

**5483M4: ACCESSING CAPITAL FOR COMMUNITY DEVELOPMENT**

**Format:** Seminar – 2 Units  
**Time:** Fourth Period Module  
Thursday -- 9:00 to 12:00 noon  
First Class – March 13, 2003  
**Instructor:** William Apgar  
Joint Center for Housing Studies  
1033 Massachusetts Avenue, Room 510

**Course Description:** This module will examine how for-profit and not-for-profit entities access debt and equity funding for affordable housing development and job creation activities in distressed urban and rural communities. First, the course will assess the rapidly changing world of real estate and economic development finance. The course will then examine the operation of the mortgage-backed securities (MBS) market, and the growth and development of secondary markets. Particular emphasis will be placed on recent efforts to securitize debt linked to the construction and sale of affordable housing, as well as small business lending. Next, the course will review current efforts to attract equity capital for affordable housing and community economic development, including the low-income housing tax credit and new markets tax credit programs, as well as emerging venture capital funds and philanthropic initiatives. Finally, the class will review several case studies of efforts by both private and not-for-profit groups to structure community development initiatives that take full advantage of these newly emerging sources of capital.

**Pedagogic Objectives:** Course lectures and class discussion, along with course readings and case study material will enhance student understanding of capital markets and the operation of both traditional and newly emerging capital market institutions. Students will learn how to assist both for-private and not-for-profit organizations to better access debt and equity funding to promote affordable housing and community development. There are no prerequisites for this course, but familiarity with basic concepts of real estate finance will prove helpful.

**Class Sessions:** Class will meet once a week from 9 am to 12:00 starting on March 13. The first half of each class will consist of a lecture and discussion concerning key concepts raised by the class readings. Following a short break, the class discussion will focus on applying these concepts to specific housing and community development cases. The case material will also serve as the basis for the required written assignments.

**DEPARTMENT OF URBAN PLANNING AND DESIGN      SPRING 2003**  
**GRADUATE SCHOOL OF DESIGN**

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**Time Commitment of Students:** Students are expected come to class prepared to discuss course reading and case material. In addition, students will be asked to select two (out of four) sets of case materials and complete a short memo that addresses one or more of the critical issues raised by these cases. The first written assignment will be due in class as follows:

- April 3:**            Establishing a secondary market for Hong Kong
- April 10:**        Establishing a Revolving Loan Fund for Small Business
- April 17:**        Transforming CDFIs
- April 24:**        Establishing a Venture Capital Fund for New Business  
Development
- May 1:**            Non-Traditional Approaches to Venture Capital

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|------------------------------|------------------------------------|------|
| <b>Basis of Final Grade:</b> | 1 <sup>st</sup> Written Assignment | 33%  |
|                              | 2 <sup>nd</sup> Written Assignment | 33%  |
|                              | Class Participation                | 34%  |
|                              | Total                              | 100% |

**Course Materials:** Most class readings are available on line. Two text books and selected other readings will be available at the GSD Loeb Library. In addition, several Harvard Business School case studies as well as selected case material will be distributed in class.

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**March 13: Financing Housing and Community Development**

The opening session will present an overview of the institutional structure and operation of capital markets and examine capital market imperfections and the financing gaps that result from these imperfections. In addition, this first class will briefly survey the various models and existing resources – including federal resources -- that exist to address capital gaps and stimulate private investment to expand access to affordable housing and to promote community economic development.

**Study Questions:**

1. What issues do individuals and firms consider when making an investment?
2. According to Ryan and Andrews there are many socially motivated entities that require capital to expand their operations. What are the market failures that limit the flow of capital (both debt and equity) to these ventures and what are some ways to structure financial instruments to support these capital needs?

**Required Readings:**

David Geltner and Norman G. Miller, Commercial Real Estate Analysis and Investments, Chapter 7: “Real Estate as an Investment” also skim Chapter 16: “Mortgage Basics I: An Introduction and Overview.” **Loeb Reserve**

William B. Brueggeman and Jeffrey D. Fisher, Real Estate Finance and Investments, 10<sup>th</sup> Edition, Chapter 17, “Institutional Sources of Real Estate Capital.” Read pp. 558-565, skim rest of chapter. **Loeb Reserve**

Julia Sass Rubin, “Community Development Venture Capital: A Double-Bottom Line Approach” **Available at [www.chicagofed.org/cedric/2001/Rubin.pdf](http://www.chicagofed.org/cedric/2001/Rubin.pdf)**.

William P. Ryan, “Non Profit Capital: A Review of Problems and Strategies,” a paper prepared for the Rockefeller Foundation and the Fannie Mae Foundation, 2001. Please review the entire document but read carefully the “Executive Summary and Introduction,” pp 1-3, and “Strategy # 4,” pages 26 to 37.

**Available at [www.rockfound.org/documents/453/npcapital.pdf](http://www.rockfound.org/documents/453/npcapital.pdf)**

**Optional Reading:**

William B. Brueggeman and Jeffery D. Fisher, Real Estate Finance and Investments, 10<sup>th</sup> Edition, Chapter 6, “Underwriting and Financing Residential Properties.” **Loeb Reserve**

Julia Ann Parzen and Michael Kieshnick, Credit Where It’s Due: Development Banking for Communities, Philadelphia: Temple University Press, 1992, Ch. 1, “Introduction,” and Chapter 2, “Capital Market Failures.” **Loeb Reserve**

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**March 20: The Secondary Market and Mortgage-Backed Securities**

The second class will begin with a brief review of basic economics of mortgage finance discuss of the evolution of the secondary market and the major organizations – including the Government Sponsored Enterprises – that have led the growth of secondary market activities. In addition, the class will discuss various types of mortgage-backed securities that have evolved in recent years, and provide a framework for analyzing their investment characteristics. The class will continue on with a case discussion of issues relating to the creation of a secondary market operation in Hong Kong.

**Study Questions:**

1. What are the preconditions required for developing an MBS market? Was the Hong Kong Mortgage Corporation (HKMC) venture into MBS products a timely one?
2. Do you think it was a good opportunity for banks to partner with HKMC in development of MBS? What were the risks involved? Do you think the benefits would outweigh the costs?

**Required Readings:**

Brueggeman and Fisher, Real Estate Finance and Investments, 10<sup>th</sup> Edition, Chapter 18, “The Secondary Mortgage Market: Pass Through Securities,” and Chapter 19, “The Secondary Mortgage Market: CMOs and Derivative Securities.” **Loeb Reserve**

Leon T. Kendall and Michael J. Fishman, A Primer on Securitization, (Cambridge: MIT Press, 1998) Chapter 1, “Securitization: A New Era in American Finance,” and Chapter 2, “Securitization’s Role in Housing Finance,” pp. 17 to 29. **Loeb Reserve**

“Securitisation in Hong Kong and Asia,” Harvard Business School Case HKU169, November 9, 2001. **Course Case Packet.**

**Optional Readings:**

Geltner and Miller, Chapter 19, “Commercial Mortgage Economics and Investment”, and Chapter 20, “Introduction to Mortgage-Backed Securities.” **Loeb Reserve**

Frank J. Fabozzi and Franco Modigliani, Capital Markets: Institutions and Instruments, 2<sup>nd</sup> Edition, Chapter 26, “The Market for Collateralized Mortgage Obligations,” and Chapter 27, “The Market for Asset-Backed Securities.” **Loeb Reserve**

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**April 3: Expanding Access to Capital for Low-Income Homeownership**

The class will begin by examining recent trends in the mortgage lending to low- and moderate-income households, particular attention to the Community Reinvestment Act (CRA). This session will discuss recent trends in low-income lending in light of the changing structure of the banking and mortgage industries. In particular, the class will focus on efforts to securitize pools of high risk home purchase and refinance loans both by for-profit and not-for-profit entities. These issues will be discussed in terms of the situation facing the Neighborhood Housing Services Corporation of Chicago and its efforts to provide affordable loans to low-income borrowers in distressed inner city areas.

**Study Questions:**

1. What have been the key changes in the structure of the banking and mortgage banking industries and how have these changes altered the ability of lower-income borrowers to access capital for home purchase and refinance?
2. Advances in technology and the growth of the MBS and ABS markets have fostered the rise of subprime lending. How can these financial innovations be deployed to promote lending by community non-profits and other socially motivated entities?

**Required Readings:**

William C. Apgar and Mark Duda, "The 25<sup>th</sup> Anniversary of the, Community Reinvestment Act: Past Accomplishments and Future Regulatory Challenges," Federal Reserve Bank of New York, Economic Policy Review, 2002. Available at [www.jchs.harvard.edu/publications/govprograms/cra02-3\\_apgar.pdf](http://www.jchs.harvard.edu/publications/govprograms/cra02-3_apgar.pdf)

Gregory M. Stanton and Jed Emerson, "Going Mainstream: NPOs Accessing the Capital Markets: Exploring the Use of Traditional Financing Methods, Processes and Debt Instruments for Expanding the Capital Structure of Nonprofit Community and Economic Development Organizations," February 2001. Available at [www.redf.org/download/other/cmap\\_going.doc](http://www.redf.org/download/other/cmap_going.doc)

"Seeking Sustainability: Neighborhood Housing Services of Chicago Faces Financial Challenges," KSG Case C16-02-1658.0, August, 2002." **Course Case Packet**

**Optional Reading:**

Robert Weissbourd, "Banking on Technology: Expanding Financial Markets and Economic Opportunity," a Brookings Institution Paper, June 2002. Available at [www.brookings.edu/es/urban/publications/weissbourdoppexsum.htm](http://www.brookings.edu/es/urban/publications/weissbourdoppexsum.htm)

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**April 10: Financing Small Business Development**

Many small businesses face considerable difficulty in securing needed startup and working capital. This class will assess the potential market failures and the role of government in small business finance. In particular, the class will look at various programs designed to fund “micro-business,” as well as other initiatives – including programs of the Economic Development Administration, the Small Business Administration. A series of case studies will provide examples highlighting the advantages and disadvantages of these alternative approaches.

**Study Questions:**

1. What are the market failures that justify government intervention in the market for small business lending?
2. What do you perceive to be the major obstacles that limit the effectiveness of revolving loan funds to expand capital resources for economic development? What have been some of the most promising approaches?

**Suggested Readings:**

Nancy O. Andrews, “Equity with a Twist: The Changing Capital Needs of the Community Development Field,” in Capital Xchange. **Available at [www.brookings.edu/dybdocroot/es/urban/capitalxchange/andrews.pdf](http://www.brookings.edu/dybdocroot/es/urban/capitalxchange/andrews.pdf)**

Kelly Robinson “Expanding Capital Resources for Economic Development: An RLF Demonstration, 2001.” Focus your attention on Executive Summary and Chapters 1, 2, 4, and 5, and the case study of the Community Reinvestment Fund on pages 65 to 70. **Available at [www.osec.doc.gov/eda/pdf/1g3\\_17\\_capresources.pdf](http://www.osec.doc.gov/eda/pdf/1g3_17_capresources.pdf)**

Timothy Bates, “Government as Venture Capital Catalyst: Pitfalls and Promising Approaches,” in Economic Development Quarterly, Vol. 16, No. 1, February, 2002), pp 49-59. **Available at Proquest -- an e-Resource of the Harvard Library System. Go to Proquest and enter author’s name.**

**Optional Readings:**

Kelly Robinson, “Revolving Loan Funds,” Chapter 9 in Sammis White, et al, Financing Economic Development, (Newbury Park, CA: Sage: 2003)

Timothy Bates, “Use of Bank Credit to Finance Small Businesses,” Chapter 15 in Sammis White, et al, Financing Economic Development, (Newbury Park, CA: Sage: 2003).

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**April 17: CDFIs – From Community Banks to Global Markets**

Community development lending has increased dramatically over the past 20 years, with much of that growth attributed to the rise of Community Development Financial Institutions (CDFIs.) When CDFIs started, securitization was in its infancy, now it accounts for trillions of dollars of transactions. This class will assess issues relating to efforts by the CDFI industry to enhance their technological sophistication and to enhance scale economies to achieve greater conformity with – and greater access to – conventional capital market structures.

**Study Questions:**

1. Despite their steady growth over the years, Moy and Okagaki argue that CDFIs risk losing ground in the community development arena to mainstream financial organizations. Do you agree and if so why?
2. Looking forward, how best can CDFIs link the highly specialized capital needs of economically distressed markets, with the increasing focus on national and international capital markets on high volume and standardization?

**Required Readings:**

Kirsten Moy and Alan Okagaki, “Changing Capital Markets and Their Implications for Community Development Finance,” July 2001. **Available at**  
**[www.brookings.edu/dybdocroot/es/urban/capitalxchange/moy.pdf](http://www.brookings.edu/dybdocroot/es/urban/capitalxchange/moy.pdf)**

Mark Pinsky, “Taking Stock: CDFI’s Look Ahead After 25 Years of Community Development Finance,” December 2001. **Available at**  
**[www.brookings.edu/dybdocroot/es/urban/capitalxchange/pinsky.pdf](http://www.brookings.edu/dybdocroot/es/urban/capitalxchange/pinsky.pdf)**

Daniel M. Leibson, “Expanding Resources for Community Development,” a presentation to the Financial Innovations Roundtable (FINIR). **Available at**  
**[www.finir.org/expand\\_cap/ec\\_home.htm](http://www.finir.org/expand_cap/ec_home.htm)**

**Optional Readings:**

Kirsten Moy, “Technology, CDFIs and Community Development Finance,” a presentation to the Financial Innovations Roundtable (FINIR). **Available at**  
**[www.finir.org/technology/tech\\_home.htm](http://www.finir.org/technology/tech_home.htm)**

Jeremy Nowak, “Civic Lesson: How CDFIs Can Apply Market Realities to Poverty Alleviation,” March, 2001. **Available at**  
**[www.brookings.edu/dybdocroot/es/urban/capitalxchange/nowak.pdf](http://www.brookings.edu/dybdocroot/es/urban/capitalxchange/nowak.pdf)**

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**April 24: Venture Capital and Equity Investment**

This class focuses on a recent and increasingly important source of economic development funding – venture capital and equity-like investments. Today, these are common sources of funding to support technology based businesses or businesses with innovative product offerings. In addition, these approaches are finding their way into various forms of social investing. Using selected case examples, the class will examine the unique nature of these financing sources, as well as alternatives including direct equity investment and convertible debt.

**Study Questions:**

1. How has Northeast Ventures sought to blend community development with the traditional venture capital model? What alternative structures could or should they consider adopting?
2. Will institutional investors become a major source of capital for community development venture capitalists? Will the federal or state governments? What will be the implications if either of these become a more important capital source?

**Suggested Readings:**

Bob Zidor, “How Venture Capital Works,” in Harvard Business Review, November-December, 1998, pp. 131-139. **Available from Proquest**

Thomas Hellman, “A Note on Valuation of Venture Capital Deals,” Harvard Business School Case 9-296-093, March 2001. **Course Case Packet**

Eric K. Jackson, “Northeast Ventures: January 1996,” Harvard Business School Case 9-296-093, November 15, 1997. **Course Case Packet**

David E. Arnstein, “Venture Capital,” Chapter 17 in Sammis White, et al, Financing Economic Development, (Newbury Park, CA: Sage: 2003). **Loeb Library**

**Optional Reading:**

Adam J. Bock, “Business Angels,” Chapter 16 in Sammis White, et al, Financing Economic Development, (Newbury Park, CA: Sage: 2003). **Loeb Library**

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**May 1: Non-Traditional Venture Capital Funds**

While many venture capital funds focus on high technology businesses located in the more prosperous portions of larger urban centers, this class will focus on the operations of a new breed of innovative venture capital funds – including socially motivated philanthropic ventures -- that seek to promote investments in low-income communities, and in non-high tech business enterprises. A series of case studies will examine alternative organizational strategies, investment experience and future prospects for these “non-traditional venture capital funds.”

**Study Questions:**

1. What are the main differences between venture capital funds operating in rural areas from “more traditional funds?” What are the common features?
2. Jed Emerson suggests a new and expanded role for foundations in providing access to capital in low-income areas. Using the Roberts Enterprise Development Fund as a case in point, what is your assessment of Emerson’s argument?

**Suggested Readings:**

David L. Barkley and others, Establishing Nontraditional Venture Capital Institutions: Lessoned Learned, a report prepared for the Rural Equity Capital Initiative Study of the Rural Policy Research Institute, 2001. **Available at [www.rupri.org/pubs/equitycap/index.html](http://www.rupri.org/pubs/equitycap/index.html).**

David L. Barkley and others, Public Involvement in Venture Capital Funds: Lessons from Three Program Alternatives, report prepared for the Rural Equity Capital Initiative Study of the Rural Policy Research Institute, 2001. **Available at [www.rupri.org/pubs/equitycap/index.html](http://www.rupri.org/pubs/equitycap/index.html).**

Jed Emerson, “The Roberts Enterprise Development Fund: A Case Study on Venture Philanthropy,” 1999. **Available at [www.redf.org](http://www.redf.org)**

**Optional Readings:**

David L. Barkley and others, Case Studies, a report prepared for the Rural Equity Capital Initiative Study of the Rural Policy Research Institute, 2001. **Available at [www.rupri.org/pubs/equitycap/index.html](http://www.rupri.org/pubs/equitycap/index.html).**

J. Gregory Dees, “Enterprising Non-Profits,” in Harvard Business Review on Nonprofits, **Loeb Library**