

# The Power & Impact Of Community Investing

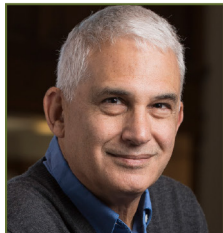
“Decent affordable housing should be a basic right for everybody in this country. The reason is simple: without basic shelter, everything falls apart,” Matthew Desmond wrote in his book *Evicted: Poverty and Profit in the American City*. Many endowments and experts focused on Community Investing would agree. While affordable housing serves as one aspect of Community Investing, such investment programs tends to catalyze local innovation and stimulate the economy by way of job creation and education. Further, for some investors, Community Investing tends to hit the bottom line twice: invigorating local economies while boosting returns.

**The Intentional Endowments Network (IEN)** approached specialists within the Community Investing space to get their perspectives on the value of Community Investing, understanding how to incorporate such investments in ones portfolio and how to truly make an impact regardless of varying levels of assets under management. IEN approached:



**ELYSE CHERRY**

CEO and President, BlueHub Capital<sup>1</sup>



**MICHAEL SWACK**

Center for Impact Finance, University of New Hampshire



**ERIK GROSS**

Treasurer, University of New Hampshire Foundation



**MICHAEL HOKENSON**

Partner, Community Investment Management

## ***IEN: How do you define Community Investing, and why is it important?***

**CHERRY:** Endowments and other organizations, as well as individual investors want to put their capital to work building stronger communities. They invest in affordable housing, good jobs, quality education, community health centers, energy resilience and foreclosure relief to revitalize distressed neighborhoods. Investors committed to community investing promote opportunity to low-income individuals and families and support an inclusive economy.

**SWACK:** “Community investing” is investment that seeks to deliver social benefits to low income or marginalized communities while also generating a financial return.

**GROSS:** The key element in Community Investing is the ability to better achieve our mission. The investment objective of the UNH Foundation is to manage the University’s endowment allowing us to achieve our educational mission to the fullest extent possible, by preserving the purchasing power of our endowed funds, while providing a continuing and stable funding source to support the current and future mission of UNH.

Our recent decision to direct a portion of the Foundation’s endowment investments to the New Hampshire Community Loan Fund (NHCLF) strongly aligned with providing the financial resources to allow us to achieve our educational mission. Community Investing is also one of those rare opportunities for the Foundation to find a truly “local” investment that also fits well in the portfolio. Because of the mission and admirable track record of the NHCLF to “serve as a catalyst, leveraging financial, human, and civic resources to enable traditionally underserved people to participate more fully in New Hampshire’s economy” our investment allows us simultaneously contribute to the University’s commitment to serving the public good more broadly.

**HOKENSON:** We consider Community Investing as a subset of the broader field of impact investing focused on reaching those whom are underserved by the conventional market such as small businesses, low-income neighborhoods or regions, women, or communities of color.

Community Investing is especially relevant in the current environment of rising income inequality. Despite nearly

a decade of strong performance of the United States economy, US small businesses face significant challenges obtaining capital and a majority (57%) of US families are considered financially unhealthy, with household expenses growing faster than income, largely driven by healthcare and education costs.

Community Investing can play a role in counteracting these trends by deploying capital to address conventional market failures and creating economic opportunities for creditworthy but underserved small businesses and families. In particular, recent advances in technology and greater availability of data are changing how Community Investing strategies reach, understand, and responsibly support these underserved communities.

## ***IEN: How does Community Investing fit into a typical endowment portfolio in terms of asset classes and risk and return profile?***

**CHERRY:** Endowments use us as a fixed-income asset to diversify their portfolio and generate returns. We mitigate risk with a well-capitalized balance sheet (over \$1 billion), robust lending and underwriting standards; over our more than 30 years our loan loss has been less than ½ of 1% and have never lost any investor’s money.

**SWACK:** Endowments can access a wide variety of asset classes in the community investment product landscape, including fixed-income investments such as debt in nonprofit loan funds, cash investments such as deposits in community development banks and credit unions, and equity investments in real estate—often accompanied by government tax credits—and in private equity impact funds. Investors can get the best sense of their opportunities

**“The key element in Community Investing is the ability to better achieve our mission.”**  
— **GROSS**

# “Interest in socially beneficial investing is growing in the U.S., with the potential to drive more endowments to supporting community investment.”

—SWACK

and venture capital funds, and comprises a substantial but incomplete portion of the greater community investment field. Other community investments are often in the form of direct investments into specific projects (e.g. affordable housing, commercial development.)

**GROSS:** Our investment in the NHCLF falls into the fixed-income segment of our portfolio. It supplements our mutual fund investments. The committee views this investment as beneficial to the portfolio’s overall performance. It has a guaranteed rate of return at maturity, so this helps to reduce some of the volatility we may experience in other fixed-income investments and overall. Fixed Income has not been a major contributor to our portfolio’s overall return experience, and even detracting in certain periods, so the NHCLF investment is viewed as pushing for a more consistently positive return from fixed income as a whole. Because NHCLF has never defaulted on one of these investments, the investment committee is very reassured as to the security of the principal. The risks are very low. The committee is willing to take on the relative illiquidity of this investment (we must hold to maturity) for this risk and return profile.

by understanding the range of intermediary organizations offering investment products (hereinafter referred to as “investees”).

Many community investment investees pursue formal certification as Community Development Financial Institutions (CDFIs). The CDFI field includes nonprofit loan funds, regulated banks and credit unions,

**HOKENSON:** Community Investing strategies fit within a broad range of asset classes. Depending on the particular investment opportunity, Community Investing strategies often fall within an endowment allocation to alternative investments (with respect to private debt, private equity, venture capital, real estate, etc.) or cash equivalents (with respect to deposits held at or loans to a community bank, credit union, or community development financial institution).

Given that the conventional endowment model typically involves larger allocations to alternative investments in non-traditional asset classes, we have observed a preference by endowments in identifying those Community Investing strategies that meet the risk and return profile hurdles generally associated with their alternative investments.

## *“IEN: Can endowments of any size engage in Community Investing strategies? If so, do you have any recommendations of how a smaller vs. larger endowment can engage and make an impact?”*

**CHERRY:** Endowments of any size can participate in community investing. For example, Boston Community Capital investments can range from \$1000 to millions of dollars. Every investment counts toward our mission to build healthy communities where low-income people live and work.

**SWACK:** Interest in socially beneficial investing is growing in the U.S., with the potential to drive more endowments to supporting community investment. Convincing endowments to direct even a small amount of money into community investment vehicles could drive vast increases in scale. However, a variety of challenges must be overcome to increase involvement from endowments. Interestingly, most of these challenges apply to both retail and high-net-worth investors, at least in broad strokes:

- Investment advisors are the gateway to most individual investors. They must be able to honor their fiduciary duties to the client, which impacts their ability to facilitate investment into (perceived) below-market

vehicles. They also need to earn fees for their work that further diminish investor returns.

- Most community investment vehicles are not registered securities and do not carry CUSIP numbers, which can make both investment advisors and custodians reluctant to handle them.
- Endowments can have widely varied interests around the geography and type of impact they wish to support, which creates logistical and marketing challenges for product managers.
- A substantial marketing effort is needed to gain the interest not only of clients but also of investment advisors and educate them about community investment opportunities.

**“By bringing new capital to under-served communities, Community Investing can profoundly transform those communities.”**

**— CHERRY**

investment can both help meet investment goals and align with the institution’s mission to serve.

**HOKENSON:** There are many investment options for endowments of various sizes to engage in Community Investing. In Community Investing, as with many non-traditional asset classes, manager selection, fees, and liquidity all are heavily weighted variables. Generally, we recommend endowments carefully consider manager track record, lock-up period, and total expense ratio alongside the strategy’s impact goals to determine if the Community Investing opportunity is in line with the endowment’s objectives.

A larger endowment may be more comfortable with allocations to less liquid impact investment funds focusing

on marginalized communities, such as an affordable housing private equity fund, while a smaller endowment may have cash requirements that require them to focus their Community Investing strategy on more liquid options, such as cash equivalents.

## ***IGN: What are some of the main topic areas or issues that Community Investing seeks to address?***

**CHERRY:** By bringing new capital to under-served communities, Community Investing can profoundly transform those communities. We provide financing to communities traditionally denied access to capital. We work with civic, government, community-based and private sector partners and stakeholders to develop projects that stabilize and revitalize communities.

**SWACK:** Options exist, and many are being implemented, to address some of the challenges described above. For example:

- Standardized reporting metrics—such as those in the IRIS catalogue, managed by the GIIN—that have been developed could help the community investment field to communicate a more cogent and compelling picture of the impacts it is creating, while lessening reporting burdens to multiple investors.
- The use of the Aeris rating system for CDFIs has been growing. Some CDFIs have also obtained S&P ratings, which provide a degree of confidence for investors with limited ability to conduct an exhaustive underwriting of the investee organization on their own.
- Product managers have formed special-purpose vehicles or other off-balance sheet structures to increase their ability to raise equity or increase leverage. Others have utilized tranching structures to create market returns for a portion of their investment needs.
- Online investment marketplaces—such as CapNexus can facilitate the matching process between investors and products.

In addition to the above, additional data collection and research could better document the performance of community investment products and help to clarify which products truly operate with market returns, and how far below market concessionary products fall.

In a survey we carried out among investors, one thing we sought to understand is their investment goals when selecting among community investment opportunities. It is notable that for foundations, there is a clear emphasis on measuring and reporting on social impact. While information on financial performance is also considered important, aspects such as strong returns and high liquidity were not considered to be of primary importance. For non-foundation investors, on the other hand, attractive risk adjusted returns as well as reliable and meaningful social impact are both given high importance. Low loss rates and information on both social and financial performance are other aspects that scored high.

**GROSS:** Community Investing connects UNH and the Foundation even more closely with the NH community. Our involvement in the web of activities around NH is critical to continually improving the public's perception of the value of UNH throughout the state. This investment improves all parties involved, in very real ways, and it allows the Foundation and UNH to leverage its resources to directly benefit our neighbors throughout the state. And our own University community has been asking for this. It's a tremendous win on a number of levels.

**HOKENSON:** In the United States, there exists a breadth of community development and neighborhood improvement needs that Community Investing strategies can assist in addressing. These national needs span nearly all areas of American health and wellbeing, including investment opportunities in skills-based education, the renovation and expansion of healthcare facilities, the development and preservation of affordable housing, and inclusive financial services that create local economic value.

Within the many areas of Community Investing, CIM focuses on providing responsible financing to US small businesses and other underserved communities. US small businesses are critical as the principal engine of jobs,

growth, and innovation in the US, employing 130 million individuals. Nevertheless, a recent Federal Reserve Bank of New York's small business credit survey revealed that 42% of small businesses report limited business expansion due to credit denial. Traditionally marginalized demographics are disproportionately affected by this lack of credit availability. In the US small business market, women-owned businesses start with half as much capital, are two times more likely to finance their businesses with family loans and have 15 to 20% lower loan approval rates from banks despite performing just as well. Businesses owned by people of color are 2.5 times more likely to be denied credit than other businesses and are 1.8 times more likely to be discouraged from applying.

Our approach to Community Investing is to identify and scale responsible innovation in lending to provide productive and transparent financial services at affordable prices with the aim of improving the financial health of small businesses and underserved communities. Emerging financial technology is transforming Community Investing by offering solutions to efficiently acquire, underwrite, and service traditionally underserved borrowers with smaller amounts of capital. By aligning the incentives of the investor and investees through thoughtful Community Investing strategies, measurable impact and financial return can be achieved in parallel.

**“By aligning the incentives of the investor and investees... measurable impact and financial return can be achieved in parallel.”**  
— **HOKENSON**

---

<sup>1</sup> BlueHub Capital was formerly known as Boston Community Capital