

Community Development Finance in Los Angeles

Challenges and Responses

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Introduction

Los Angeles is an enormous, growing market with the highest level of poverty of the 10 largest U.S. metropolitan statistical areas (MSAs). It is one of the most ethnically diverse metropolitan areas in the country, with a unique history and a vast array of community development organizations. This study documents the array of community development finance activities and organizations in the Los Angeles MSA and some of the challenges they face.

As part of the study we analyzed the level of community development financial institution (CDFI) activity and assets in the most populous urban areas in the United States and, more critically, looked at which areas have more activity and assets relative to the number of people living in poverty in those areas. This is the first time this type of analysis has been done. We examine the challenges of developing affordable housing in one of the most expensive markets in the country and the role that CDFIs have played in this arena. We also look at the dynamics of the small business lending market and the CDFI response to these challenges. Finally we make a number of recommendations to the CDFIs in Los Angeles, their supporters, and the CDFI industry nationwide.

CDFIs are specialized financial institutions that provide financial services to people and communities that are underserved by the traditional financial services industry. They provide loans, investments, and basic financial services to help individuals and families become more self-sufficient and to revitalize low-income communities. They make loans and investments to provide affordable housing, create jobs for low-income people, support businesses that serve low-income communities, and assist nonprofit organizations that work with low-income people. To do this, they gather capital from a variety of public and private sources.

Four types of institutions serve a broad range of needs in CDFI markets:

- **Community development banks** are for-profit corporations with community representation on their boards of directors. Community development banks are regulated by either a federal regulator or state banking agencies, depending on their charter. Their deposits are insured by the Federal Deposit Insurance Corporation.
- **Community development credit unions** are nonprofit financial cooperatives owned by their members. Credit unions are regulated by the National Credit Union Administration (NCUA), an independent federal agency, by state agencies, or both. In most institutions, deposits are also insured by the NCUA.
- **Community development loan funds** are unregulated institutions. Most have nonprofit certification and are governed by boards of directors with community representation.
- **Community development venture capital funds** can be either for profit or nonprofit and include community representation on their boards.

The CDFI field is in the midst of a transformation from an array of relatively small, independent, vertically integrated financial intermediaries into a broad, interconnected network of specialty financial institutions and support corporations. This transformation reflects the development of the field as we move from the high growth of the 1990s to the scale and permanence we aspire to in 2010 and beyond.

In the past three to five years, a number of trends in the external environment have had a big impact on CDFIs, including the following:

- **The reduction in subsidy for CDFIs for operations and capital.** This is an across-the-board change, as all major sources of CDFI support are decreasing at the same time, including government, foundations, banks, and other corporate support. CDFIs will need to adapt a new, more efficient business model to survive and continue to grow.
- **The changing economics and demographics of poverty and the workforce.** The economy has slowed considerably since the go-go growth days of the 1990s, but that has not slowed the growth in the gap between the wealthy and the poor, either in terms of income or wealth. The supply gap of affordable housing is growing and is likely to continue to grow in light of the decrease in federal subsidies for affordable housing. At the same time, our country is becoming much more diverse, with immigrant populations driving population growth in many areas and fueling the engine of the small business economy. Such changes present challenges to CDFIs in terms of outreach to different cultures and languages.
- **Shifts in access to capital.** In the traditional banking world, credit scoring and business credit cards have opened access to credit to people and businesses previously denied loans. In the subprime financing industry, lenders are making loans for mortgages to many people previously denied for bad credit. Some of those loans are predatory and hurtful to our communities. Predatory lenders often target elderly and minority homeowners. These trends challenge CDFIs in different ways. Business lending through credit scoring means increased competition for loans and, in some cases, CDFIs seeking new, more risky markets. Predatory lenders strip wealth from the communities we work in, eliminating the progress made in some neighborhoods and by some households.

The Los Angeles Community Development Environment

Los Angeles is populous and vast geographically. The Los Angeles MSA is made up of Los Angeles and Orange counties. It is the second largest metropolitan area in the country, with close to 13 million people; New York is the largest at 18 million residents. The Los Angeles MSA accounts for 36.2% of the population of California, the country's most populous state.¹

¹ U.S. Census Bureau, "Quick Facts about Los Angeles and Orange Counties," June 3, 2005 <<http://quickfacts.census.gov>>.

As of January 2005, Los Angeles County alone had slightly more than 10.2 million residents, making it the largest county in the country. This is more people in one county than in 42 US states!² Los Angeles County covers 4,061 square miles; it has 88 cities; and 65% of the area is “unincorporated.” In an unincorporated area, the county is the local government and the areas are assigned to one of the elected county supervisors. The unincorporated areas include areas one might assume are part of the city of Los Angeles, such as East Los Angeles and East Compton. Orange County, located to the south of Los Angeles County, is the second largest county in the state, with 2.96 million residents according to 2003 Census Bureau estimates. The city of Los Angeles is by far the largest city in the two counties, with almost 4 million inhabitants. The next largest cities are in Orange County: Santa Ana and Anaheim, with 349,123 and 343,046 residents according to January 1, 2004, state of California estimates.³

The Los Angeles MSA had the highest percentage of people living in poverty of the 10 largest MSAs in the country, at 15.6%, or just under 2 million individuals living in poverty in 2002. The next highest was Miami, with 14.1% of its residents living in poverty. Median household income in Los Angeles County dropped 11% from 1990 to 2000 from \$46,977 to \$42,189, in contrast with increases in the state of California and the nation as a whole. In 2002, requests for emergency food assistance increased 32% over 2001 levels in the city of Los Angeles.⁴ Homelessness is an increasing problem in Los Angeles County. In 2002, 254,000 people were estimated to be homeless at some point during the year.⁵ Income inequality is increasing in Los Angeles faster than in the rest of the state and the nation.⁶

For an outsider, Los Angeles County can feel vast and confusing. The number of cities, neighborhoods, highways, ethnic groups, and community development organizations is overwhelming. Most people would have a hard time knowing that they just left the city of Los Angeles and entered the city of Inglewood if they missed an old washed-out sign. The urban presence is continuous throughout the county with the exception of uninhabitable valleys and mountains. For such a large metropolis, downtown Los Angeles is not the center or core one would expect. Downtown is not even referenced on the Hertz rental map! Downtown is a relatively small area bounded by highways on three sides, with many high-rise office buildings and hotels; it mostly empties out after the workday, with the exception of when something is going on at

the Staples Center. There are few residents in downtown, and almost no retail or service establishments for residents. That is beginning to change with the new lofts being developed from unused downtown office buildings and dilapidated hotels; a supermarket is under construction.

Los Angeles continues to grow, although more slowly than California. Los Angeles County grew 3.7% and Orange County grew 3.9%, compared with California’s 4.8%, between 2000 and 2003, according to the Census Bureau. Los Angeles’ growth in the past has been based on spreading out into new, undeveloped areas. However, now Los Angeles has developed almost all the available land, and further growth will mean greater density.

Two unique events in Los Angeles have played a role in shaping its community development finance industry over the past 13 years: the riots following the Rodney King verdict in May 1992 and the Northridge earthquake of January 1994. In each case, CDFIs received funding to help the communities they serve rebuild, alongside the larger government and private efforts to recover from those events. In the case of the earthquake, funding from the Economic Development Administration and elsewhere was restricted to restoring commercial buildings directly damaged by the earthquake or to businesses negatively affected by the earthquake. Almost a dozen years later, a number of CDFIs still have this funding with those same restrictions, making it very difficult to deploy. They are working with the government to get the restrictions removed. The distribution of these funds among so many different groups targeted at specific areas is part of the reason there are so many area-specific CDFIs in Los Angeles.

The Los Angeles population and economy present at least two specific challenges to the community development finance sector: lending in a very diverse market and developing affordable housing in one of the most expensive markets in the country.

Diversity in Los Angeles

The Los Angeles MSA is extremely diverse. The majority of residents are non-white,⁷ with the largest proportion being Hispanic or Latino, followed by Asian, then African American. However, the census figures do not do justice to the ethnic, linguistic, and racial diversity of Los Angeles. The MSA is the most linguistically diverse in the nation, with 137 languages spoken.⁸ An example of that diversity is the city of Glendale, which has an estimated 40% Armenian population, reportedly the largest Armenian community outside of Armenia. In 2001, Los Angeles led the country in population growth from abroad with 91,131 new immigrants.⁹ Many neighborhoods are shifting from being dominated by one group to becoming multi-ethnic.

2 “LA County Online: Overview,” Los Angeles County Web site, 2005, August 1, 2005 <<http://lacounty.info/overview.htm>>.

3 California State University, Fullerton, “Demographics by Orange County Jurisdiction,” June 28, 2005 <www.fullerton.edu/cdr/quickfacts.pdf>.

4 P. Tepper and J. Barrett-Simpson, “The Puzzle of the Los Angeles Economy: A Look at the Last Thirty Years,” Institute for the Study of Homelessness and Poverty at the Weingart Center, October 2003, May 5, 2005 <<http://www.weingart.org/institute/research/other/pdf/PuzzleLAEconomy.pdf>>.

5 Daniel Fleming, Patrick Burns, and Brent Haydamack, Homeless in LA: Final Research Report, Economic Roundtable. September 2004, January 5, 2005 <www.economicicrt.org>.

6 Tepper and Barrett-Simpson, “Puzzle of the Los Angeles Economy.”

7 In the 2000 Census, white persons not of Hispanic/Latino origins made up 31% of Los Angeles County and 51% of Orange County residents.

8 U.S. English Foundation, “Many Languages, One America: The Most Linguistically Diverse MSAs,” 2005, July 10, 2005 <http://www.usefoundation.org/foundation/research/lia/top_50.asp>.

9 U.S. Census Bureau, “Metro Movers,” 2003, April 15, 2005 <www.census.gov/Press-Release/www/2003/cb03-80.html>.

The Los Angeles Economy

The Los Angeles economy is diverse and growing, but the quality of jobs has declined. Despite the loss of many manufacturing jobs in the defense industry, Los Angeles is the largest manufacturing employment center in the United States with 482,200 workers.¹⁰ The leading industries in terms of jobs in Los Angeles County are international trade, tourism, motion pictures/television, technology, and business and professional services. In 2001 there were 307,878 private firms in the Los Angeles MSA with paid employees, or 38.2% of such firms in California. Despite healthy growth in the economy, most of the job categories predicted to grow the most do not require a college degree and have a starting pay of \$8.50 or less per hour, including retail sales, cashiers, clerks, waiters, guards, food preparation, and janitors.¹¹

Much of the growth in the Los Angeles economy is in the small business sector, and specifically in immigrant- or ethnic-owned businesses.¹² The fastest growing sector is the informal, or underground, economy.¹³

Los Angeles is one of the most expensive housing markets in the country. In July 2005, the median price of a single-family home was \$515,000, a 21.2% increase over July 2004. The median price for a condominium was \$399,000, a 20.9% increase over the previous year. The median prices are not affordable even in low-income areas.¹⁴

To afford a \$350,000 home, a household needs to earn \$78,000 a year, or \$37 an hour, about six times the minimum wage. Condominiums, frequently a more affordable option especially for first-time home buyers, are rarely available in these neighborhoods and throughout Los Angeles. Not surprisingly,

the homeownership rate in Los Angeles was 39%—compared to 69.2% nationally—in the second quarter of 2004.¹⁵

In Los Angeles nearly half of all renters pay more than 30% of their income for rent, and nearly 25% of all renters spend more than half of their income on rent. The fair market rent set by the U.S. Department of Housing and Urban Development for a two-bedroom apartment in Los Angeles County is \$1,021. To afford that, a household's annual income would have to be \$40,840.

According to the Institute for a Competitive Inner City, 23% of the land area of Los Angeles is defined as "inner city," or contiguous census tracts where the population has a poverty rate of 20% or more or has a higher poverty rate, lower median income, and higher unemployment than the MSA. This area is home to 46% of the city's population, whereas the average is 38% for the largest 100 inner cities. The inner city of Los Angeles ranks first among inner cities in terms of employment, with 469,533 jobs in 2001. Only 31% of those jobs are held by inner-city residents, meaning that many people from other areas come to the inner city for their jobs. There is slower employment growth and wage growth in the Los Angeles inner city than in the rest of the city: between 1995 and 2001, inner-city jobs grew by only 0.1%, whereas those in the rest of the MSA grew by more than 4.3%. City jobs grew by 2.4%.¹⁶

Overview of Los Angeles CDFIs

Los Angeles is served by at least 33 CDFIs,¹⁷ including loan funds, credit unions, one bank, and one venture capital group. The CDFIs range from small organizations focused on one neighborhood to large statewide and even national institutions. Appendix I gives an overview of Los Angeles CDFIs. In addition, Los Angeles has a myriad of state- and city-based programs that provide financing and other types of support; banks that provide a variety of community development loan products and deposit services; and other nonprofits that develop affordable housing, deliver financial education and counseling to low- and moderate-income people, and/or

10 Los Angeles Economic Development Corporation, "LA Stats," June 2005, July 5, 2005 <<http://laedc.org/reports/LAStats-2005.pdf>>.

11 Tepper and Barrett-Simpson, "Puzzle of the Los Angeles Economy."

12 K. Klowden and P. Wong, "The Los Angeles Economy Project," Milken Institute, December 2005, p. 5, July 5, 2005 (early edition) final report available: <<http://www.milkeninstitute.org/publications/publications.taf?function=detail&ID=468&cat=ResRep>>.

13 Klownden and Wong, "Los Angeles Economy Project," p. 11.

14 "Southern California Home Resale Activity," Data Quick Real Estate News, August 5, 2005 <www.dqnews.com/ZIPLAT.shtm>.

15 Los Angeles Housing Department, "Building Healthy Communities 101: A Primer on Growth and Housing Development for LA Neighborhoods," July 6, 2005 <www.lacity.org/lahd/curriculum/index.html>.

16 Institute for a Competitive Inner City, "State of the Inner City Economies: Los Angeles, 2004," May 3, 2005, July 4, 2005 <<http://www.icic.org>> Path: State of the Inner City Economies.

17 This figure includes certified CDFIs, several noncertified credit unions, and several noncertified loan funds.

Single-Family Home Prices by City

Neighborhood	Median Price for Single-Family Home, Nov 2005	% Change in Price from Nov 2004 to Nov 2005
Compton	\$317,000	37%
East LA	\$418,000	54%
Watts	\$335,000	31%
Pacoima	\$485,000	26%

deliver entrepreneurial training and technical assistance to small business. Each such program developed to serve its own mission and market, and there is no organizing or coordinating force. It is very difficult for new entrepreneurs or nonprofits to figure out what is available to them, what they

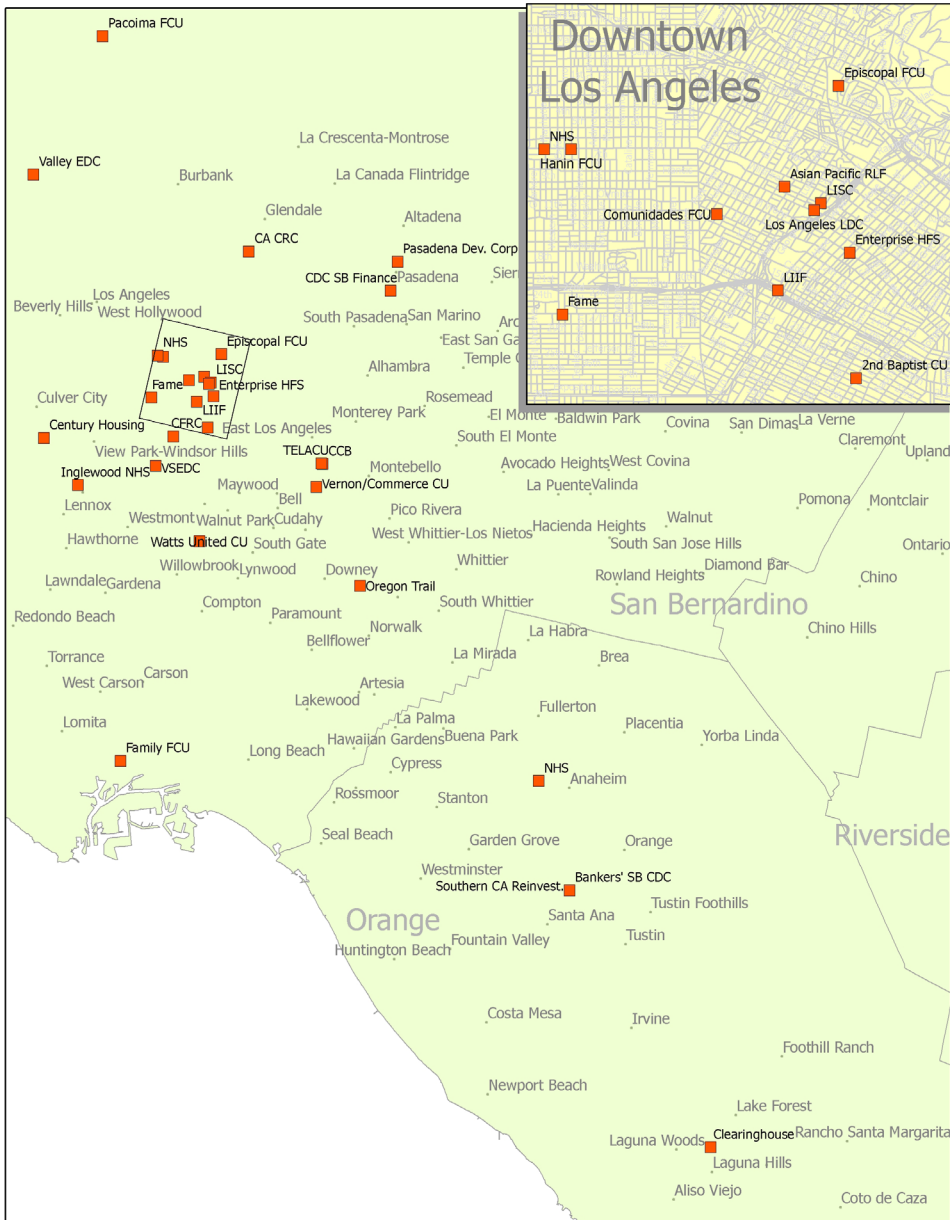
qualify for, and how to access the best deal to get the capital and technical assistance they need.

The CDFIs include the full range of CDFI sectors.

Breakdown of CDFIs by Type

Type	Number	% of Total
Loan Fund	23	71%
Credit Union	8	24%
Bank	1	3%
Venture Capital Fund	1	3%

CDFIs Based in Los Angeles and Orange Counties



Of those 33 CDFIs, 25, or 74%, are certified as CDFIs by the U.S. Treasury Department. Seven have offices in the Los Angeles MSA but are headquartered outside it, including some of the largest lenders, such as Enterprise Community Loan Fund and the Low Income Investment Fund (LIIF).

The nondepository CDFIs in the Los Angeles MSA tend to focus on either affordable housing lending or business lending. In other cities there are CDFIs that do both, and they often find synergies between real estate and business lending in a given community. Of the nondepository CDFIs in Los Angeles, 10 are housing/real estate-based lenders and 12 concentrate on lending to microbusinesses, small businesses, and minority-owned businesses.

The depository CDFIs include eight community development credit unions and one community development bank, Community Commerce Bank. The credit unions serve local areas and provide basic retail customer services. Community Commerce Bank was established by TELACU Community Capital, a Latino community development corporation headquartered in East Los Angeles. Community Commerce Bank is a full-service bank with eight branches throughout Southern and Central California. Broadway Federal Bank, although not a certified CDFI, was founded in 1946 to provide bank services in underserved neighborhoods. Today the bank has three branches in Los Angeles and more than 1,300 accounts.

Each of these CDFIs plays a useful role in the market and in its community. However, there is no dominant CDFI in the Los Angeles area, such as The Reinvestment Fund (TRF) in Philadelphia or Boston Community Capital in Boston. TRF provides financing for housing, business, and community facilities and has a policy department that integrates learning from its lending activities with research to make policy recommendations to the city and state. Many of the other 10 largest MSAs in the country also do not have one big player. That is both a strength and a weakness. From the customer's perspective, it is clearer where to go for assistance in a city where there is one large player. A dominant organization is more likely to have a policy presence and a "seat at the table" in community development policy discussions. On the other hand, dominant players often absorb most of the funding, making it more difficult for niche players to get started or stay in business. If the one dominant player has chosen not to serve a certain market, that market may remain underserved.

Housing CDFIs

Housing CDFIs in Los Angeles face one of the highest-priced housing markets in the country. That means every unit of affordable housing financed needs deep subsidy. Most subsidy comes from government sources. In the Los Angeles MSA, there are two housing CDFIs with notable sources of capital: a legal settlement from a highway project capitalized Century Housing, and the insurance industry capitalized Impact Community Capital.

Many of the larger housing CDFIs either are not headquartered in Los Angeles or lend statewide. Enterprise Community Loan

Fund, Local Initiatives Support Corporation (LISC), and the Low Income Investment Fund are national CDFIs with active offices in Los Angeles. California Community Reinvestment Corporation lends statewide and is located in Glendale. These groups mainly or exclusively lend to developers of affordable housing. There are three NeighborWorks America affiliates in the Los Angeles MSA, actively lending to low- and moderate-income people to do home repair or improvement and to purchase homes. The credit unions do that type of lending as well.

Business CDFIs

Los Angeles is a city with a growing, vibrant small business community, especially immigrant-owned businesses. Los Angeles is served by a wide variety of small business-focused CDFIs. Mirroring the Los Angeles community, such organizations tend to focus on a single area of Los Angeles or a single ethnic community. There are individual business CDFIs focused on the Latino, Asian, and African American communities located in East Los Angeles, downtown, and South Los Angeles. Many of them have larger service areas or target populations, but they concentrate their outreach and target their services to these particular communities.

One exception is Valley Economic Development Center (Valley EDC), located in the San Fernando Valley, which is an active lender to all businesses in Los Angeles, Ventura, and Santa Barbara counties (Ventura and Santa Barbara counties are not in the Los Angeles MSA). Valley EDC also houses the Small Business Development Center and the Women's Business Center for these counties, and it has a workforce program. Valley EDC works to be a one-stop shop for small businesses and says, "It's all about business." It works across the region and ethnic groups, and it partners with other CDFIs—such as by referring and selling deals to TELACU Community Capital in East Los Angeles and originating deals in partnership with FAME Assistance Corporation/FAME Renaissance (FAME) in South Los Angeles. It operates Small Business Development Center offices at FAME and the Asian Pacific Islander Small Business Program. Valley EDC has taken over the remaining portfolio of the Los Angeles Community Development Bank. Valley EDC sees its role in working with the local CDFIs and technical assistance providers as helping them with the components they don't have.

The Los Angeles Community Development Bank (LACDB) must be mentioned in any discussion of Los Angeles business lending. The "bank," which was not legally a bank, but a government-driven loan pool, grew out of public-private partnership in response to the 1992 Los Angeles riots and began lending in 1996. The bank made business loans in Los Angeles' federal Empowerment Zones, covering much of East, South, and Central Los Angeles. Capitalized by the U.S. Department of Housing and Urban Development with \$435 million, LACDB ranks as the largest federal inner-city development initiative ever.

LACDB had trouble from the outset. The report "The Los Angeles Community Development Bank: The Possible Pitfalls

of Public Private Partnerships”¹⁸ identifies a myriad of factors behind the bank’s difficulties, but the two root factors were (1) the weak foundation of the public-private partnership, and (2) the fractured nature of Los Angeles politics. An example of how the first factor played out is that banks were on board as co-lenders without a means for the city to enforce their co-lending. An example of the second was that city council members became informally involved in loans to their own districts but not the overall strength of the bank. By 1999, 60% of the portfolio was invested in problem loans, and the bank frequently exceeded its lending limits. A move to a CDFI model was explored, but the bank did not achieve certification. It filed for bankruptcy in early 2004, officially closing its doors in 2005.

Putting Los Angeles in Context: CDFI Activity and Assets in the 10 Largest MSAs

As part of this study, Opportunity Finance Network (formerly National Community Capital Association) sought to determine the level of CDFI activity and assets in Los Angeles as compared with such activity and assets in the other most populous urban areas in the United States. More critically, we wanted to know which areas have more activity and assets relative to the number of people living in poverty in those areas. Such data would be an indication of the level of resources available compared with the extent of the challenge. This is the first time a study has been done of CDFI assets and activity by geographic area, and the first time such resources have been compared with the level of poverty in those areas.

To complete this study, Opportunity Finance Network brought together data from two main sources: the Census Bureau, for population and poverty figures, and the CDFI Data Project (CDP), an industry collaboration that produces data about CDFIs. The CDP figures presented in this study are from fiscal year 2003, the most recent data available. A complete explanation of the methodology can be found in Appendix II.

Seventeen CDFIs in this data set work in Los Angeles, including 11 that work exclusively in the Los Angeles MSA and six that work in other areas as well. They include one bank, six credit unions, one community development venture fund, and nine loan funds.

Opportunity Finance Network selected three points of data about each CDFI that was active in the 10 most populous MSAs: total assets, total financing outstanding, and financing originated in 2003. Total assets provides a figure of the resources available to serve the low-income community in the MSA. Those assets may or may not be deployed. Total financing outstanding provides a measure of the level of the CDFI activity in the region over time. Such loans and investments were disbursed over a period of time and are in the process of being repaid. Financing originated in 2003 provides a snapshot of loan and investment productivity in the most recent year.

18 Julia Sass Rubin and Gregory M. Stankiewicz, “The Los Angeles Community Development Bank: The Possible Pitfalls of Public Private Partnerships,” *Journal of Urban Affairs* 23, no. 2 (2001): 133–153.

The 10 most populous MSAs in the United States are (in order) New York, Los Angeles, Chicago, Philadelphia, Miami, Dallas, the District of Columbia, Houston, Atlanta, and Detroit.

Los Angeles Findings

- Los Angeles is the second most populous MSA in the country, after New York.
- Los Angeles has the third most CDFI assets, loans outstanding, and loans originated as of 2003.
- Los Angeles has the highest percentage of individuals living in poverty of the 10 MSAs, 16%.
- Los Angeles ranks seventh in CDFI assets and loans outstanding per individual in poverty, and eighth for loans originated in 2003 per person living in poverty.

On an absolute level the resources and activity of the Los Angeles CDFIs rank well. However, they are not equipped with the resources available in other MSAs when compared with the number of people in poverty.

General Findings

- Chicago has the highest level of CDFI assets per person in poverty, \$1,414, followed by Atlanta with \$861 and New York with \$649; Los Angeles is ranked seventh at \$249. Dallas has the lowest assets available per individual in poverty at \$44.
- Chicago has the highest level of financing outstanding per person in poverty with \$854, followed again by Atlanta (\$524) and New York (\$376). Los Angeles is ranked seventh at \$161. Dallas was the lowest with \$30.
- In terms of financing originated in 2003, Chicago is again the highest with \$437, followed by New York (\$170) and Miami (\$127). Los Angeles is ranked eighth at \$88. Dallas and Houston were the lowest with \$35 and \$37 respectively.
- Texas has two of the largest MSAs in the country, Dallas (fifth largest) and Houston (sixth largest). These two MSAs consistently rank the lowest in terms of assets and lending activity.
- New York, the most populous MSA in the country with more than 18 million people, also has the largest number of CDFIs serving the MSA that are in our data survey, 50, followed by Philadelphia with 24. Los Angeles ranks third with 18. Houston is number 10 with three CDFIs.
- The range of average assets per CDFI serving an MSA ranges from \$97.9 million in Chicago to \$4.7 million in Dallas. Los Angeles is ranked sixth with \$29 million.

Chart 1 on page 9 shows a weighted average of CDFI assets and activities in the top 10 MSAs;¹⁹ it clearly shows Los Angeles in the seventh position.

Most of the largest CDFIs are community development banks, in part because banks can accept individual deposits, are

19 We weighted the data as follows: assets—30%, financing outstanding—40%, and financing originated in 2003—30%.

insured, and are familiar to customers. New York leads the top 10 MSAs with five community development banks in our data survey; next is Chicago with two. Los Angeles has one community development bank in the study. Two MSAs, Philadelphia and Dallas, do not have any community development banks in the study.

Where Do CDFI Assets Come From?

Most CDFI capital comes from private sources, including individuals, financial institutions, corporations, foundations, and religious institutions. In 2003, only 9% of CDFI debt capital came from either federal or state government. The CDFIs in the 2003 CDP study managed \$13.1 billion in assets at the end of fiscal year 2003. Although that represents a significant amount of capital for underserved communities, it is still quite modest compared with the mainstream financial sector. As of December 31, 2003, for comparison, U.S. financial institutions alone controlled almost \$9 trillion in assets.²⁰

The CDP collects data on the sources of a CDFI’s debt capital, which includes deposits for banks and credit unions. That does not include a CDFI’s equity or permanent capital. This data

is available for 276 institutions. By far the biggest source of capital overall is individuals, at 59%. Nonregulated institutions (the loan funds and venture capital groups) receive a greater percentage of their capital from corporations. Loan funds’ largest source of debt capital are banks, at 47%. In most cases, CDFI capital is below-market-rate capital, provided by socially motivated investors (individuals, religious institutions, foundations) or regulatory motivated capital (banks). Although CDFIs have been very successful in growing through accessing subsidized capital, it is in limited supply.

A relatively small number of institutions control a substantial portion of the assets of the industry, with 10 institutions in the CDP study controlling more than 42% of the assets. More than 70% of the organizations in the study have \$10 million in assets or less. In Los Angeles, 10 of the CDFIs had less than \$10 million in assets, and seven had more than \$10 million.

Conclusions

The challenges of providing access to capital to underserved people and communities are much greater than the resources available to the CDFIs in any of the MSAs. Even the MSAs with the most CDFI resources and activity could use much more activity. The CDFI industry is currently transitioning to scale, and it recognizes that it needs much greater resources

²⁰ As of December 31, 2003, according to the Federal Deposit Insurance Corporation.

Chart 1: Weighted CDFI Dollars per Individual in Poverty Across the 10 Largest MSAs

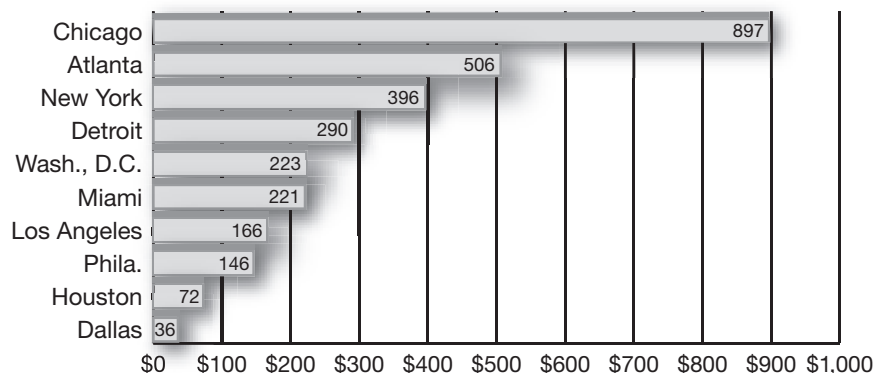
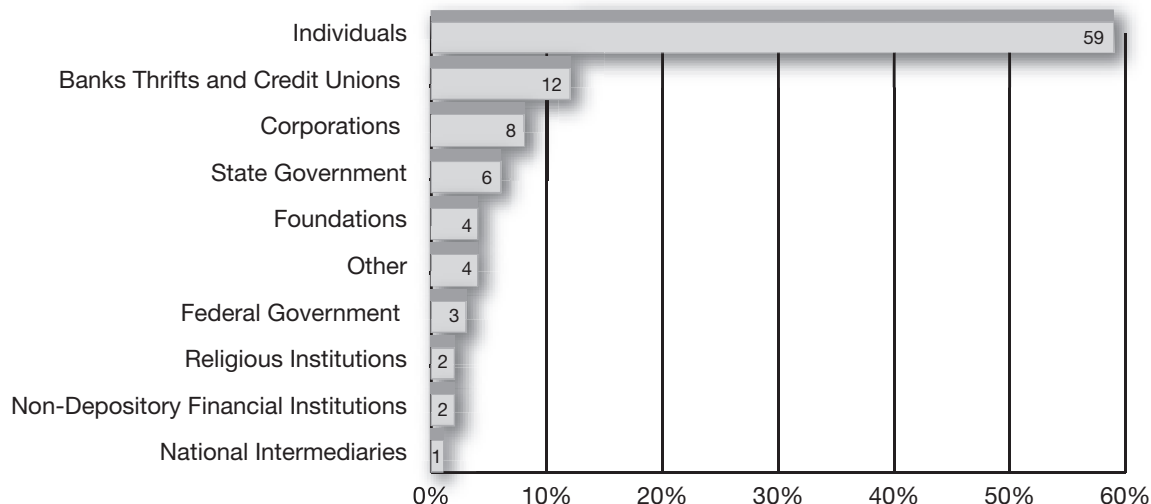


Chart 2: CDFI Sources of Debt Capital



in order to serve the growing markets. One aspect of reaching scale is for CDFIs to be able to access and use market rate capital, which is more available than subsidized capital.

The CDFIs in Los Angeles face the challenge of working in the MSA with the greatest percentage of impoverished people, with fewer assets per person in poverty. With these data, those CDFIs have a new approach to investors that should be helpful in recruiting additional capital.

The Affordable Housing Challenge in Los Angeles and the CDFI Response

Background

Housing costs in Los Angeles are among the highest in the country. Poor households in Los Angeles pay as much as 73% of their income for housing, compared with a country-wide average of 27%.²¹ In 2000, 30% of California households could afford the median price of a house, which was \$244,230, but by mid-2004, only 16% of California households could afford the median price at \$542,720.²²

Renters face similar problems. In 2000, an average two-bedroom apartment in California cost \$791 a month. In 2004, that price had reached \$1,104²³—a nearly 40% jump. Incomes in California rose only 12% in the same period.²⁴ In 2005, a worker earning the California minimum wage of \$6.75 per hour would need to work 128 hours per week to afford a two-bedroom fair-market-rent apartment in the Los Angeles

MSA.²⁵ At this cost, overcrowding is the norm. Sam Mistrano of the Southern California Association of Non-Profit Housing (SCANPH) says that often three families will live in one home.

Federal, state, and local programs have been actively producing affordable housing units for many years. Such units, however, account for only 3% (52,379 units) of the city housing stock, according to the Housing Crisis Task Force. Most such units are dedicated to very-low-income households. Fifty percent of current affordable rentals will expire before 2010 due to expiration of tax-credit time requirements. Moreover, fewer deals are getting done due to the high price of land, construction costs such as materials and prevailing wages, and the scarcity of subsidy to offset growing cost.

Demand for affordable housing far exceeds supply. Century Housing estimates that the need is for an additional 250,000 affordable units. Existing affordable units are overwhelmed with applicants. The Los Angeles Times reported in January 2005 that 150 advertised affordable units resulted in 3,000 applicants. Stephen Peelor of Century Housing says that for every affordable rental unit it helps produce, there are 10 families on its waiting list; Van Scott of Los Angeles Neighborhood Housing Services reports that 90% of people who are qualified through homeownership counseling cannot find a house they can afford to buy. Based on these figures, it appears that demand is 10 to 20 times the supply.

As in other high-cost markets, it's not just lower-income households that can't afford to live in Los Angeles and many areas of California. According to a recent opinion poll, there is widespread concern about the region's housing, with 80% percent of respondents across Southern California saying that it is difficult to find housing that even middle-class people can afford in their community. Most respondents doubted that the next generation will be able to afford to purchase a home in their community.²⁶ There is also concern at findings

21 Century Housing, "Affordable Housing," 2005, July 6, 2005 <http://www.centuryhousing.org/affordable_housing.htm>.

22 Daniel Yi and Dave McKibben, "Laws Aim to Ensure Low-Cost Housing; As Home Prices Soar, a Number of Cities Decree That Some New Units Be Affordable to Many," Los Angeles Times, August 15, 2005.

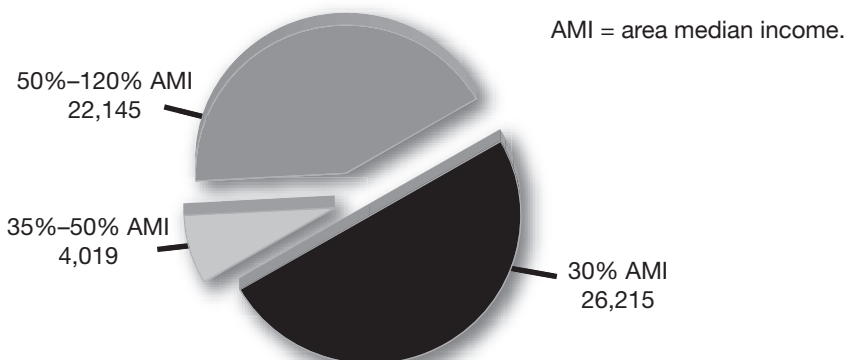
23 National Low Income Housing Coalition, "Out of Reach," 2005, October 7, 2005 <<http://www.nlihc.org/oor2004/>> Path: select state/California; select MSA/Los Angeles-Long Beach, CA HMFA.

24 V. Ngyuyen, "A Dream Denied: The African American Dream of Homeownership and Reality of California's Housing Crisis," Greenlining Institute, December 2004, July 5, 2005 <<http://www.greenlining.org>>.

25 Benchmark Institute, "Affordable Housing Quiz," September 30, 2005 <<http://www.benchmarkinstitute.org>>.

26 Jocelyn Stewart, "L.A. Becoming City of Renters, Census: Only 38.6% of Families Own Their Homes, a Reversal of National Trend, New Figures Show," Los Angeles Times, November 29, 2001, p. B-1.

Chart 3: Number of Affordable Housing Units by Level of Income



Source: Los Angeles Housing Department, August 2004.

“While Los Angeles County’s population increased by more than 1 million in the 1990s, housing production dropped by 70% from the previous decade.”

that California’s housing crisis is discouraging businesses from moving to California.²⁷ This makes workforce housing, housing for moderate-income households, a priority.

As housing becomes more expensive, the amount of subsidy to develop affordable housing increases. Neelura Bell of LISC says that to develop a 40-to-60-unit multifamily site, acquisition costs \$1.5 to \$2 million and development \$20 to \$25 million, resulting in a total cost of about \$275,000 to \$325,000 a unit. The cost of single-family homes can be twice that amount.

The major factors contributing to the housing crisis are as follows:

- Population increase—in the 1990s the Los Angeles MSA grew by close to 2 million residents, ranking second in the nation for population increase.²⁸
- Proposition 13 and anti-homeownership tax laws have created incentives for commercial development rather than housing production—during the 1990s, housing production dropped by 70% from the previous decade to only 120,000 units.²⁹
- Planning and zoning is slow to shift from sprawl to “smart growth” strategies when available greenfields are running out.
- Low area median income.

City building regulations and power structures that undermine attempts to introduce affordable housing in many areas include the historical approach to planning and zoning, which

is low density, and neighborhood resistance to mixed and affordable developments.

Elements of the housing crisis include

- one of the highest median monthly payment rates in the nation;
- low levels of homeownership (Southern California’s homeownership rate of 55% is lower only than New York’s³⁰ and compares to 68% nationally);
- overcrowding; and
- very high levels of homelessness.

The Housing Trust Fund and the Inclusionary Zoning Debate

The current Los Angeles housing crisis began in earnest during Richard Riordan’s mayoral administration (1993–2001). In response to the growing housing crisis and lack of city commitment to address the problem, SCANPH organized Housing LA, an advocacy group that included the Los Angeles Archdiocese, unions, and broad public support. The purpose of Housing LA was to lobby the city for a \$100 million affordable housing trust fund to kick-start affordable housing production. The media joined the cause in early 2001 after the collapse of a tenement that killed three and injured 35.

Under continued public pressure, the city organized a Housing Crisis Task Force to make recommendations on how to approach the critical housing shortage. Housing LA participated in all deliberations. In 2003, the task force made two major recommendations: establish an affordable housing trust fund, funded at \$100 million annually; and adopt an inclusion-

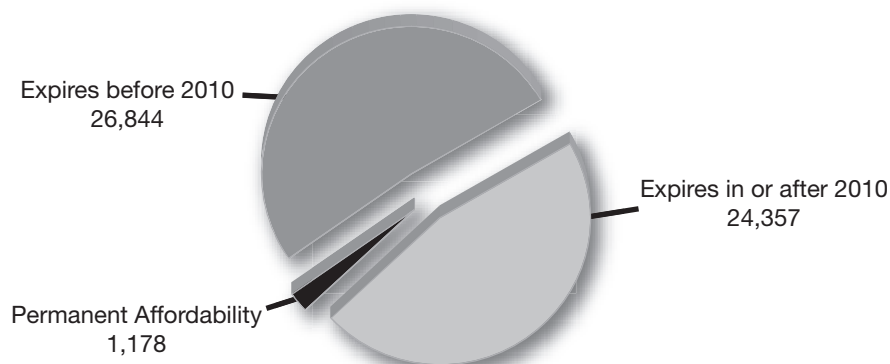
27 Ngyuyen, “A Dream Denied.”

28 Ngyuyen, “A Dream Denied.”

29 Brookings Institution, “Sprawl Hits the Wall: Confronting the Realities of Metropolitan Los Angeles,” Southern California Studies Center at USC and the Brookings Center on Urban and Metropolitan Policy, March 2001, July 20, 2005 <<http://www.brookings.edu/metro/la/abstract.htm>>.

30 M. Barreto, M. Marks, and N. Woods, “Homeownership: Southern California’s New Political Fault Line?” Prepared for Western Political Science Association, March 12, 2004, August 20, 2005 <<http://lmu.edu/csla/white/reports/homeownership.pdf>>.

Chart 4: Expiration of Affordable Rental Units



Source: Los Angeles Housing Department, August 2004.

“Housing production was halved between 1993 and 1998 although the city’s population increased by 300,000 in the 1990s.”

—Jan Breidenbach, SCANPH

ary zoning (IZ) ordinance. IZ is a mandate that requires any development over a set number of units to provide a percentage of affordable units.

IZ has existed in California and around the nation since the 1970s and is recognized as an effective tool for creating affordable housing. One hundred and sixteen, or almost 25%, of California jurisdictions have an IZ ordinance,³¹ including two within Los Angeles County: Pasadena and Santa Monica. All these programs account for about 34,000 of California’s affordable units.³² Southern California culture has traditionally been anti-density, and in Los Angeles most neighborhoods, even low-income ones, consist of detached single-family homes. The housing code has supported this in numerous ways, such as making it difficult to build three-story apartment complexes due to high-price sprinkler requirements, and making row or town homes difficult to build. As Ann Sewill of the Enterprise office in Los Angeles put it, “The culture is in the code.” For many decades the Los Angeles housing pattern has been to build further out from the city, but the county has just about run out of habitable land, and increasing density is the main way to increase housing supply at any price. “The key to increasing affordable housing in Los Angeles is going vertical,” says Michael Banner of the Los Angeles Local Development Company. So far, change to higher density has been slow. In downtown, new lofts are being built in former office and hotel buildings, but they are middle- to high-income units. The nonprofit affordable developers are just beginning to figure out how to take advantage of recent code changes. In this environment, IZ faces an uphill battle.

During the following mayoral administration of James Hahn (2001–2005), the city created the Housing Trust Fund. The first priority of the fund, as set out by the Housing Crisis Task Force, was to preserve and expand rental units for households earning below 60% of area median income; the second priority was to help households below 120% of area median income become homeowners; and the third targeted a homelessness prevention strategy. The trust funds are used in projects that have received other public funding, and they help to leverage funds for projects that might not otherwise be built. Changes were also made in zoning ordinances, which introduced more mixed-use zoning, but those changes did not stipulate or induce mixed-income developments. IZ ordinances were proposed and fiercely debated during the Hahn administration but did not reach a vote in city council.

Affordable housing advocates met the city’s creation of the Housing Trust Fund with widespread approval but later criticized Mayor Hahn for failing to approach anywhere near the targeted \$100 million a year.³³ It is difficult to ascertain the exact figure of the trust fund each year, but it appears to have been no higher than \$50 million. Hahn was also criticized for failing to devise a strategy that could finance the trust fund annually. According to the Planning Department, the Housing Trust Fund has helped build 1,000 units of affordable housing since its creation in 2002.

Affordable housing advocates launched a campaign to get permanent sources for the trust fund. IZ is one obvious source of funding: developers who want to waive the IZ requirement would pay into the fund, but this in turn depends on how the final IZ ordinance (or ordinances) is written and successful passage of IZ legislation.

In 2002, the city commissioned a study of the feasibility of IZ in Los Angeles.³⁴ That study reached two major findings:

1. IZ requirements did not have a negative effect on housing and construction in other California cities; and
2. IZ is economically feasible for most residential building types in Los Angeles when developers receive some kind of benefit to offset the costs.

In contrast, two studies commissioned by the California Building Industry Association (BIA) found that IZ ordinances make the housing crisis worse.³⁵ Those studies found that mandatory IZ laws in Los Angeles and Orange counties drove the price of new homes up an additional \$33,000 to \$66,000, and that the construction of new houses dropped by an average of 31% the year following adoption of IZ policies. The Los Angeles Inclusionary Zoning Coalition responded by saying that if the right developer incentives and compensation are offered, there is no disincentive to housing production.

A clear-cut line was drawn in the IZ debate, with builders, realtors, neighborhood councils, and business groups on one side, under the Los Angeles Business Council and Center City Association, and on the other side, housing advocates, most notably the Los Angeles Inclusionary Zoning Coalition, comprising 65 housing organizations, religious groups, unions, and social justice groups.

31 City of Walnut Creek, “Inclusionary Zoning Housing Ordinance,” August 2004, attachment B, October 7, 2005 <<http://walnut-creek.org/pdf/IZProceduresManualAPPENDIX.doc>>.

32 Non-Profit Housing Association of Northern California, “Seven Bay Area Foundations Announce Quarter of a Million Dollars to Launch Initiative That Will Double Inclusionary Housing Production,” press release, June 7, 2004, October 1, 2005 <<http://www.nonprohousing.org>> Path: About; Pressroom; Releases; Posted; Inclusionary Housing.

33 Ngyuyen, “A Dream Denied.”

34 David Paul Rosen and Associates, “City of Los Angeles Inclusionary Housing Study,” Los Angeles Department of Housing, September 25, 2002, October 30, 2005 <<http://www.lacity.org/lahd/inclusio.htm>>.

35 B. Powell, E. Stringham, and A. Moore, “Housing Supply and Affordability: Do Affordable Housing Mandates Work?” The Reason Public Policy Institute, June 2004, September 4, 2005 <<http://www.reason.org/ps320.pdf>>.

“Trust fund campaigns in California face tremendous political obstacles created by both Propositions 13 and 218—which, combined, require a two-thirds vote on all taxes and a vote of the affected homeowners on property-based fees. Triggering either of these votes meant losing.”

— Jan Briedenbach, SCANPH

BIA proposed that IZ be voluntary, or merely an available density bonus, a move supported by Mayor Hahn. BIA shifted emphasis from IZ to a \$500 million affordable housing bond measure, which would go before voters in 2006. The bond measure would go toward funding the Housing Trust Fund. In contrast, IZ advocacy groups see IZ as the key to scale affordable housing production, and they would require that the IZ be mandatory and that builders be compensated by density bonuses and other incentives (e.g., building deviations from area requirements or a reduction or waiver of required parking).

In July 2005, Mayor Antonio Villaraigosa took office. His campaign had detailed plans for affordable housing, including using smart growth, increasing first-time homeownership and middle-class homeownership, financing the Housing Trust Fund at the proposed rate of \$100 million a year, and passing an IZ ordinance. IZ advocates temporarily shelved the issue as they crossed their fingers and waited for the November 2005 special election to fill two city council seats with pro-IZ members.

In October 2005, the Los Angeles Business Council hosted a Mayoral Housing Summit. One of the challenges put to Mayor Villaraigosa was how to secure long-term financing for the Housing Trust Fund. The mayor chose the hardest option: to place before the voters a \$1 billion bond measure to finance the fund over 10 years at \$100 million per year. The bond measure would need to receive two-thirds of the vote to pass. Early polling suggests that about two-thirds of Los Angeles supports the measure, and the higher the bond amount, the higher the support. That suggests Angelinos want a response equal to the size of the issue.

Now comes a twist in the IZ debate: the Los Angeles Business Council will work with advocates of affordable housing to promote the bond measure before it goes to the voters in two years, but only with the understanding that IZ advocates will not push the IZ agenda. The IZ side of the debate has agreed to cooperate.

According to LISC’s Neelura Bell, in the end, the issue may be whether IZ is citywide or confined to certain areas. Even if IZ laws were to pass, implementing high-density developments would remain very difficult because there is still the issue that developers are required to give notice and neighborhood councils and the public can appeal the development.

Incentive and Building Code Responses to the Housing Crisis

One proposal put forward by the Housing Crisis Task Force was to change the building codes to make them more density-friendly, as, for instance, a recent ordinance permitting smaller lot sizes does. Several ordinances have passed to this end.

- **The Density Bonus.** A few years ago, the state enacted a law that granted a minimum of 25% extra density to developments that put aside 10% to 20% of their units for affordable housing. Few developers took advantage of this so the city supplemented the offer with increased density near transit corridors. In 2005, the state further increased the density bonus and decreased the percentage of affordable set-asides. The city supplemented the state ordinance with a sliding scale, for greater flexibility in implementing the bonuses.
- **Town Homes Ordinance.** Town homes (or row houses) used to come under the purview of the Condominium Association with its high cost of construction defect liability insurance, which could run \$20,000 per unit. That slowed both town house and condominium development. The new Town House Ordinance allows homes to be built on smaller lots. The ordinance allows the buyer of a small-lot town home to own the land and the structure, thus removing the surplus cost. This will allow more homes to be built per block, without side yards, making the entire project more cost-effective.
- **Live/Work Initiative.** Effective from July 2000, the city adopted an ordinance for the Live/Work Initiative. The ordinance changed zoning to allow warehouses to be zoned as residential. This has spread from around the downtown and North Hollywood to Venice Beach.
- **Adaptive Reuse Ordinance.** Similarly, the Adaptive Reuse Ordinance, adopted in 1999, allowed for former offices to be converted to residential spaces. The rezoning ordinance is fully applied in Hollywood, Koreatown, and Chinatown, and a modified version is applied citywide.
- **Residential Accessory Services Zones.** In 2003, two new zones, Residential Accessory Services zones, were created to allow mixed-use development along commercial and transportation corridors, allowing for increased height and floor area, and reduced setbacks. The two zones differ by the density of units per acre. This has been quite successfully implemented in the downtown and inner-city areas, but it has been difficult to implement in lower-income areas.
- **Transit-Oriented Development.** The transit-oriented districts now allow higher density along Los Angeles’ 40 miles of light rail, 18 miles of subway, commuter lines, and perhaps some bus lines in the future. One ordinance allowed for a density bonus around transit stations for affordable units. Following this was an ordinance that included density bonuses within 1,500 feet from station stops, and the city has aims to increase incentives

to developers by providing a menu of options, such as reductions in parking, open space, and setback requirements. Developers can choose one or more options depending on the percentage of set-aside units and the income level of the units. Jane Blumenfeld, the principal city planner in the Los Angeles City Planning Department, said that these transit-oriented development ordinances have not had much of an impact to date. She feels that attitudes toward higher-density developments need to alter, as was the case in San Francisco when similar ordinances were implemented around the BART.

Stakeholders in Los Angeles' affordable housing market acknowledge that such ordinances have had only limited impact so far outside of downtown. The culture of higher density has not sunk in enough for the ordinances to have teeth. Both LISC and Enterprise Community Loan Fund work with community development corporations (CDCs) and developers to help them work with the new ordinances.

Homelessness

The Los Angeles Homeless Services Authority conducted a comprehensive homeless count in Los Angeles County and published the results in the 2004 report "Homeless in LA."³⁶ The report concluded the following:

- On average, at any point in time, 78,600 individuals were homeless in Los Angeles, and during the course of a year 253,900 were homeless. Homelessness in Los Angeles is more than twice as high as the highest national rate.
- There are approximately 18,500 shelter beds in the county, which is a bed for one in five homeless people. Fifty-five percent of homeless people sleep in places "unfit for human habitation" on any one night.
- Homeless residents are skewed to younger ages, with many young mothers and their children. Children make up 25% of the point-in-time population.
- An estimated 17% of the homeless population has been homeless for a year or more.

Geographically, most services for the homeless are close to downtown. Recent loft conversions and revitalization have displaced many in the downtown area. The city moved those people east of downtown but made no attempt to shelter them. "Homeless in LA" found that there is a great unmet need for services in South Los Angeles and then San Gabriel Valley. That is where the greatest number of ex-foster homeless youth are found.

The report "Bring LA Home," the follow-up to the first report, outlines four scenarios ranging from optimistic to cautious, for ending homelessness in the city, with prevention as the key. All four scenarios in the report emphasize the need for training and job placement as the service needed by the greatest number of people; however, there is a real shortfall in such services available for the homeless.

Current city expenditure on homelessness is estimated to be only 35% to 59% of the cost required of an effective strategy over the next 10 years. Recent studies indicate that the cost of housing chronically homeless people is nearly offset by savings in the mainstream health system, law enforcement, and correctional costs. One study commissioned by the city and county of San Diego revealed that 15 individuals who were chronically homeless cost the city and county nearly \$3 million in 18 months.

It is not financially feasible to end homelessness unless the numbers becoming homeless are dramatically reduced, as "Bring LA Home" concludes. Reducing the flow of people from major government institutions into homelessness would reduce the total estimated cost by 47%. For example, more than half of the 1,000 foster youth emancipated each year become homeless. More than half of homeless youth enter the justice system.

Single-room occupancy hotels and transitional housing have been financed by CDFIs such as the Low Income Investment Fund and Century Housing. Typically, transitional housing provides additional social services for residents. Century Housing's Century Villages at Cabrillo is the largest residential social service complex of its kind in the country, serving 10,000 homeless people every year and placing 1,000 into jobs annually. The Low Income Investment Fund also finances transitional housing.

Since the publication of "Homeless in LA," homelessness ostensibly has been higher on the city's agenda, but there has been no activity to date. Villaraigosa did not campaign on this issue, so groups working with the homeless population are not hopeful.

CDFI Financing for Affordable Housing

Banks and mainstream financing have been more active in the housing development market over the past five or six years, especially in construction financing, so CDFIs now fill specialized gaps. These gaps are generally riskier types of financing, predevelopment and permanent capital, and smaller acquisition and construction loans. Many of the larger banks such as Wells Fargo, Citibank, and Bank of America refer developers to the larger CDFIs for loans they are unwilling or unable to make. CDFIs financing real estate and housing in Los Angeles find that they need to close loans within 30 days because of the active real estate market.

In the face of high costs, decreasing subsidy, and increasing need, CDFIs are also looking for new ways to finance affordable housing production. The time developers need to cobble together financing and subsidy and entitle the land can take up to a year. This is a key obstacle to affordable developers, especially given the time constraints of a heated housing market. Many CDFIs are working with developers to offer products that allow them the speed and flexibility they need.

The California Community Reinvestment Corporation (CCRC) has an equity fund among its financing funds. CCRC invests up to 25% of equity in workforce housing developments (80% to 120% of area median income) to develop for-sale housing. The

³⁶ Fleming, Burns, and Haydamack, Homeless in LA.

state, cities, or municipalities provide soft second mortgages. The only other subsidy with this type of financing may be a density bonus and other waivers and allowances, depending on the area. CCRC is the first in and last out, so the investment is higher risk. CCRC's Mary Kaiser says that CCRC has a reliable core of returning developers who know about developing for-sale housing and like its equity product. Some of the developers have started investing in the fund themselves.

Other CDFI products that provide the same time-flexibility incentive to developers of affordable housing as equity are lines of credit and long-term mortgages. The Low Income Investment Fund is developing a line of credit for acquisitions. With that product, developers can better compete with market-rate developers at the crucial stage of acquisitions. Another form of flexible capital is Clearinghouse CDFI's permanent capital for developers, which is amortized as a 30-year mortgage. Enterprise Community Loan Fund offers mini-permanent loans and equity bridge loans.

CDFI Strategies for Homeownership

Homeownership in Los Angeles is slowly broadening to encompass condominiums in multifamily developments as single-family affordable housing becomes less viable. This is a culture change for Southern California. CDFIs and other stakeholders have been quick to grasp this, but it has been difficult bringing many of the developers along given the obstacles to higher density found in building codes and elsewhere.

One strategy for homeownership for lower-income households is lease-purchase. In Los Angeles, the Affordable Housing Clearinghouse, a subsidiary of Clearinghouse CDFI, has a lease-purchase program. In 2004 Clearinghouse, through partnership with state lease-purchase programs, financed more than \$11 million in lease-purchases.

Enterprise's strategy in Los Angeles was initially to focus on homeownership through loans to CDCs. This was at a time when other groups were focusing on rental. Enterprise has continued homeownership strategies through its subsidiary Enterprise Home Ownership Partners (EHOP). EHOP also has focused on moderate-income households for homeownership. EHOP made an agreement with the city to buy all foreclosed FHA housing in bulk in East, South, and Central Los Angeles and the San Fernando Valley. EHOP rehabs them and sells them with soft second mortgages from the city. Some of the sales are exclusive to teachers and police officers. The program receives loans and grants from banks and foundations. Now that FHA properties are becoming scarce, EHOP is focusing more on infill and town house developments.

Another strategy is to keep affordable units affordable. Century Housing monitors the affordability of some 5,000 units that it helped develop. These single-family homes and condominiums are kept affordable through a right-to-purchase agreement, allowing Century to buy back units that come on the market.

Los Angeles Neighborhood Housing Services, Ingelwood Neighborhood Housing Services, Neighborhood Housing

Services of Orange County, and Clearinghouse CDFI offer financial products to individuals seeking homeownership.

The Outlook for Affordable Housing in Los Angeles

How the city council votes on IZ will likely have a large impact on the course of affordable housing in Los Angeles; so too will other national factors, such as interest rates and the economy. There is much debate over how frothy the market is and how much a housing bubble burst would bring prices down. One national study shows that Los Angeles has a high house-price:income ratio, similar to other California cities.³⁷ The study predicts that the bubble in Los Angeles wouldn't begin to deflate before the city experiences at least 12 months of decline in economic output, as happened in the late 1990s.

The Center for the Study of Los Angeles surveyed Southern Californians to gauge attitudes toward "no growth" versus "suburban sprawl." Respondents were fairly evenly split as to what they favored, with renters more likely to favor the no-growth option. The survey did reveal that no-growth was more favored where the benefits of no-growth, such as proximity to work, preserved open spaces and allowed the next generations to buy in the area. To be more receptive to many of the strategies used to produce affordable housing, it appears that Southern Californians need to see the benefit first.³⁸

Small Business Development and Finance in Los Angeles

The Los Angeles Economy

A recently released study by the Milken Institute's Los Angeles Economy Project³⁹ paints a mixed picture of the Los Angeles small business economy. On the one hand, the economy has recovered from the recession of the early 1990s that was triggered by defense cuts and a credit crunch. The overall number of jobs increased 7% from 1992 to 2002. The recovery is due in large part to the influx of immigrant population and entrepreneurialism. Chart 6 found on page 16 shows that jobs increased in every sector except manufacturing.

The number of businesses increased at a much higher rate, 34%, as many larger employers closed or downsized and smaller establishments opened. As of 2001, more than 56% of all business establishments in Los Angeles were small enough to be considered microenterprises, having four employees or less. More than 85% of all business establishments are in the size range that business CDFIs generally lend to, with 19 employees or less.

The current job market is more polarized between low-end and high-end jobs than it was in 1990. The Milken study identifies

37 James Hagerty, "Bubble Metrics: Economists Handicap Housing Markets," Wall Street Journal, August 24, 2005, August 25, 2005 <http://online.wsj.com/public/article/SB112474611480519927-7SYqDPFbNMg3Sz0rH5NguPe10UI_20060825.html?mod=rss_free>.

38 F.J. Guerra, M. Marks, and H. Brackman, "Rebuilding the Dream: A New Housing Agenda for Los Angeles," Loyola Marymount University, October 2001, July 15, 2005 <<http://www.lmu.edu/cscla/white/reports/rebuild/rebuild.pdf>>.

39 Klowden and Wong, "Los Angeles Economy Project."

two barriers to the growth of higher-end jobs: the skills gap in the labor market and the difficult business environment, including limiting regulations and the lack of affordable capital. The Los Angeles labor market is less educated, with lower high school and college graduation rates than the surrounding counties, the state of California, and the nation as a whole. Los Angeles businesses tend to create high-end and low-end jobs and few jobs in the middle.

An interesting example of how the economy shifted in Los Angeles since 1990 is the manufacturing sector. While manufacturing is still a surprisingly significant sector of the Los Angeles economy, it declined from 19% of those employed in 1992 to 16% in 2002. Within the manufacturing sector, many unionized, high-paying jobs disappeared in the aerospace industry (from 13.7% of total manufacturing employees in 1982 to 8% in 2003) while other lower-paying jobs were created in the garment industry (an increase from 8% to 12.8% of total manufacturing employment for the same period).⁴⁰

Los Angeles has considerable competitive advantages, including a variety of higher education institutions, the international airport, multiple ports, and a connection to the global economy through its diverse population. Not surprisingly, one of its competitive disadvantages is the high cost of housing. Other factors limiting the Los Angeles economy in addition to the lower-skilled workforce include traffic congestion, higher crime rates, and higher taxes.

Los Angeles Business CDFIs

As a group, the Los Angeles business CDFIs have smaller staffs and lower levels of assets and loans outstanding than the housing CDFIs. They are also less engaged in policy. Many serve a particular section of the city, focus on a particu-

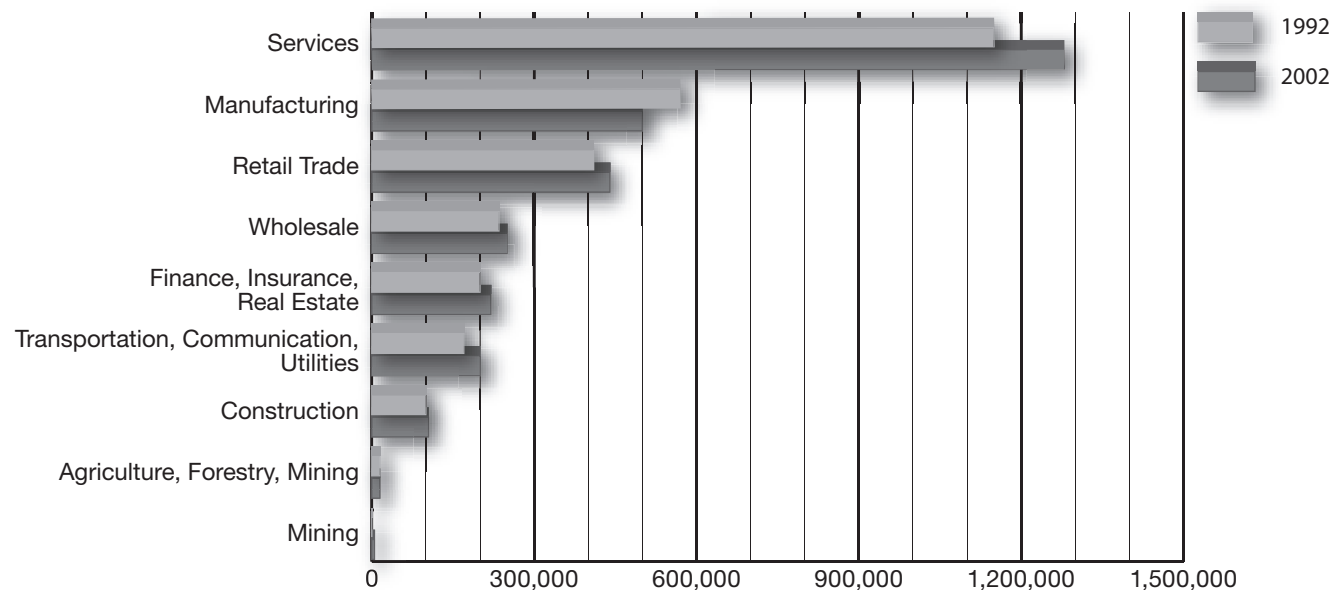
lar minority group, or both. Among the missions of business CDFIs are helping low-income people, minorities, and women create businesses and creating jobs for those populations by helping small businesses expand and grow. The neighborhood-based CDFIs—such as Community Financial Resource Center, Asian Pacific Revolving Loan Fund, and TELACU Community Capital—are more focused on helping local residents start businesses. Those businesses often are local retail or service businesses with few linkages to the larger economy. Such activities can help individuals and families become self-sufficient and provide needed services to the local neighborhood. Other CDFIs, such as Valley Economic Development Center and Los Angeles LDC, focus more on helping existing businesses expand, acquire a site, or open a second location. Valley EDC also operated the Small Business Development Center for most of Los Angeles County.

A third type of CDFI business finance activity is community development venture capital, where the CDFI provides equity or quasi-equity to a business with high growth potential. The only CDFI providing venture capital financing and advising in Los Angeles is Pacific Community Ventures, which has invested in eight Los Angeles-area companies. It opened an office in Los Angeles in 2005, which should help focus more attention on this market.

The small business lending environment has become a great deal more competitive, with banks encroaching on what had been CDFI markets in the past. Through credit scoring and use of government credit enhancements such as the SBA 7(a) Guaranty Loan Program, many banks are making smaller loans to riskier borrowers. In 2004, the 25 largest SBA lenders in the Los Angeles district increased their number of loans

40 Klowden and Wong, "Los Angeles Economy Project."

Chart 5: Los Angeles County Employment Numbers



Klowden and Wong, "Los Angeles Economy Project."

originated by 30.8% for a total of 4,843 loans.⁴¹ Bank of America, the top originator, offers business loans as small as \$5,000, and its average 7(a) loan was \$35,000.

Los Angeles is divided into seven planning districts. There is a CDFI presence in each of those districts, some stronger than others. Many of the business CDFIs in Los Angeles focus on just one of the planning districts, and Valley Economic Development Center covers them all.

CDFI Business Lenders in Los Angeles' Planning Districts

When business CDFIs focus on job creation, they often target certain industries based on their propensity to create jobs with living wages, potential for employee advancement, or other benefits to help employees become self-sufficient. The Milken Institute has done a thorough analysis to evaluate which industries are prevalent in Los Angeles, offer sustaining salaries, and have stable or growing employment. It developed a list of 76 industries that meet these criteria.⁴² It further analyzes which industries are prevalent in each of the planning districts. Up until now, the business CDFIs in Los Angeles have been more focused on helping individual entrepreneurs or serving any business with access to capital challenges. To our knowledge, they have targeted specific industries, with the exception of Pacific Community Ventures.

The Milken report found a rough northwest/southeast divide in prosperity in Los Angeles, with East and South Los Angeles lagging behind West Los Angeles and the Valley along many

41 David Nusbaum, "SBA Lenders: Ranked by Value of Loans Awarded in L.A. District," Los Angeles Business Journal, December 6, 2004.

42 Klowden and Wong, "Los Angeles Economy Project," pp. 252-255.

different poverty and proficiency measures. East Los Angeles and South Los Angeles have 32% and 37% working poor residents; the Valley has 18%. More than one-third of workers in South and East Los Angeles do not earn a living wage. Wages correlate closely with educational attainment. A little more than 25% of city residents do not have a high school diploma, but a disproportionate number of such people live in East and South Los Angeles. Those areas are also home to a higher proportion of residents with limited proficiency in English. Employers increasingly demand employees with English language proficiency, and residents with low English language proficiency are constrained in their job opportunities.

Recommendations

Based on our research into the particular challenges Los Angeles MSAs face and on our knowledge of the CDFI industry generally, we offer recommendations in three areas: recommendations for the CDFIs themselves, policy recommendations, and one recommendation for the entire CDFI industry.

Recommendations for CDFIs

1. The Los Angeles area CDFIs tend to focus exclusively on the housing or small business market. This leaves a gap of nonhousing real estate deals, such as community facilities and mixed-use properties. A few CDFIs are working to fill that gap, such as Clearinghouse CDFI, which does larger real estate deals through its New Markets Tax Credit program, and the Low Income Investment Fund, which finances educational facilities. However, no one is financing the smaller, neighborhood deals in commercial strips or the small-to-medium-size community facilities deals on a consistent basis. This is a critical market as nonprofits are a critical component of the city's

CDFI Business Lenders in Los Angeles' Planning Districts

Planning District	Active Business CDFIs	Business and Demographic Characteristics
North Valley	Valley Economic Development Center	Used to house major defense/aerospace manufacturers and has become a center for research and testing. Construction industry expanding. Highly educated workforce.
South Valley	Valley EDC	Dominated by entertainment industry.
West LA	Valley EDC	Financial sector located here, which created growth in the legal and information technology sectors.
Central LA	Asian Pacific Revolving Loan Fund, Los Angeles LDC	Central LA lost a great deal of the financial services industry to consolidation and to West LA. Gains in high-end service and low-end retail jobs.
East LA	TELACU Community Capital	Businesses that serve the local residential population, mostly low-end retail and service. Mostly very small businesses with minimal linkages to the rest of the region.
South LA	Community Financial Resource Center, FAME, Vermont Slauson EDC	Lost much of its manufacturing base. Only planning area to have net job loss from 1996 to 2002. Highest percentage of minority-owned businesses. Much vacant land and brownfield sites have development potential.
Harbor	Valley EDC	An "old economy" area, with jobs generated by the port, automobile, and fabricated metal industries.

employment base, its tourism business, and services for low- and moderate-income people. Los Angeles needs a consistent provider of capital to this market.

2. Housing CDFIs should embrace “higher-density” or “smart-growth” strategies, educating and promulgating such strategies among their CDC borrowers. Higher density is a tough sell in Los Angeles, because of the longstanding culture and a housing code that promotes single-family dwellings. Yet the only solution to more housing in a reasonable proximity to jobs is to “go vertical.” The community development industry should consider a branded campaign to promote the concept of town homes, apartments above commercial strips, and small apartment buildings that are a key element of the city’s future prosperity.
3. Business lenders need to make the connection between their borrowers and the labor market. As the Milken study demonstrates, many of the growing industries create substandard jobs that provide wages below 150% of the federal poverty level. Business lenders should target business sectors that can create better jobs and career ladders. They should also make connections with the Workforce Investment Board and other workforce agencies to make sure better-quality employers and borrowers are getting access to employees with the skills and knowledge they need. Finally, business lenders should educate and provide technical assistance to borrowers about being employers when appropriate. As businesses grow from no employees to a few employees and then from five employees to the 6–15 range, they often need assistance in understanding how to train, supervise, manage, and provide the right level of wages and benefits. The CDFIs could also assist business borrowers in accessing the various local, state, and federal benefits available to them for hiring and retaining low-income employees.
4. Business lenders that are area-specific should focus on growing good jobs in their areas, especially in East and South Los Angeles, which have a disproportionate number of non-living wage jobs. Employers require employees with English language proficiency, and in those areas there is a high percentage of low-English-proficient individuals. CDFIs there should work to educate residents about the importance of English-speaking skills to their future prosperity and help employers and borrowers connect residents with English-for-speakers-of-other-languages classes.
5. Los Angeles CDFIs should continue their efforts to rationalize the capital delivery system, as CDFIs in other parts of the country are doing. For example, Valley Economic Development Corporation is co-lending with other business CDFIs and managing other portfolios. CDFIs around the country are discovering ways to be more efficient and effective through improving operations, outsourcing, and consolidation. In an era of less subsidy, the Los Angeles CDFIs must remain focused on ways to improve capital access for their markets while improving efficiency.

Policy Recommendations

6. To effectively address the housing crisis in Los Angeles, Los Angeles CDFIs must create, build, and maintain collaborations with other groups that have similar interests, including large employers of middle- and low-income people, unions, and others. Housing CDFIs must continue the effort for policy and regulatory solutions to the housing crisis, including inclusionary zoning, full funding of the Housing Trust Fund, and various changes to the housing code that will permit greater density. The Southern California Association of Non-Profit Housing is making strong inroads on this recommendation.
7. Business CDFIs should advocate for workforce initiatives for small businesses. Most workforce initiatives focus on large businesses, where the initiative can place many people with one employer. However, much of Los Angeles’ economic growth is in the small business arena, and those employers need workers with specific skills and abilities to compete. Los Angeles CDFIs could learn from the experience of two CDFIs active in workforce development: Seedco in New York City and The Reinvestment Fund in Philadelphia.
8. Despite all their accomplishments, Los Angeles CDFIs need more resources to deal with the scope of the problems in Los Angeles and the level of poverty. The resources could come through a combination of direct investments by the private and public sectors, tax incentives, and regulatory schemes. As we have shown, Los Angeles CDFIs have a lower amount of assets per person living in poverty compared with the other large MSAs. The state of California and the city of Los Angeles should encourage investments in CDFIs through direct investments and other means. CDFIs multiply federal government investment 27 times with private investments. This is an opportunity for CDFI investors, bankers, and government officials to convene and develop solutions drawing on national innovations and apply them to the Los Angeles context.

In its recently released report, the Milken Institute made some specific recommendations about raising capital that we endorse:⁴³

- Create a Los Angeles capital access program to provide loan loss guarantees, similar to the California Capital Access Program.
- Create a Los Angeles community investment note that pools investments from institutions and individuals à la Calvert and invest in CDFIs.

CDFI Industry Recommendation

9. The CDFI industry should collect and analyze geographic data reflecting its lending activity. Such data will help individual CDFIs compare the locations of their loans with poverty patterns and other geographic data. That may help CDFIs further target their activities. From an industry perspective, Opportunity Finance Network could analyze geographic lending patterns overall compared with poverty patterns over all the MSAs and rural areas.

43 Klowden and Wong, “Los Angeles Economy Project,” p. 19.

Appendix I: CDFIs Active in Los Angeles

CDFI Name	City	County	Area Served
ACCION San Diego	San Diego	Orange	San Diego, Orange, Riverside, San Bernardino, and Southern LA counties
Asian Pacific Revolving Loan Fund of Los Angeles	Los Angeles	LA	LA City and County
Bankers' Small Business CDC of Orange County	Santa Ana	Orange	Orange County and parts of Riverside
California Community Reinvestment Corporation	Glendale	LA	State of California
CDC Small Business Finance	Pasadena	LA	San Diego, Orange, and Riverside counties
Century Community Development Inc./ Century Housing	Culver City	LA	Greater metropolitan Los Angeles
Clearinghouse CDFI, The	Lake Forest	Orange	Los Angeles, Orange, and San Diego counties; Oakland and Sacramento
Community Commerce Bank	Los Angeles	LA	California
Comunidades Federal Credit Union	Los Angeles	LA	The area bounded by Olympic Boulevard, the Santa Monica Freeway, the San Pedro Freeway, and Normandie Boulevard
Enterprise Community Loan Fund	Los Angeles	LA	Los Angeles metropolitan area
Episcopal Community Federal Credit Union	Los Angeles	LA	Echo Park Community and through Episcopal outreach programs
FAME Assistance Corporation/FAME Renaissance	Los Angeles	LA	Los Angeles area, with a target focus on Koreatown, Lynwood, East Los Angeles, Compton, Watts, Crenshaw, and West Adams
Family FCU	Wilmington	LA	Wilmington
Hanin FCU	Los Angeles	LA	Los Angeles County
Impact Community Capital LLC	San Francisco		State of California
Inglewood Neighborhood Housing Services Inc.	Inglewood	LA	Inglewood and the South Bay
Local Initiatives Support Corporation	Los Angeles	LA	Neighborhoods that are most at risk, spanning across East Los Angeles, Downtown, the Valley, Hollywood, South Los Angeles, and the Westside
Los Angeles Community Reinvestment Committee, dba Community Finance Resource Center	Los Angeles	LA	The area bounded by Pico Boulevard, 120th Street, Crenshaw Boulevard, and Alameda Street
Los Angeles LDC Inc.	Los Angeles	LA	Greater metropolitan Los Angeles
Low Income Investment Fund	Los Angeles	LA	Core markets: Northern California, Southern California, and the New York metropolitan area
Neighborhood Housing Services of Orange County	Anaheim	Orange	Low- and moderate-income neighborhoods of Orange County
NHS Neighborhood Lending Services	Los Angeles	LA	Southern California
Oregon Trail Corporation	Downey	LA	LA and Orange counties

Pacific Community Ventures Investment Partners	Los Angeles	LA	State of California, but focus on Bay Area and LA
Pasadena Development Corporation	Pasadena	LA	San Gabriel Valley and Los Angeles County
Second Baptist Church CU	Los Angeles	LA	Members are from the congregation and reside for the most part in South LA
Southern California Reinvestment CDFI	Santa Ana	Orange	Orange, Riverside, and San Bernardino counties and contiguous communities
TELACU Community Capital	Los Angeles	LA	Southern California
Valley Economic Development Center	Van Nuys	LA	Los Angeles, Ventura, Santa Barbara, and Orange counties
Vermont Slauson Economic Development Corporation	Los Angeles	LA	South Los Angeles
Vernon/Commerce CU	Commerce	LA	Serving employees in the cities of Vernon, Commerce, Huntington Park, Bell, Bell Garden, East LA, and zip codes 90022 and 90023
Watts United CU	Los Angeles	LA	The Watts area
Pacoima Federal Community CU	Pacoima	LA	Northeast San Fernando Valley

Appendix II: Methodology for CDFI Activities and Assets in the 10 Largest MSAs

Objective

The objective of this study is to determine the total CDFI assets and financing activity within each of the 10 most populous metropolitan statistical areas (MSAs) in the United States, and to compare the assets and loans outstanding with the number of individuals living in poverty⁴⁴ within each MSA.

Procedure

1. Identify the 10 most populous MSAs and the number of people in poverty living in those MSAs.
2. Identify CDFIs active in the CDFI Data Project (CDP) in those MSAs.
3. Identify CDFI assets and financing activity within each MSA.
4. Allocate national and regional CDFIs' assets and financing to the top 10 MSAs.
5. Arrive at MSA rankings in terms of CDFI assets and financing per individual in poverty.

44 The Census Bureau uses a set of Orshansky money-income thresholds that vary by family size and composition to determine who is in poverty. For example, the poverty threshold is \$9,645 for a one-person household, 12,334 for two people, and \$15,067 for three. Thresholds also vary according to householders over and under 65 years of age. If a family's total income is less than the family's threshold, then that family and every individual in it are considered in poverty. The official poverty thresholds do not vary geographically. The official poverty definition uses money income before taxes and does not include noncash benefits, such as public housing, Medicaid, and food stamps.

MSA Population and Poverty Data

The data source for the 10 largest MSAs and their populations is a census report that provides 2003 MSA populations⁴⁵ using 2003 MSA definitions.⁴⁶ The poverty data are for 2002, the most recent year available.⁴⁷ The definitions of MSAs changed in 2003, so we added the poverty totals in the counties according to the 2003 definitions for each of the 10 MSAs.

CDFI Activity

CDFI data in this study were obtained from the 2003 CDFI Data Project.⁴⁸ In cases where the CDFI has activity in more than one area, we also collected new data from the CDFI directly. CDFI data are valid for the individual CDFIs as of the end of their fiscal year 2003.

The CDP does not include exact locations of all financing activity but does tell us the state (or states) the CDFI lends in

45 U.S. Census Bureau, "Statistical Abstract of the United States, 125th Edition," 2004–2005, April 3, 2005 <<http://www.census.gov/statab/www/>> Path: Population.

46 U.S. Census Bureau, "Combined Statistical Areas and Component Core-Based Statistical Areas," December 2004.

47 U.S. Census Bureau, "Small Area Income and Poverty Estimates, County Estimates, 2002: 125th Edition," June 5, 2005 <<http://www.census.gov/hhes/www/saie/district.html>>.

48 The CDFI Data Project is an industry collaboration that produces data about CDFIs. The goal of the CDP is to ensure access to and use of data to improve practice in and attract resources to the CDFI field. The CDP is a collaboration of the Association for Enterprise Opportunity, Aspen Institute, Community Development Venture Capital Alliance, Corporation for Enterprise Development, Opportunity Finance Network, National Community Investment Fund, National Federation of Community Development Credit Unions, and their member CDFIs. For an analysis of the CDP data for 2003, see "Providing Capital, Building Communities, Creating Impact: CDFIs," available through Opportunity Finance Network at <<http://www.opportunityfinance.net>>.

and the geographic area served: neighborhood, city or town, county, metropolitan area, multicounty, state, multistate, national, or member-driven. We used this information to isolate CDFIs that had financing activity in the states where the top 10 MSAs are located. Then we divided the CDFIs into three groups:

- **Category I CDFIs** had activity exclusive to one of the 10 MSAs (109 total).
- **Category II CDFIs** had activity within one or more of the 10 MSAs but not exclusive to the MSAs of interest (34 unique CDFIs—many had activity in more than one MSA).
- **Category III CDFIs** had activity within the state but not within the MSA of interest.

We included all Category I CDFIs in and removed all Category III CDFIs from the study. The Category II CDFIs are either national or regional and lend in more than one MSA. To allocate their assets and financing activity, we used as a proxy the percentage of their 2003 loans originated within each MSA. We then applied that percentage to the CDFI's total assets and total financing outstanding to estimate the CDFI's assets and loans outstanding in the relevant MSA (or MSAs). We used that proxy because there is no readily available loan level data with precise addresses in the CDFI industry.

Opportunity Finance Network staff contacted the CDFIs in Category II, providing a list of counties for each relevant MSA and requesting the CDFI's 2003 loan originations within the MSA counties. We received 31 responses out of a total of 34 Category II CDFIs. We excluded the three CDFIs that did not respond. Those three CDFIs were relatively small.

Data Limitations

Opportunity Finance Network acknowledges the limitations of this study, which include but are not limited to the following:

- CDFIs included in the study were drawn from the 477 CDFIs in the 2003 CDP. There are about 800 active CDFIs in the United States. We are aware that CDFIs are active in many of the MSAs not in the data project. We are aware that this study contains only 17 out of 32 CDFIs active in Los Angeles. However, the CDP is the most comprehensive data set for CDFIs available.
- The data extrapolation technique used for CDFIs that do not lend exclusively within an MSA provides only a general idea of CDFI financing in the MSAs.
- Loan originations in any one area can vary a great deal from year to year. If any large national CDFI did an unusually large or small amount of lending in any one MSA in 2003, that skews the data.
- Precise geographic data were not always available, so based on available information, we assumed the activity of some CDFIs to be exclusive to one MSA, when in fact it may have been nonexclusive.
- The data do not include off-balance-sheet lending.

Methodology Notes for Category II CDFIs

- One Category II CDFI did not have a record of its 2003 loan originations within an MSA and instead provided its 2003 loans outstanding within the MSA. We used that figure to calculate the proxy, dividing 2003 loans outstanding by the CDFI's total loans outstanding to calculate a percentage for total assets and 2003 loans originations in the MSA.
- The CDP data for one Category II CDFI active in two of the top 10 MSAs were missing total 2003 loan originations in the CDP, so we could not calculate the proxy. The CDFI provided a percentage of its total financing in each MSA, and we used that to calculate assets and loans outstanding in each MSA.
- The CDP data for one Category II CDFI were missing the total loans outstanding and total assets data points, so it was not possible to calculate MSA-specific loans outstanding and MSA-specific assets. In this case we used the CDFIs' 2003 loan originations in an MSA to also represent dollars outstanding and assets in the MSA.
- The CDP excludes off-balance-sheet lending, as did the study; however, three Category II CDFIs reported loan originations in the MSA as higher than total loan originations. We assume that this indicates off-balance-sheet lending. In two cases we used the larger reported MSA figures, rather than CDP totals, and 100% as the percentage of activity in the MSA. In the third case we excluded a CDFI in the Philadelphia MSA as its off-balance-sheet lending was the majority of its loans outstanding.
- It is often difficult to collect geographic details of credit union loans. In one case the credit union estimated the percentage of its members within the MSA counties for us, and we used that percentage to calculate MSA-specific 2003 loan originations, loans outstanding, and assets, from the CDP data.
- For one bank that made loans exclusive to two MSAs, the CDP was missing 2003 originations, so we could not calculate the proxy. We asked the bank for a current figure of loans outstanding in each MSA, calculated the percentage of financing for each MSA, and applied the percentage to calculate assets and 2003 loan originations in each MSA.

Methodology Notes for Category I CDFIs

- Four Category I credit unions did not provide 2003 originations. To estimate this amount, we used the same technique that we used for the banks not reporting originations, but we used only Category I credit unions in the study to calculate an average percentage of 2003 originations/outstanding. This percentage was 61.4%.
- Eight Category I community banks had not reported total 2003 originations to the CDP. To estimate 2003 originations for those banks, we used the other CDFI banks in the study to calculate the average percentage of CDFI banks' 2003 originations/outstanding. Seven Category I and II CDFI banks were used to reach this

average. Several other banks were excluded from this estimation due to 2003 originations greater than outstanding, as reported in the CDP. We found the average percentage of 2003 loan originations to financing outstanding to be 50.4%.

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