The Center for Community Development Investments

The community development investment field has grown increasingly complex in recent years. While still significantly influenced by CRA-motivated depository institutions, the field is now populated by a wide array of investors, including banks, insurance companies, pension funds, foundations, religious institutions, investment intermediaries, and individuals. Coupled with an increasing range of investment vehicles, this crowding has prompted a need for better research and collaboration to inform the fast-paced evolution of the industry.

To address this need, the Center for Community Development Investments (the Center) was created to seek out new ideas that have the potential to further expand investment in low-income communities. The Center disseminates information through its website and two publications: the *Community Development Investment Review* (the *Review)* and an ongoing working paper series. The Center also propels the industry forward by bringing together community development finance experts at conferences, roundtables, and online. These forums provide platforms for innovation.

One such innovation recently advanced by the Center is the expansion of the secondary market to include community development loans. A widely used financial tool, the secondary market refers to the sale of loans—which have typically been converted into securities—to third party investors. By converting illiquid assets such as mortgages, credit card payments, and municipal bonds into liquid, tradable securities, investors can now tailor their investments to fit a particular appetite for risk and return. If properly applied, this approach has the potential to radically improve the community development landscape. Community development loan originators—such as community development financial institutions (CDFIs)—could offer more affordable and flexible products if they were free to sell their loans to third party investors. Significant strides have been made in recent years to make these loan sales a reality. The Community Reinvestment Fund (CRF), for example, is testing a beta version of an electronic marketplace to trade such loans. As a result of these and other significant efforts, CRF has made efficient community development loan trading a genuine possibility. Nevertheless, the recent sub-prime mortgage crisis has depressed demand for asset-backed securities; it may be some time before the mainstream finance industry can be persuaded to invest in “exotic” community development securities.

The Center is also encouraging innovation in rural community venture capital. Rural areas have been underserved by investors for a host of reasons; distance from supply lines, a lack of technology-based opportunities, and limited human capital conspire to isolate rural communities from global capital markets. To explore solutions to this problem, the Center recently invited policy makers, venture capitalists, academics, and community organizations to participate in a conference at the Federal Reserve Board in Washington, DC. Many valuable themes came out of the conference; among them, a recognition that more must be done to attract venture capitalists to small rural towns. Most venture capital dollars flow through Silicon Valley or Boston’s “Route 128” because these locations offer numerous clustered investment opportunities. Rural communities will never achieve this level of concentrated deal flow, but they can do a much better job of utilizing existing technologies, such as the internet, to counteract their geographic disadvantage. The Center will continue to work with both rural entrepreneurs and venture capitalists to help match investment dollars with promising rural business opportunities.

To facilitate further innovation, the Center is also developing a social networking platform to bring leaders in the community development finance community together online. In addition to this networking component, the online platform will have decision-making tools such as an information market and a dynamic poll that will allow its participants to work collectively towards solving challenging community development problems. This peer collaboration could lead, for example, to industry-wide agreement on standardizing community development loan documents and other underwriting procedures, collecting data on performance, and structuring transactions.

Despite these and other innovations in the field, capital needs remain. Two interrelated problems—the absence of reliable loan data and an inability to accurately assess risk—continue to restrict growth in the field. Accordingly, the Center is actively encouraging loan data collection and identifying promising new approaches to risk assessment. In the most recent issue of the *Review*, data collection experts highlighted the improvements that have been made in recent years to measurement processes and tools. Community development loans are increasingly being monitored and risk patterns have begun to emerge. In light of the subprime mortgage crisis, capturing these patterns will be a crucial step towards making community development investments more attractive to traditional investors. While much work remains, the Center will continue to find ways to lower data collection costs, increase access to capital markets, broaden the appetite for community investments, and develop innovative ways to encourage industry-wide collaboration.

Please visit the Center for Community Development Investments website at: http://www.frbsf.org/cdinvestments for more information and to subscribe to the Center’s publications.