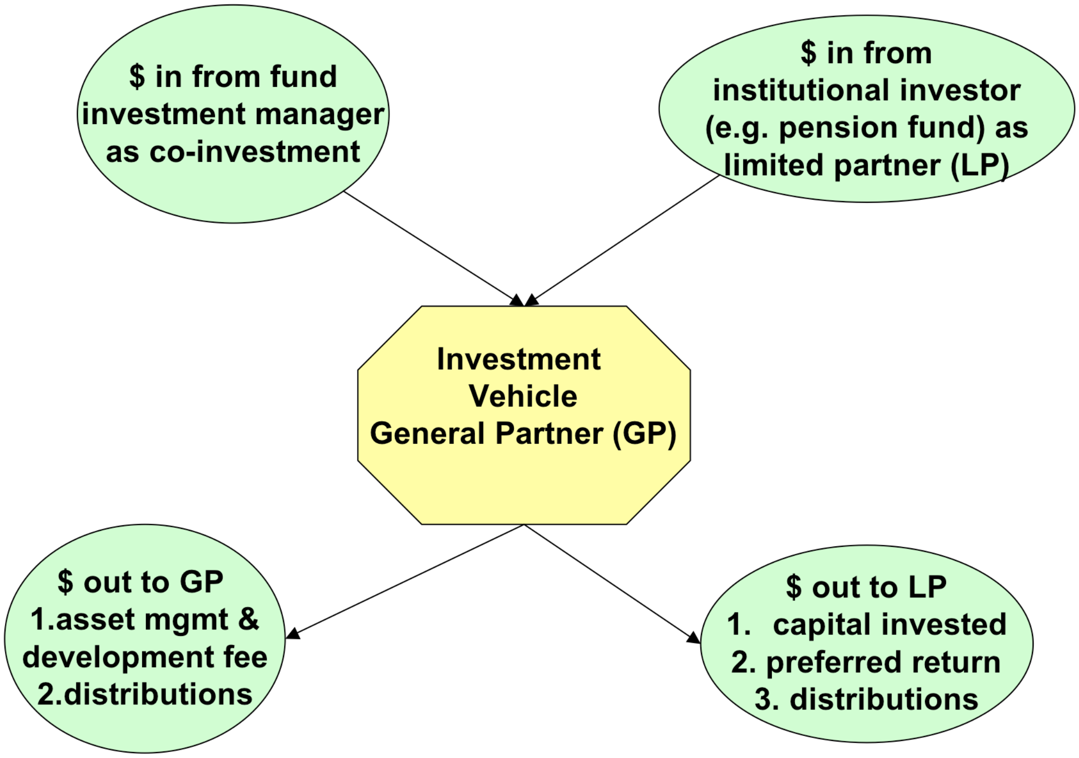
4 Structures of investment vehicles

Investment vehicles intermediate between the public sector pension fund and the investment venture. The investment intermediary has the financial engineering expertise to achieve scale and minimize risk—making the investment attractive to the institutional investor.

Merton (1995, 2) puts forth six core economic functions performed by a financial intermediary or in this case termed financial system that include: "A financial system provides a mechanism for the pooling of funds to undertake large-scale indivisible enterprise…A financial system provides a way to manage uncertainty and control risk". Investment intermediaries that build funds within a framework for scale and risk diversification are well positioned to reach the targeted financial and social returns. Investment vehicles manage their risk by pooling, spreading, and pricing up to risk.

Private equity real estate and private equity funds (venture capital) are built in different ways—in terms of both the flow of capital and organizational (legal) structure. Figure one illustrates the flow of funds between the institutional investors (e.g. pension fund, bank, insurance company, foundation) and the investment vehicle. The diagram shows the financial relationship and flow of income generated between the institutional investor and the investment intermediary.

Figure 1 Distribution of money between investment vehicle and investors



As compensation for managing the fund the investment intermediary receives what is generally referred to as a management fee or asset management and development fee. When the project exits (sale of real estate development or sale of company) the general partner and limited partners receive profits as per the "offering memorandum". The General Partner must first return the principal to its investors before taking a share in the profits—distributions or sometimes called the "carry".[4] After the principal is paid back usually an additional preferred rate of return or "hurdle rate" is first distributed to the limited partner before the general partner shares in the remaining profits—typically mid to high teen returns (The Double Bottom Line Handbook 2007).

[4] "Sometimes called "the carry", the carried interest is the Fund Manager's incentive profit. {The typical private equity fund} generally provides for returns on investment to be split roughly 80 percent to the limited partners and 20 percent to the general partner…"(The Double Bottom Line Handbook 2007, 143).

The investment fund manager manages the fund making private investments, under their control, into companies or real estate developments. The fund manager, or their parent company, can also make a "co-investment" in a fund. As such, the fund manager's interests align directly with those of the investor. Incentive-based fee structures promote similar goals between the investment fund manager and the investor.

An institutional investor (e.g. public sector pension fund) can be referred to as a limited partner (LP), as they assume a limited partner role in the fund and commit capital alongside other investors to the limited partnership. In its legal organizational structure, the investment fund vehicle can be referred to as the General Partner (GP) in a Limited Partnership (LP) legal structure or a Managing Member in a Limited Liability Company (LLC) legal structure. An LLC is a crossbreed between a partnership and a corporation. Generally, the investment fund manager is referred to as the GP and will be in this discussion. Figure two outlines the operating legal structure of the two fund legal models.

Figure 2 Legal structure of investment vehicles

Limited Partnership (LP)	**Limited Liability Company (LLC)**
For-profit fund manager legally termed: *General Partner (GP)* (SEC filing as registered investment advisor)	For profit fund manager legally termed: *Managing Member* (SEC filing as registered investment advisor)
Institutional investor legally termed: *Limited Partner*	Institutional investor legally termed: *Non-managing member*
Not-for-profit fund sponsor termed: *Special Limited Partner*	Not-for-profit fund sponsor termed: *Special Member*

Source: Hagerman modified from original (Daniels 2004).

The investment intermediary links the institutional investor to the revitalized area through different operating models. It is important to recognize that there are various frameworks for building an investment fund that work together or independent of a not-for-profit entity. The

"Double Bottom Line"[5] industry refers to four different approaches to the oversight of an investment fund. Economic Innovation International, a Boston based consulting firm, has identified four operating models. Table one illustrates these four models: the contractual model, the ownership model, the legislative model, and the fund manager model. In this study we generally refer to the investment intermediary as the manager of the fund that operates within the "for-profit fund manager model" and without a "not-for-profit fund sponsor".

Table 1 Operating models of investment vehicles

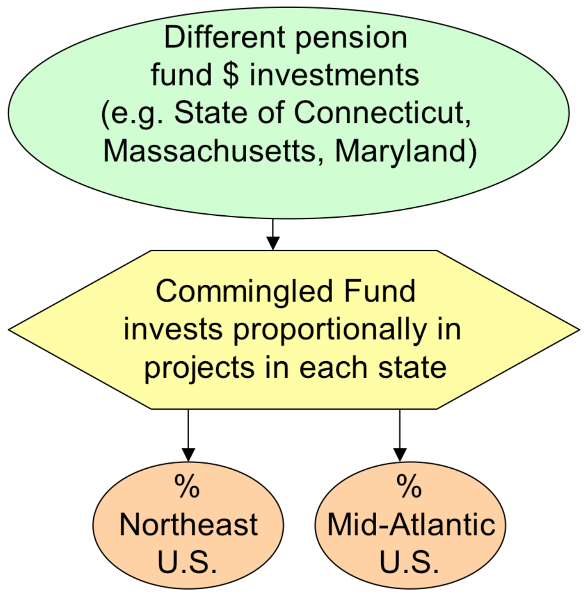
Legal Model	Structure	Strengths	Weaknesses	Examples
Contractual Model	Fund Sponsor contracts with a proven fund manager to serve as fund manager, and the Fund is then structured either as an LLC or Limited Partnership	Proven outside Fund Manager	Fund Manager can run off with the idea with no accountability to not-for-profit sponsor, if on-going Funds are not built into the contract	Genesis LA Funds, Bay Area Family of Funds, San Diego & Sacramento
Ownership Model	Nonprofit Community Fund Sponsor owns for- profit Fund Manager	Nonprofit Community Fund Sponsor has control over Fund Manager	Institutional investors may not have confidence in the not-for-profit manager	Community Preservation Corporation/CPC Resources Coastal Enterprises/CEI Ventures MA Housing Investment/MHIC Equity LLC
Legislative Model	Fund criteria and tax deal codified in state legislation	Good option with a sympathetic legislature	Not an option with an unsympathetic legislature	MA Life Initiative, MA Property & Casualty Initiative
Fund Manager Model	Fund manager operates without a nonprofit Fund Sponsor	Investors like returns, fund managers, and Double Bottom line concept	Who is monitoring Second Bottom line?	American Ventures, CA Urban Investment Partners, Canyon Johnson Urban Fund, Paradigm Properties, Urban America, Yucaipa Fund, SJF Ventures

Source: (Daniels 2004)

In the for-profit fund manager model, different operating structures exist to achieve scale. A fund established as a commingled limited partnership reaches scale by pooling assets from a variety of investors in one fund thus enabling the fund to take a larger position in the investment venture. Reciprocal targeted investing is a feature of a commingled fund. The fund manager targets investments in geographic areas based on the limited partner's investment percentage. Figure three illustrates a commingled for-profit fund structure.

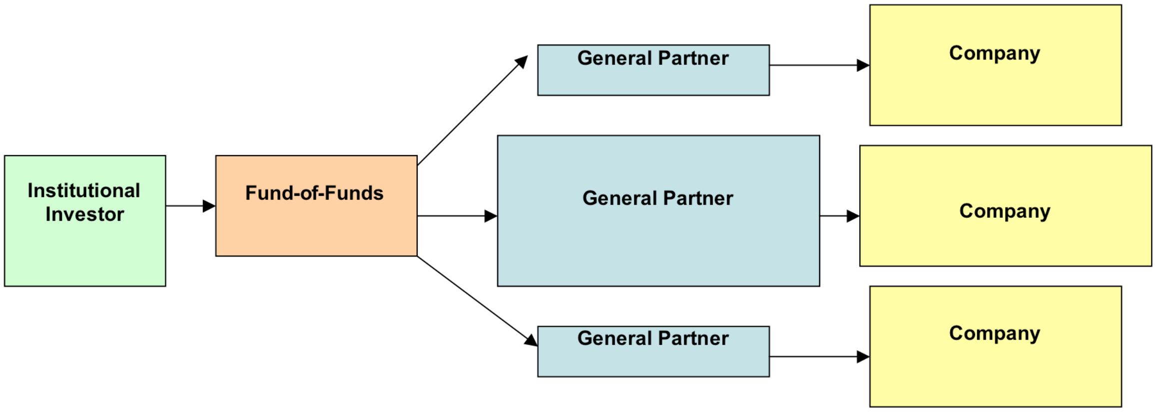
[5] The industry that includes "Double Bottom Line Private-Equity Funds" that produce two bottom lines: the first bottom line is a risk-adjusted, market-rate of return for institutional investors…the second bottom line includes positive economic, social, and environmental benefits produced by the investment…"(The Double Bottom Line Handbook 2007).

Figure 3 Commingled fund structure with reciprocal targeted investing



Another structure in private equity investing is through a fund-of-funds that provides an opportunity for a fund to achieve scale and diversify its investments. This fund structure is illustrated in figure four.

Figure 4 Fund-of-funds structure



Source: Hagerman modified from CalPERS original (http://www.calpers.ca.gov/)

A fund-of-funds allows for diversification in that a pension fund can be invested in ten different funds but only has to actually make an investment in one fund.[6] Examples of different investment vehicles that operate through these different fund structures are identified in the following section.

[6] An institutional investor can also choose to make an investment directly in a company either as a co-investment with a general partner or without other investors directly into a company.

5 Making the link to urban revitalization

Investment fund managers provide scale and impact urban communities through clearly defined business models that invest institutional capital in debt-based affordable housing investments, large-scale urban development projects, and mission-oriented companies.

Fixed Income Investment Vehicles

In thinking about investing in urban revitalization through debt-based affordable housing products we examine the investment vehicle CPC. CPC was founded in 1974 after David Rockefeller led a study with New York City officials and other leading commercial banks to address the lack of apartment building financing (construction/rehabilitation loans) from traditional savings banks. During the mid-seventies the City was losing 25,000 units a year due to abandonment as building incomes could not make the necessary upgrades and repairs in declining neighborhoods. As CPC President Michael Lapin commented, CPC's founders had a clear vision of their mission, "...to finance the rebuilding of New York City's deteriorating neighborhoods". CPC links institutional investors to the secondary affordable housing market. The investment intermediary makes construction loans and sells permanent loans to participating investors. In this way, CPC acts as a bridge between government and the financial community to encourage investment in distressed communities.

For example, the New York City Retirement System pension fund (NYCERS) makes forward-rate commitments and commits to buy a loan, up to 24 months at a long-term lock-in interest rate, from the Community Preservation Corporation.[7] CPC, with the guaranteed take-out financing in place, makes the construction loan to its contractors for the gut-rehabilitation of a dilapidated apartment. After construction, CPC converts the loan to permanent financing and sells it at par to NYCERS. The investor relies on CPC for their understanding of the neighborhood, developers, rent regulations and operating costs of the project (Hagerman 2005). In these investments the ultimate measure of success transpires when traditional markets re-enter the underserved neighborhood, such as local banks once again financing the revitalized area.

[7] NYCERS commitment is backed by the State of New York Mortgage Agency commits to insure the loan.

Equity Real Estate Investment Vehicles

In terms of equity real estate, the industry has matured with funds exiting and able to demonstrate track records. In many cases they are now starting second and third funds.[8] In some cases urban private equity funds are a subsidiary of a traditional real estate investment firm with long standing track records. In other cases the firms may have started their first economic development fund with seasoned staff from traditional real estate firms. The industry is competitive and has grown to the extent that real estate and general consultants are including "urban investments" in their information databases. Similar to tracking traditional investments consultants are now aggregating information on urban offerings.

Equity real estate funds invest in the development, re-development, and acquisition of mixed-income, mixed-use, transit-oriented community development in retail, housing, industrial, and office projects. They bring expertise in the form of property management, financial analysis, environmental engineering, urban planning, architectural design, legal, and portfolio management skills. The fund managers are registered investment advisors and can often partner with a joint venture developer and a community development corporation. An equity real estate fund's value-added is their ability to deliver projects on time and under budget, access state and federal subsidy programs, and produce the financial and social goals.

One of the first urban real estate private equity offering aimed at achieving both a financial and social return was the UrbanAmerica LP Fund I. UrbanAmerica has significant experience in putting institutional capital into urban commercial real estate and distinguishes themselves as "the first national conduit of institutional capital into urban commercial real estate". Their first equity real estate fund was created in 1998 and they have successfully exited two of their funds and are now in their third fund. The firm is a minority-controlled registered investment advisor (UrbanAmerica 2005).

Another example of an equity real estate fund is the Urban Strategy America (USA) Fund, L.P. that grew out of a traditional real estate firm, the New Boston Real Estate Funds. New Boston is a 15-year old real estate investment management and development firm. The firm

[8] Pacific Coast Capital has now started its Smart Growth Fund IV with $740 million of capital under management. MacFarlane partners has $9.7 billion under management and Canyon Johnson has $900 million.

started as a local Boston developer and now invests throughout the Eastern U.S. with close to $1 billion of equity under management. Dating back to the 1950's the principals of New Boston Fund were active in urban redevelopment. The USA Fund, established in 2004, is the firm's first fund that seeks to achieve both a financial and a social return. The Fund has raised $170 million in commitments with $50.7 million specified for investment (USA Fund Portfolio Update 2006). An investment vehicle organized as a commingled limited partnership is the Urban Strategy America (USA) Fund. The targeted geographic diversification is the northeast, mid-Atlantic and southeastern United States. Projected investments by state include: 30% in the mid-Atlantic region (Washington DC, Virginia, and Maryland) 30% in Connecticut, 25% in Massachusetts, and 15% in other parts of the country (USA Fund Executive Summary 2005). The fund has outlined 12 measures of success that map out the social and environmental goals of the USA Fund.

To be able to successfully serve as the link between institutional investors and the revitalized area, investment fund managers create a niche for themselves in the marketplace. For example, Cherokee Investment Partners specializes in the cleanup and sustainable redevelopment of contaminated properties commonly known as brownfields.[9] Originally in the brick manufacturing business, Cherokee founders turned to soil remediation after purchasing a brick plant located on petroleum-contaminated soil. By 1990, they became the largest soil remediator in the mid-Atlantic region of the United States. In 1993, company founders formed Cherokee Investment Partners and began to buy contaminated industrial sites, remediate them and return them to productive use. Cherokee has successfully raised four funds totaling more than $2 billion, enabling the firm to invest in environmentally impaired sites nationally and internationally.

An equity real estate manager's success in connecting investors to the revitalized neighborhood can be a result of the firm's legal framework. CPCR is another example of an urban real estate private equity fund. CPCR's framework falls within the ownership model (referred to in table 1) in which the not-for-profit manager, CPC, owns the for-profit

[9] "According to the EPA, a brownfield is an abandoned or underused property where reuse is complicated by the presence or potential presence of environmental pollutants. Brownfields include abandoned factories, gas stations, oil storage facilities, dry cleaners and other industrial sites where hazardous materials were utilized" (Cherokee Investment Partners 2005 Sustainability Report).

subsidiary CPCR. CPC has been in existence since 1974 as a not-for-profit mortgage lender with entrenched relationships in the neighborhoods they serve. In 1992 CPC was capitalized with $2 million making equity investments in which it owns and develops property in the same areas in which CPC makes loans (CPC Corporate Overview 2005).

Private Equity (Venture Capital) Investment Vehicles

Thus far we have examined types of urban equity real estate funds and the expertise they provide in connecting large institutional investors to the revitalized neighborhoods. On the private equity side, investment intermediaries connect investors to mission-oriented growth companies that are linked to emerging economies at the regional, national, and global scale. The success of the investment intermediary is in their ability to find emerging companies that will turn around significant financial returns and also deliver on the social investment criteria.

The JP Morgan Bay Area Equity Fund (BAEF) is a venture capital fund investing in companies in consumer products and services, technology, and healthcare fields.[10] BAEF is part of a "regional" investment initiative in that it aims to foster business ventures linked to the regional economy. The companies should connect urban areas to regional, national, and global economic activity (The Double Bottom Line Handbook 2007). The fund's social mission includes providing jobs, majority entry-level, for low-and moderate-income community residents, as well as staff benefits, health care, and equity sharing (Office of the Comptroller of the Currency 2005) community engagement, financial literacy, as well as regulatory assistance and incentive management.

Another venture capital private equity fund is SJF Ventures that invests in small growing companies with an environmental focus. SJF has received funding from institutional investors such as major banks, foundations, and trade associations. In this example, SJF's market niche is in their ability to link institutional investors to smaller companies. The Fund looks for rapidly growing companies that are in their expansion stage. SJF Managing Director, Rick Larson commented that SJF Ventures invests in "companies that have a $1 million to $20 million in commercial revenue and are at some kind of inflection point for

[10] The JP Morgan Bay Area Equity Fund (BAEF) is part of the Bay Area Family of Funds that also includes a real estate fund and a fixed income fund; Bay Area Smart Growth Fund (SGF) and the Bay Area California Environmental Redevelopment Fund (CERF).

growth, needing working capital to expand." Larson notes that this strategy works well from a financial perspective and is also able to generate additional entry-level employment, a key social goal for the Fund (Hagerman 2006). In this section we have examined the types of investment intermediaries in urban economic development. We now move to a discussion of the role of the community partner in urban investing.

An example of a fund-of-funds is the Banc of America Capital Access Funds. The goal of the fund-of-funds manager is to find opportunities and source deals to different investment vehicles. The fund-of-funds focuses on "people in places who historically haven't had access to capital." This fund-of-funds product seeks out private equity fund managers that have a focus in women, ethnic minorities, urban areas, and low and moderate-income areas. (Hagerman 2006).

Another example of a fund-of-funds private equity investment is the Oregon Investment Fund managed by the Credit Suisse Customized Fund Investment Group, in their Alternative Investment Group. The Oregon Public Employees Retirement System maintains the fund as directed by Oregon state legislation (HB 3613) to establish a $100 million program to foster the growth of small businesses in the state. The Fund analyzes and invests in leading private equity and venture capital funds that "foster the creation and growth of young and maturing companies in Oregon" (http://www.oregoninvestmentfund.com).

6 Role of the community partner

In community based investing the community partner serves as the community development catalyst. The institutional investor (e.g. public sector pension fund) sets broad geographic targets while the investment vehicle narrows those targets to realize the benefits in the community. The investment intermediary collects and deploys the money often working in partnership with a community development organization. The community partner ensures that the investment provides ancillary benefits to their community. While the investment intermediary provides structure in the financial sense, the community partner does so in the geographic sense. In effect the community partner also serves the role of an intermediary. In this case the community organization intermediates between the investment fund manager and the economic development area. For purposes of this discussion we will refer to the community intermediary as the community partner.

The community partner is the essential link for a successful urban revitalization investment venture. They can ensure, for example, that a vibrant urban community includes civic and public spaces for community residents. Embedding a community partner in the deal translates into enhanced communities through investments that improve quality of life in the economic development area. Regional cooperation with municipalities and counties collaboratively revitalizes neighborhoods, improves infrastructure, and accommodates for growth.

In order for neighborhoods to be transformed in a way that positively impacts the community, and yields the targeted financial returns, investment intermediaries partner with not-for-profit groups—community development corporations (CDCs). Investment intermediaries recognize that community organizations have the local insight to transform neighborhoods and promote companies that benefit the community. Community organizations link the investment fund manager to the underserved neighborhood and local government organizations. In doing so CDCs help get investments to scale—allowing for neighborhoods to be significantly improved in the interests of the community. The partnerships empower CDCs, and other community partners, to foster further investment in the community. These organizations serve an important role in ensuring that the urban equity real estate investment or venture capital fund incorporates the needs of the community and realizes the social returns.

Economic development consultants are another kind of intermediary and able to link the investment intermediary with the community partner. An example of such a consultant is Economic Innovation International, Inc. known as a "fund builder" in the community based investing industry. The firm was founded in 1971 to identify and build market solutions to social problems. As noted in the firm's website (www.economic-innovation.com), since its founding the firm has built funds to address social problems, and has founded five industries now adopted by the market. Since January 15, 1997 Economic Innovation has been building what the industry refers to as "Double Bottom Line" private equity funds. Economic Innovation has been a pioneer in building more than $2 billion of these funds that have both a financial and a social objective. The firm has created a model that includes a not-for-profit sponsor organization, a community partner in place to monitor and ensure the social returns are realized.

Economic Innovation International structures the fund so that the not-for-profit sponsor is embedded into the operating agreement and shares in the fund's management fee and carried interest. The sponsor is considered a "special limited partner" (in a Limited Partnership legal framework) or "special member" (in a Limited Liability Corporation legal framework) of the fund depending on how the fund is organized (as defined in figure 2). This not-for-profit sponsor can often be the "community development catalyst" that may identify the development site, seek out the joint venture developer, or provide technical assistance (The Double Bottom Line Handbook 2007). This is in particular is the function of a community partner acting as an intermediary between the investment vehicle and the urban community, as noted earlier.

The first private equity fund incorporating the not-for-profit sponsor model in a contractual arrangement with the for-profit fund manager was Genesis LA. Genesis LA was formed in 1998 by Los Angeles Mayor Richard Riordan and Deputy Mayor Rocky Delagillo after the civic turmoil and Northridge earthquake of the 1990s. The not-for-profit sponsor corporation was formerly established in 2000. Assistant Deputy Mayor, Deborah La Franchi, served as the point person on the project, working with Belden Daniels of Economic Innovation International and a group of civically-minded professionals that later become the Board of Directors, to create the Genesis LA not-for-profit sponsor model. Ms. La Franchi, then served as the first CEO and President of Genesis LA, getting the model and its first three funds off the ground. Now in her capacity as CEO of Strategic Development Solutions Deborah La Franchi partners with Belden Daniels' firm in building "Double Bottom Line" Funds in this country and overseas. Ms. La Franchi commented that, "Genesis LA currently has seven funds with more than $450 million of capital under management with a pipeline of over $1.5 billion in deals. The partnership with fund managers supports a full time professional staff of more than eight without any public or charitable support."

As of 2006 Economic Innovation International has built multiple national, regional family of funds (e.g. Genesis LA Family of Funds, Bay Area Family of Funds, San Diego Capital Collaborative, Maryland Regional Workforce Housing Fund and others) often working in partnership with Strategic Development Solutions, Sustainable Systems, and Economic Research Associates that contribute to the due diligence and feasibility studies of the fund and initiative building process. These economic development consultants are part of an "initiative building team" that assists the not-for-profit sponsor of the Double Bottom Line Fund in the creation and operation of the Fund and assists in a variety of ancillary activities to contribute to the overall mission of community revitalization (Double Bottom Line Handbook 2007). The not-for-profit sponsor may not, initially, have the expertise required and consultants can help in the capacity building of these organizations.

The Bay Area Family of Funds is another example of a fund initiative that includes a not-for-profit sponsor, the Bay Area Council. The Bay Area Council is a public-advocacy group (in education, housing, environmental resources, and transportation) that promotes a vital business environment in the nine-county Bay Area. The Bay Area Council is sponsored by 275 of the largest employers in the region (www.bayareacouncil.org). In building the Bay Area Family of Funds, Economic Innovation International, in partnership with Sustainable Systems, saw that the Bay Area Council's overall mission was aligned with the goals of the not-for-profit sponsor. The Bay Area Family of Funds is an initiative of the Bay Area Council, in association with the Bay Area Alliance for Sustainable Communities as called for in the Compact for a Sustainable Bay Area.

In this example, Economic Innovation International was the consultant to the Bay Area Council in building the Bay Area Family of Funds as both a regional initiative and a Family of Funds. The firm did the due diligence and orchestrated the terms and conditions of the funds. The fund builder takes part in the implementation and structure of the fund sponsor, investors, fund creation, selection of fund managers, and capitalization.

The Bay Area Family of Funds served as the link to the local community. A community partner was formed to leverage capital invested in the underserved neighborhoods, the San Francisco Bay Area Community Investment Network (BACIN).[11] The group was established to provide a pre-screened, pre-qualified flow of real estate and business deals to BACIN participants—investors such banks, insurance companies, and community organizations. BACIN participants can invest independently or together with funds in the Bay Area Family of Funds. Pension funds are not direct participants in BACIN but are invested indirectly as the Contra Costa County Retirement System is an investor in the Bay Area Family of Funds JP Morgan Bay Area Equity Fund.

BACIN facilitates collaboration by "sharing information on pre-screened investment opportunities that can lead to investment or co-investment by BACIN participants". BACIN ensures that the investments reach the 52 priority neighborhoods in the Greater San Francisco Bay Area, where the median household income of residents is 80% or less than the average incomes for the same county (www.bacin.org). Investments are at a large scale yet developed through small, cultivated relationships among community, business, and civic leaders. The deals sourced through BACIN can serve the local market but often serve the regional or even a global market allowing for the scale necessary to attain the financial returns promised.

Shifting to the for-profit fund manager model the USA Fund, in their Olmsted Green project, has partnered with a local community development corporation, Lena Park. In this example

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[11] BACIN is organized by the Bay Area Council and the Bay Area Family of Funds, launched in 2003 with the joint effort and support of the Federal Reserve Bank of San Francisco and the Ford Foundation (www.bacin.org).

the CDC played a vital role in project development working directly with the local community. The CDC has a 35-year history of serving the community and provides affordable housing and human services to low-income families in Dorchester, Mattapan, and Roxbury, Massachusetts (www.lenapark.org). The Olmsted Green project in Mattapan, Massachusetts (www.olmstedgreen.com), broke ground in May 2006 and will provide workforce housing, youth programs, community and healthy living centers—a holistic "cradle to grave" community development. Lena Park was instrumental in building programs and resources to benefit the community they serve, given their long standing history as a partner in the community. Similarly, the Fund partners with joint venture real estate developers (i.e. New Boston Development Partners) in the development of the project sites. The joint venture developer is generally responsible for the day-to-day management of the deal and acts as the general contractor of the project.

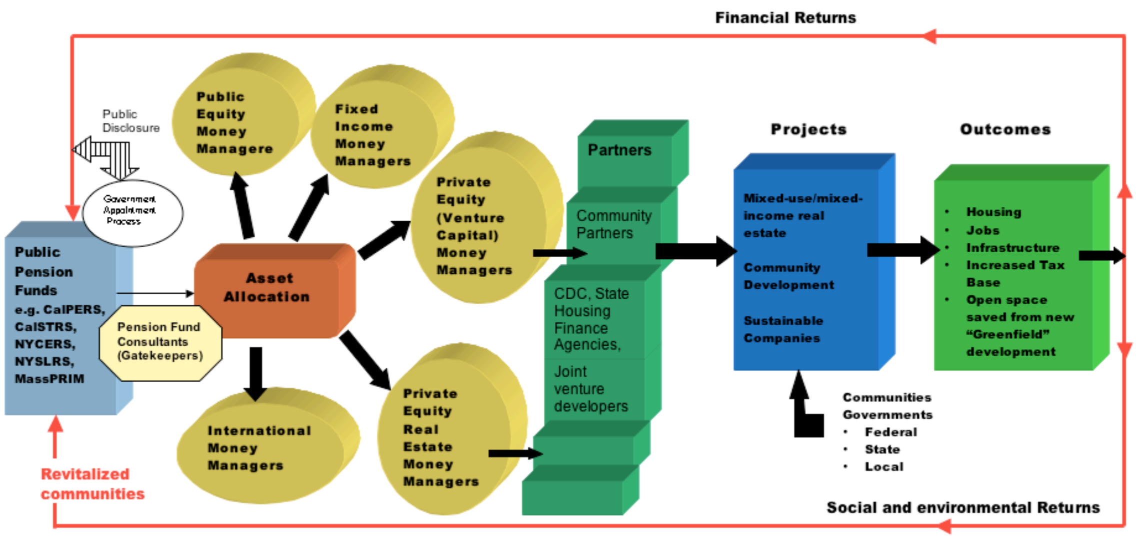
In many cases developers of significant projects negotiate with neighborhood community groups to form partnerships through Community Benefits Agreements (C.B.A.)—contracts that include concessions such as a day care center, a new park, and even cash that is directly administered by the community group (New York Times, June 14, 2006). C.B.A's provide a mechanism for the community partner to leverage its position and ensure that development decisions deal with a wide range of social and economic issues (e.g. transportation, jobs, and housing).

It is important to recognize the community partner link as it is critical in helping investment intermediaries achieve scale and ensure that the financial and social goals are realized.[12] Models that incorporate a community partner have the greatest success in transforming neighborhoods to benefit the community.

[12] Community partners link private investment to the underserved neighborhoods. The micro-credit lending pioneer and Nobel Peace Prize winner, Muhammad Yunus, founded the Grameen Bank of Bangladesh and made it a success by replacing traditional risk management with the "power of trust". As Connie Bruck (New Yorker October 30, 2006) describes microfinance institutions are realizing a significant profit in lending to the poor. Models such as Compartamos and the recently created Omidyar-Tufts Microfinance Fund look at ways to achieve scale in the microfinance world. Similarly, in the community based investing industry, partnering with a community organization is built on a relationship of trust, and this enables the massive investment intermediary, and as such the institutional investor, to impact the community.

Figure five illustrates how the flow of money reaches the underserved community. In the diagram we see both the link between the institutional investor (labeled "public sector pension fund" in figure), the investment intermediaries ("fixed income, equity real estate, and private equity money managers" in figure), and the community partners ("partners" in figure).

Figure 5 Flow of money to the community



The links illustrate how institutional capital flows from the massive institutional investor to the underserved communities. Many of the investment intermediaries described in section two have formed partnerships with local community organizations. The public-private partnerships are essential for a revitalized economic development area.

7 Capital flow and sourcing of investment ventures

The success of the investment intermediary is in their ability to source, analyze, and executive investments. Each investment vehicle has perfected their niche in the marketplace in terms of structuring and sourcing deals, expertise that institutional investors seek out in their money managers.

The capital structure of an investment fund is developed through complex financial engineering. The structure can involve a debt component that helps bring the deal to scale.[13] This is an important factor in understanding how the investment vehicle provides scale that leads to a transformation of neighborhoods and significant investment in growth companies. A successful real estate development includes a well-structured capital source. This is outlined in a proforma detailing the sources and uses of funds. Funding sources include a combination of equity and often a bank loan for construction financing and other third party debt financing. Equity is leveraged with mortgage financing to generate substantial capital in new developments in the economic development area.

The role of subsidies is another component in the capital structure of private equity funds. While the second and third generation of community based investing has moved away from a reliance on public subsidies, they can still continue to play a role. The Community Preservation Corporation, both the not-for-profit (CPC) and for-profit subsidiary (CPCR) receives permanent sources of financing through federal tax credit programs. CPC and CPCR receive funds through the Low Income Housing Tax Credit Program, a federal program for the construction and development of affordable housing.[14]

Credit enhancements also play a role in the capital structure of the funds. In this scenario governments can use their dollars to leverage institutional investment into the emerging domestic markets. Often without these credit enhancements, investments in the underserved neighborhoods would not take place. Allen and Gale (1994) see credit enhancement as a way

[13] The English Encarta dictionary defines the word leveraged as the "action of a lever pivoting about a point" or in relation to investment funds the extra force needed to make the deal.

[14] "The Low Income Housing Tax Credit (LIHTC or Tax Credit) program was created by the Tax Reform Act of 1986 as an alternate method of funding housing for low- and moderate-income households, and has been in operation since 1987"(http://www.danter.com/taxcredit/about.htm assessed October 10, 2006).

to remove the barriers to investing (unfamiliarity with product and unsure of risks involved) by having banks and insurance companies guarantee the securities. The guarantees enhance the ability to sell the securities as well as the liability. Pension funds are increasingly entering this market.

The CPC fixed income example referred to earlier, in which the New York City Retirement System commits to buy the loan from CPC at a long-term lock-in interest rate, is an investment backed by a government guarantee from the State of New York Mortgage Agency. The guarantee component offers institutional investors an incentive to invest in a new financial product that they might otherwise be reluctant to participate in. This has worked well for institutional investors reluctant to enter into the space of targeted investing, given their unfamiliarity with this emerging domestic market and its associated high risk.

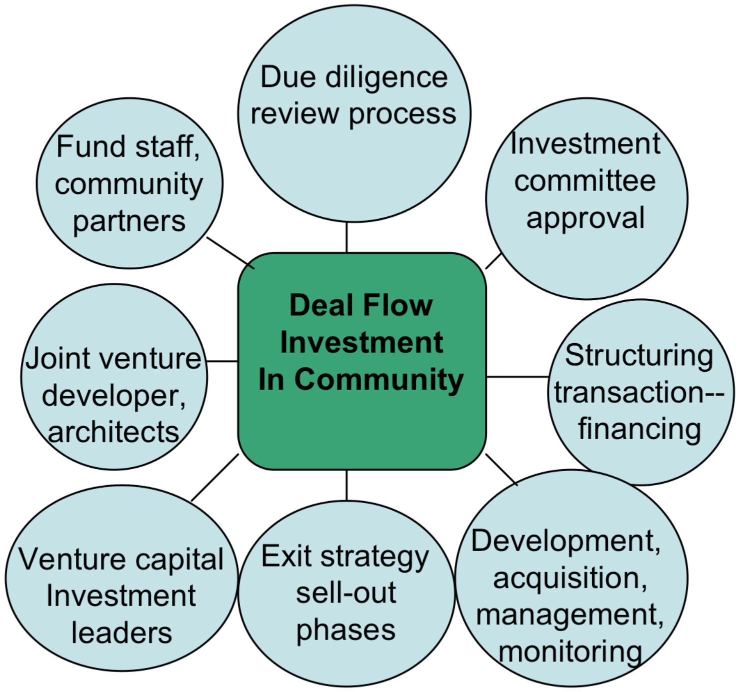
While the complexity of government subsidies (e.g. low-income housing tax credits, real estate tax abatements) can add to processing costs and slow up the transaction, they can also provide the needed lift and insurance guarantee, for an investment transaction to take place particularly as pension fund investors are risk adverse. The Community Preservation Corporation intermediates between the flow of capital and the flow of expertise in the community. The CPC model has been able to make efficient use of small parcels of infill development and use of government subsidies in line with the neighborhood's environment. CPC is the link between capital (from investors and public subsidies, and to the borrower) and the expertise in the development community.

A successful economic development investment depends on a fund manager's ability to find attractive investment ventures or so-called "deal sourcing". A fund manager's expertise is in their ability to find and review deals. Fund staff will assess market conditions, characteristics of the potential investment venture, demographic trends, purchasing power, and locational advantages among other factors.

Market studies identify whether economic conditions are in place for the financial and social success of a potential project. In this practice the fund manager participates in a rigorous due diligence process. A proper sourcing model should be able to mitigate the risk inherent in urban investing. Investments in venture capital are sourced through Fund staff and investment banking and research professionals. These investment professionals have long standing track records in finding high quality potential investment candidates. Figure six illustrates the players and actions that are a part of the deal flow process. Each participant in the review process brings expertise and insight into the deal.

Figure six illustrates how deals are sourced that includes among other factors: due diligence, committee approval, development and monitoring, and exit strategy development. The success of the fund manager is in their ability to analyze and execute investments that create value in the economic development area.

Figure 6 Deal flow process



During the deal flow process the project type; investment parameters, investment criteria, and exit strategy are defined. In terms of real estate projects this generally includes projects in residential (e.g. rentals and for-sale in low to moderate income areas, adaptive reuse, vacant warehouse live/work artists lofts), retail, office, mixed-use development in smart growth and transit-oriented locations, and reclamation of brownfield sites. In terms of private equity this generally includes investment ventures in seed, early stage, later stage, buyout and growth companies.

The investment vehicle's due diligence includes an analysis to ensure that investments are made in growth regions in which there is a high potential for real estate appreciation. During the deal flow process, the investment advisory committee assesses the potential market demand of the development. For example, increased demand for middle-income housing in a certain economic area due to an expansion of a nearby university.

In the due diligence of emerging growth companies, a private equity fund manager might look at whether a company has the capacity to lead in their sector and bring about structural change. They will examine the company's business model, financial strength, and ability to meet the social criteria—in bringing jobs and social programs to the low-and-moderate income priority neighborhoods.

An important component in the deal flow process is the project manager's request for approval from the investment committee. The committee generally includes the principals of the fund, investment professionals, property management professionals (in the case of real estate) and venture capital professionals. The investment committee makes the final decision on whether to approve a capital investment into the venture.

The approval committee's recommendation includes factors such as (in the example of an equity real estate deal) location description, site description, development budget, market demand, affordability of housing units, joint venture partners, income distribution scheme, projected internal rates of return, and a breakdown of the sources and uses of funds. In addition the fund will often have an advisory board component made up of lead investors along with investment and community partner experts.

The investment fund manager determines the investment criteria. In real estate the investment criteria can include whether the investment is core, value added, or development/opportunistic. In private equity the investment criteria outlines the industry sectors in which to invest. The strategy also includes diversification by geography as a way to balance risk and avoid over-weighting in a single market.

The investment criteria also examines the social merits in terms of housing creation, entry-level job creation, environmental benefits, and opportunities for minority & women-owned businesses. In real estate, developments incorporate criteria for green building construction. In some cases the social criteria calls for the company's CEO to sign a "letter of intent" to meet the social objectives as a condition for fund investment in the company.

The investment dollar size of the venture varies depending on the size of the fund and can start as low as $500,000 as in the case of SJF Ventures (in expansion stage companies), and go up to $200 million, as in the case of UrbanAmerica (equity real estate). The investment period is the time it takes for the equity to be invested, often over a period of three years.

In thinking about the intermediaries' ability to achieve scale, the exit strategy can be considered most important. The strategy is developed by each investment vehicle and is part of the due diligence process. It is critical that the fund manager has a clearly defined exit strategy for each asset. In the case of equity real estate a fund manager might "sell assets on a one-off basis, package assets by type or location for sale as a portfolio to a larger institutional investor, or sell the entire portfolio. Often one-off sales will typically produce higher back-end profit". For capital appreciation in real estate there is a hold period. Before exiting the investment. Exiting is expected within three to seven years of acquisition or completion of the development (Urban Strategy America Fund 2005). In the case of venture capital often the strategy sets out to exit the investment within three to five years of the investment period. The exit strategy can include the sale of the business, IPO, redemptions, or recapitalizations.

The capital structure and sourcing of deals is a complex process that enables the fund to achieve scale and meet the targeted returns. Investment fund managers determine strategies and facilitate the flow of investment into the community. The success of the fund relies on an investment professionals' ability to collaborate with partners and successfully structure the investment venture.

8 Benchmarking financial, social and environmental returns

Community based investing takes a holistic approach to investment that produces financial returns and an improved quality of life—both for those in the revitalized area and the pensioners. This study aims to encourage more institutional investment into investment intermediaries through further research of the returns. The investment returns include the financial, social, and environmental outcomes. Greater transparency of returns is needed for more institutional dollars (e.g. public sector pension funds) to flow into the space of community based investing. Metrics to date include financial returns measured against industry benchmarks. Social returns are also being quantified, as are the environmental outcomes.

Financial returns are measured through risk-adjusted (adjusted for illiquidity and risk of investment) internal rates of return (IRR) and in investment multiples (i.e. 2X – return of two times value of the initial capital investment). The IRR is interpreted as the expected return on the investment less cost of capital and calculates what the investor would have earned over the time horizon of the investment. The California Public Employees' Retirement System (CalPERS) defines the IRR and investment multiple as:

> IRR - The dollar-weighted internal rate of return, net of management fees and carried interest generated by the CalPERS investment in the fund. This return considers the daily timing of all cash flows and CalPERS cumulative fair stated value, as of the end of the reported period.
>
> Investment Multiple - Calculation performed by adding the remaining (reported) value and the distributions received (cash out) and subsequently dividing that amount by the total capital contributed (cash in).
> (http://www.calpers.ca.gov/index.jsp?bc=/utilities/glossary/home.xml#hk)

In private equity, low or negative returns at the early stages of an investment is part of the "J-Curve effect" when funds are incurring management fees and expenses but have not yet exited on the investment. When the investment venture has matured the fund exits and the financial returns, net of management fees, are realized (Hebb, 2005). Indices such as the Lehman Aggregate Bond Index provide a benchmark for fixed income. The National Council of Real Estate Investment Fiduciaries (NCREIF) Property Index is used for benchmarking equity real estate fund performance. The benchmark is however meant for more stable, leased assets and has limitations in comparing value-added opportunistic real estate with inherent higher risk. There is no universally accepted industry index for private equity given timing issues, cash flows and the absence of an agreed upon market universe among other factors (University of California 2005). Firms such as Thomson Financial Venture Economics can however gather fund performance returns and place investment vehicles in upper and lower quartiles and create customized performance benchmarks for private equity.

The social metrics are slowly being measured and while there is not yet any standardization various funds are beginning to define and report on the non-financial returns (Double Bottom Line Project Report 2004). The venture capital trade association, Community Development Venture Capital Alliance, has produced a "Measuring Impacts Toolkit" (CDVCA 2005). Such tools for measuring the social metrics activity will continue to be followed as institutional investors (e.g. foundations investing through their endowments) expect to see quantitative results on the ancillary benefits.[15] Incorporating social goals into the investment criteria is important for the growth of this industry. Social returns can be delivered through a CEO letter of intent that locks in the commitment from the CEO to meet the social criteria. For example, SJF Ventures Fund codifies its commitment to social goals through a "Community Development Assessment" performed with the company prior to investment. During the assessment SJF's not-for-profit affiliate, SJF Advisory Services, looks at ways they can assist the company with employee benefits (health care and wealth creating packages) and potential training grants. SJF Advisory Services performs social due diligence on its companies and produces a mission impacts report. The report highlights the social impacts of SJF's portfolio companies (Broughton 2006). Similarly, the Banc of America Capital Access Funds is engaged in a research project that will include the aggregation and tracking of social indicators to include number of jobs created, diversity of management team, and range of benefits offered. Banc of America Capital Access Fund has invested in funds frequently located in California. Companies are in low-moderate income areas, in areas traditionally with a lack of access to venture capital, and are minority owned or managed. Other funds engaged in measuring the social impacts include Pacific Community Ventures, the Banc of America Capital Access Funds, and CEI Ventures.

[15] Pensions & Investments (October 16, 2006) reported that per a new survey from the Council on Foundations slowly U.S. foundations are slowly taking a riskier approach with their investments and increasing the number of outside managers. Currently, there are some Foundations investing in so-called "mission oriented" investments through their endowments.

Environmental benefits are now being tracked. For example, Cherokee Investment Partners uses its Environmental Management System to assess its performance against environmental policies, objectives, targets and other environmental criteria. As stated by the firms' senior management, "Cherokee's Environmental Management System is ISO 14001:2004-certified by the International Organization for Standardization for environmental management. In addition, the company's annual Sustainability Report summarizes progress on key environmental and social performance indicators. One such indicator is the number of contaminated acres that Cherokee cleans up and redevelops, which corresponds to the number of acres of open space saved from new "greenfield" development". Cherokee and other investment firms are also tracking green certification on individual buildings. Buildings can measured for their environmental impacts and receive a green building certification validated by external third-party systems such as the U.S. Green Building Council's Leadership in Energy and Environmental Design (LEED). LEED's is a nationally accepted benchmark for the design, construction, and operation of successful green buildings per the U.S. Green Building Council.[16] Investment vehicles are incorporating green construction certification into the investment criteria. Investments are being made in companies with clean technology objectives and real estate developments incorporate public transportation links aimed at reducing traffic congestion.

[16] "LEED promotes a whole-building approach to sustainability by recognizing performance in five key areas of human and environmental health: sustainable site development, water savings, energy efficiency, materials selection, and indoor environmental quality (http://www.usgbc.org/DisplayPage.aspx?CategoryID=19) assessed October 20, 2006.

9 Conclusion

This study shows how the investment fund manager links the pension fund to the revitalized economic development area. The investment intermediary and the institutional investor form a symbiotic relationship that allows for scale to effectively transform neighborhoods and yield financial returns to the institutional investor. Through an effective deal flow process and capital structure the investment intermediary sources deals and deploys capital into the community. Without these intermediaries large pools of capital would not be placed in the economic development area. The institutional investor relies on the investment fund manager for their expertise in successfully deploying capital to deliver both financial and ancillary results.

The investment vehicles described in this study are part of the third generation[17] of community based investing and successful conduits for pension fund investment into urban communities. As more pension funds take up this strategy of investing in economic development we expect to see more investment vehicles established rather than a consolidation of funds. New investment vehicles are continually being formed as firms compete for pension fund dollars and seek profitable returns in the underserved markets. Regional investment vehicles offer pension fund investors the ability to achieve scale through a diversified fund and reciprocal targeted investing possibilities. Alternatively, state-based investment vehicles assure pension fund investors that the fund will invest the majority of the dollars in their state. It is too early in the creation of this industry to make an assessment on which model is more effective for the institutional investor.

Investments are getting to scale as evidenced by signature projects of the vehicles profiled. Investing in a location with assessed market growth potential is a way for investment vehicles to achieve scale and realize the targeted returns. Investment vehicles aim to meet the financial, social, and environmental returns to attract more institutional capital and realize scale in their investments. Investment vehicles also stimulate third party investment that creates additional economic development in the area.

[17] Daniels and Nixon (2003) set forth the three generations of community based investing in the "Making markets work for inner city revitalization" paper presented at the Inner City Economic Forum in New York.

Relationship building among institutional investors, investment vehicles, and community partners is essential. The community partner is the entity that knows the urban culture and is able to think about the investment in terms of success for the community and its residents. Without the knowledge and influence of the community partner we can often see gentrification rather than revitalization. The community based investing industry is growing as fund managers seek opportunities in the emerging domestic markets. As the industry matures investment vehicles will continue to link pension funds to urban revitalization. Financial, social, and environmental returns are slowly becoming available and essential for the growth of the industry and increased institutional dollars into urban revitalization.

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11 Appendices

11.1 List of interviewees

David Almodovar*, Vice President, Credit Suisse Alternative Investment Group
Stephanie Calabrese, UrbanAmerica

Belden Hull Daniels, Economic Innovation International Inc.

Tom Darden, Chief Executive Office, Cherokee Investment Partners

Kathleen Dunn, Director of Development, Community Preservation Corporation Resources

John Gioia, Chair, Contra Costa County Retirement System Board of Supervisors

Jack Greene, Senior Vice President, Community Preservation Corporation

Alyssa Greenspan*, Director & Portfolio Manager, Community Capital Management

Scott Hall, Senior Vice President, Asset Management, UrbanAmerica

Katherine Henderson, Associate, Cherokee Investment Services, Inc.

Matt HoganBruen, Managing Director, Banc of America Capital Access Funds

William Howell*, Vice President, Development, UrbanAmerica

David Kirkpatrick, Managing Director, SJF Ventures

Kirk A. Sykes, President, Urban Strategy America Fund, A New Boston Real Estate Fund

David H. Keiran, Senior Vice President, New Boston Fund, Inc.

Deborah La Franchi*, CEO, Strategic Development Solutions

Michael Lappin, CEO, The Community Preservation Corporation

Rick Larson*, Managing Director, SJF Ventures

John Linger*, Cherokee Investment Partners

Richmond McCoy, President & CEO, UrbanAmerica

Sarah Monroe, Community Preservation Corporation

Nancy E. Pfund, Managing Director, Bay Area Equity Fund, J.P. Morgan Securities Inc.

Ed Powers*, Managing Director, Banc of America Capital Access Funds

Elizabeth Ferguson, EVP & Managing Director, Bay Area Family of Funds, Bay Area Council

Tracy Ericson, Assistant Vice President, Community Development Corporation, Wells Fargo Bank

Lee Winslet*, Community Development Corporation, Wells Fargo Bank

Melissa Quattrucci*, Marketing & Client Service Manager, Access Capital

Keith Rosenthal, Co-Founder, President, Phoenix Realty Group

Kerwin Tesdell, President, Community Development Venture Capital Alliance
Kelly Williams, Managing Director, Credit Suisse Alternative Investment Group
Lesyllee White*, Director of Marketing, AFL-CIO Housing Investment Trust
Adam Zoger, Managing Director, Pacific Coast Capital Partners, Smart Growth Family of Funds

* Notes phone interview and/or e-mail communication.