Unlocking Community Investment with Strategic Grantmaking

center for community investment

AN INTRODUCTION

Community investment may attract newcomers with the allure of scale, but its forbidding tangle of experts, jargon, and competing approaches can also put them off. Grantmakers drawn by the opportunity to make a long-term, sustainable difference in affordable housing, local business development, green infrastructure, and other sectors essential to thriving communities may wish to collaborate with community investment professionals but find the prospect daunting. They need to learn a new set of terms and players–capital stack and LIHTC, underwriters and CDFIs–and develop a new understanding of what success looks like. Many hesitate at the edge of community investment, trying to understand the terrain and identify a path forward.

Whether we call it community investing or impact investing, the idea that loans are the way to fund large-scale community projects is so widespread as to be practically a given. But there is another powerful way to support community investment: grants, which we generally think of when we want to fund programs, but which can also play a critical role in investment. Grants can strategically unlock investment capital for community projects–and they are an accessible first step for newcomers, especially those in philanthropy, healthcare, and other fields who are already familiar with how grants work.

> "Supporting [impact-oriented] business models can be accomplished by combining impact investment funds, which seek both financial and social return, with flexible grant funds, which seek a social return but do not require a financial return. Coordinated grants may not only decrease the risk of transactions but also prepare and support socially driven financing models, thereby enabling impact investment opportunities that might otherwise not be possible."
>
> Amy Chung, "From Grants to Groundbreaking: Unlocking Impact Investments"

HOW CAN GRANTS PLAY A ROLE IN COMMUNITY INVESTMENT – AND MOVE COMMUNITY INVESTMENT SYSTEMS TOWARD RACIAL EQUITY?

Grants–financial contributions that do not need to be repaid–are generally seen as a way to meet immediate needs: support a food bank, fund a scholarship, provide transit passes or childcare subsidies. However, they can also be used to prepare the ground for a much larger flow of resources.

Grants for community investment projects, like supermarkets, childcare facilities, affordable housing, and small businesses, can have that long-term impact. They can also be used strategically to make those community investment projects possible, both by laying the groundwork for investment and by unlocking investment capital.

As importantly, grant funds can be a significant intervention in our current financing and investment system, which was shaped by structural racism to channel resources to communities that already have them and further disinvest communities that don't. This means that the people in this country who have access to financing are largely those who already have wealth, assets, and relationships to power and money–and those people are largely white. Meanwhile, the financial system's practices of exclusion have left residents of communities of color that have not received its benefits alienated, frustrated and distrustful of political and economic systems and outside interventions.

When grants lay the physical and financial groundwork for inclusive community investment projects, they benefit the Black, Latinx, Native, Asian American and Pacific Islander, immigrant, and low-income residents who live in those communities. When we target our grant funds to community investment projects steered by people who don't already have financial and relationship capital, we help them build that capital. When we use grant funds as levers to bake inclusion into the community investment system, our money is doing powerful equity work.

So what can grants for community investment look like in practice?

Preparing for Investment

There are many steps before a project or organization reaches the point where it is ready for investment. The activities detailed below are crucial to preparing for financing. Grant funding can make them happen.

> "... philanthropic grants and government subsidies are in short supply, while the need is growing. Making the best use of every grant dollar is particularly important. Aligned grants can be critical to unlocking impact investment capital, thereby stretching the dollars going into the communities and issues we care about."
>
> Chung, "From Grants to Groundbreaking"

Market studies assess demand, examine area demographics and trends, and review comparable businesses or transactions to determine project viability, laying the data groundwork for attracting investment. **Inventories of vacant and underutilized properties** reveal where land is available for construction, along with what it will take to access or acquire that land. Grants can pay for the consultants who conduct market studies and inventories.

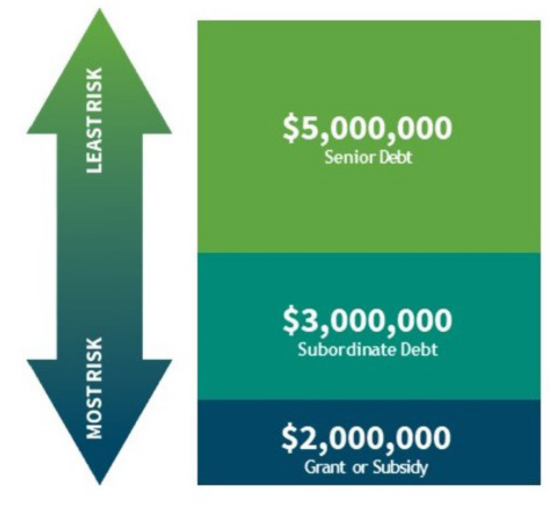
> *A collaborative housing initiative that was entering a new neighborhood in a Midwestern city used a grant to fund a market study to identify the most cost-effective approach to building new homes for community members with low incomes who were threatened by displacement as the city's home prices surged.*
>
> *The results of the inventory are enabling the team to facilitate a pipeline of projects that can be funded together, rather than just working on one project at a time, which will be more financially efficient and will more rapidly increase the supply of homes for Black residents seeking to settle permanently in the neighborhood and build their assets.*

Small business development efforts and organizational capacity building require entrepreneurs and organizations to create **business plans** to attract investors. These documents detail how the business or nonprofit plans to grow and its capital needs. Grants can fund consultants, courses, or dedicated staff members to support the development of these plans.

An immigrant entrepreneur with a promising idea for a new restaurant needed capital to fit out a rented space and begin operations. A grant that paid for a professional business plan helped convince a local fund that the business was a good bet for the modest investment needed to get going.

Grants also can fund many critical tasks during the **predevelopment** phase of a project before construction starts. These may include surveys, appraisals, cost estimates, zoning and permit fees, architectural drawings, and more.

Grants for predevelopment enabled a local anchor institution in a mid-sized city to lay the groundwork for developing 50 units of new affordable housing. Staff used the grant funds to secure sites, which included acquiring lots from private owners and the local land bank and covering legal costs. During this predevelopment period, their active collaboration with the local land bank enabled them to build relationships not only with that organization but with the city. As a result, when city funding suddenly became available, the anchor institution got a grant that it used to move forward with development on the lots they had already acquired.



A capital stack is a structure that layers together capital from investors with different risk and return expectations to finance a particular project or group of projects. From "All In Data for Community Health: Using Investment to Drive Improved Outcomes." Center for Community Investment. September 2018.

Securing Investments and Unlocking Capital

The predevelopment grant described above is also an example of how grants can unlock investment funds. This can happen in several ways.

Grant funds can provide **risk reduction** for investors who require reassurance that their loan will be repaid in order to feel sufficiently confident to lend. Grants can be used for credit enhancement in the form of loss reserves or equity. By providing a grant that sits at the bottom of a capital stack and does not need to be repaid, a grantmaker decreases the overall repayment risk for the other participants. This credit enhancement can reassure impact investors and more financially oriented investors who might not lend if they viewed the repayment risk as too high.

A foundation agreed to make a grant of $2 million to be used as a loss reserve for a $10 million revolving affordable housing predevelopment fund that would have been considered too risky by the lenders without the cushion of the grant.

Grant funds can also be used to **reduce the cost of borrowing** for communities. A grant can lower the amount that needs to be repaid from project cashflow and make a project feasible.

With interest rates rising, the expected rental income from an affordable housing project was not going to suffice to pay for a mortgage loan for 80% of the value of the building. A foundation made a grant to the project that reduced the size of the mortgage loan, making the monthly payments feasible.

Grants can provide **gap financing** that allows projects whose upfront costs are higher than their committed funding (the gap) to proceed.

A Black-owned nonprofit developer was ready to proceed with the construction of a small, multifamily affordable housing project. Due to inflation and supply chain difficulties, the anticipated cost of construction rose by more than 10% versus original estimates, meaning that the financing sources that had been assembled for the deal were no longer enough. A foundation stepped in with a grant to close the gap, and construction could proceed.

SUPPORTING BORROWER FLEXIBILITY

Grants can also provide the flexibility to experiment, increase a project's social impact, or both.

A social entrepreneur wanted to renovate an abandoned factory to provide commercial space for community small businesses. Some of the prospective tenants were relatively new and did not yet have significant income streams. However, they were owned by Latinx and Asian American community residents and had the potential to make a significant difference to the community. A grant from an anchor institution allowed the entrepreneur to borrow less, which in turn enabled them to create an innovative rent schedule based on tenants' projected annual income. This opened the building up to a wider range of potential tenants, especially tenants from the community.

WHO BENEFITS FROM GRANTS FOR COMMUNITY INVESTMENT?

When a Black developer receives a $1 million grant that helps them unlock a $25 million capital stack...

When 150 units of affordable housing for the elderly are constructed in a neighborhood of recent Chinese immigrants...

When a Dominican immigrant who owns three affordable rental units gets credit enhancement to purchase another building...

When an immigrant uses a small business grant as a loss reserve to get a loan to expand their business...

When a foundation shifts its grantmaking to focus on supporting inclusive community investment...

...we are using our grants to build an investment system that advances racial equity for individuals and communities.

About the Center for Community Investment

The Center for Community Investment at the Lincoln Institute of Land Policy works to ensure that all communities, especially those that have suffered from structural racism and policies that have left them economically and socially isolated, can unlock the capital they need to thrive. Our work is supported by the Robert Wood Johnson Foundation, the Kresge Foundation, and JPMorgan Chase & Co, and The California Endowment.

For more resources, visit centerforcommunityinvestment.org/resources.

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