

**Community Development Venture  
Capital and the Future of  
Community Development Finance**

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**Community Development  
Financial Institutions**

- Loan funds
- Banks
- Credit unions
- Venture capital funds

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**Community Development  
Venture Capital**

- Equity and near-equity capital investments in businesses for:
  - targeted economic growth
  - poverty reduction
  - the strengthening of disadvantaged communities

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### Community Development Venture Capital

- Double bottom line
  - social returns
    - jobs & healthy communities
  - financial returns
    - profits for fund's investors

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### Why is CDVC Needed?

- Access to patient capital critical for economic vitality
- Conventional venture capital concentrated
  - industry
  - size of investments
  - geography
- Rural and distressed urban geographies particularly underserved

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### Rural and Distressed Urban Geographies

- Higher operating costs for venture capitalists
  - greater difficulty and travel time to reach portfolio companies
  - entrepreneurs unwilling to give up ownership
  - lack
    - developed investment infrastructure
    - entrepreneur support networks
    - entrepreneurial culture
    - understanding of how venture capital works

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### Methodology

- Research conducted 1998 to 2007
- Case studies of 52 self-identified CDVC funds
  - interviews with fund managers
  - analysis of capital sources and investments
  - review of documents detailing fund operations
- Interviews with stakeholders
  - community development finance practitioners
  - foundation and bank officers
  - policy makers

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### Three Waves of Evolution

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### First Wave (1969 - 1980)

- 8 funds
  - primarily Community Development Corporation and Community Action Agencies
  - funded by Federal grants
- Investments
  - targeted small, primarily rural geographies
  - small investment sizes
  - all industries & development stages
  - intensive technical assistance
  - focus on job creation
    - Kentucky Highlands Investment Corporation

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### Second Wave (1980 - 2000)

- 28 funds
  - significant growth and experimentation
  - new sources of investment capital
    - foundations (21%)
    - federal government (32%)
      - CDFI Fund
    - banks (34%)
      - Community Reinvestment Act regulatory changes
  - creation of trade association
    - Community Development Venture Capital Alliance

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### Organizational Models

- State-Sponsored Funds
  - West Virginia Jobs Investment Trust, Small Enterprise Growth Fund
- Near-Equity Funds
  - Cascadia, Community Loan Fund of SW PA
- Quasi-Traditional Venture Funds
  - Coastal Ventures I LP, Sustainable Jobs Fund

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### Third Wave (2001 - present)

- 17 funds
  - growth in average capitalizations
    - \$19.6 vs. \$6.3 million
  - for-profit, limited life structures
  - larger geographies

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### Capitalization

- Federal Government ( 33%)
  - New Markets Venture Capital & Rural Business Investment Company programs
    - matching investment & grant capital
    - signal of quality to private investors
- Banks (26%)
- Foundations (12%)
- Other (29%)
  - pension funds (8.5%)
  - funds of funds (4.4%)
  - wealthy individuals (2.4%)

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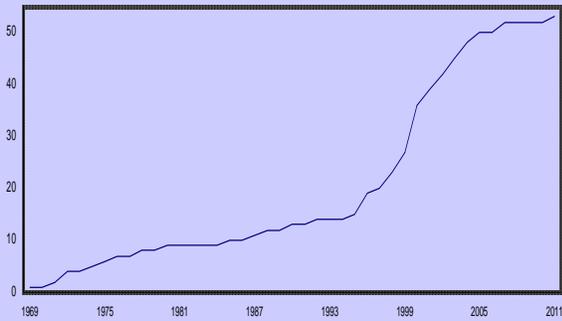
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### Cumulative Number of CDVC Funds

(By Year of First Investment)



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### Venture Capital

- High risk
- Long investment horizon
  - potentially longer for CDVC
- Vulnerable to bad timing

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### Economic Challenges

- Stock market collapse of 2001
  - hurt returns for all venture capital
    - discouraged investors
  - shrank foundation assets
- Stock market collapse of 2008
  - coincided with 3<sup>rd</sup> wave CDVC exits

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### Political Challenges

- CDVC focus on rural & distressed geographies
  - dependent on subsidy
- George W. Bush Administration
  - dramatically reduced CDFI Fund appropriations
  - weakened enforcement of Community Reinvestment Act
  - eliminated funding for the NMVC and RBIC programs

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### Financial Performance

- Lack of industry-level data
- High-profile failures
  - Cascadia, Northeast Ventures, Urban Growth Partners
- Stereotyping

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### Vague Boundaries

- Diverse organizational models
  - equity vs. near-equity
  - small vs. large geographies
  - broad vs. narrow industry focus
  - early stage vs. later stage

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### Vague Boundaries

- Multiple social objectives
  - absolute job creation
  - job quality
  - entrepreneur racial & gender diversity
  - socially-beneficial products
- Diverse social impact measures
- Nuanced results

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### Investments (2001-2007)

ZIP CODES	RURAL (RUCA codes)	POVERTY LEVEL (mean)	HOUSEHOLD INCOME (median)
CVC 100	1	9.7%	
CVC 500	1.2	10.2%	\$61,963
CDVC	1.8	15.0%	\$40,025
TOTAL US		12.4%	\$41,994

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### Competition

- Minority-focused venture funds
  - record of profitability
  - banks receive CRA credit
- Small Business Investment Companies
  - banks receive CRA credit
- Conventional venture funds
  - socially-beneficial products
  - good marketing

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### Lessons for CDFIs

- Subsidy unstable
- Funders/investors not double-bottom line
  - value social **or** financial impact
- Nuanced social impact less effective
- CDFI competition profit-driven
- Greenwashing works
- Invest in marketing

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Thank you!

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