FEDERAL RESERVE BANK
OF SAN FRANCISCO

Community Investments Vol 16, Issue 1
The Next Stage in Childcare Facilities Development

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May 2004

> One of the charges of the district Fed banks is to provide analysis and insight into regional economic development. State and local governments have been debating how to best use public funds to encourage economic growth, and research has shown that early childhood development programs should be viewed as economic development.

- Minneapolis Fed Vice President James Lyon at The Economics of Early Childhood Development: Lessons for Economic Policy conference, October 20, 2003 hosted by the Minneapolis Fed and Minnesota's McKnight Foundation in cooperation with the University of Minnesota[1]

What's At Stake?

The socioeconomic impact of inadequate child care, in terms of lost potential to promote healthy growth and development, cannot be underestimated. According to the Chicago Longtitudinal Study (2000),[2] quantitative savings

in terms of crime, welfare dependency, and special education will result in a return of more than $7 for every $1 invested in quality early-intervention child care. The study calculated a potential savings of $2.6 billion for every 100,000 children participating in the programs.

Limited Supply

Lack of facilities is probably the greatest challenge facing early childhood programs. In California, the supply of licensed child care, estimated at nearly 900,000 spaces in more than 40,000 child care businesses, meets only 22 percent of spaces needed.[3] The child care needs of the estimated 2.3 million California children in poverty are particularly acute with more than 200,000 low-income children on waiting lists for subsidized child care. The alarming shortage of affordable, high-quality child care is a significant barrier to families aiming for economic self-sufficiency. Child care is frequently financially out of reach for low-income families, and there simply are not enough child care spaces to meet the demand for children of any income. The problem is not prevalent just in California, but nationwide.

The need for a stable and efficient source of capital to finance the development of child care facilities across the nation is critical. Without sufficient funding for high-quality facilities, low-income families are forced either to refrain from working in order to care for their children, or place their children in unlicensed and perhaps unsafe child care environments. Ultimately, the critical need and value of child care spaces, particularly for low-income families, is clear, as is the necessity for a well-developed financing system to support the continued development of high-quality child care facilities throughout the nation. Seeking to address this shortage, the David and Lucile Packard Foundation, and its partners, launched the Affordable Buildings for Children's Development (ABCD) initiative in 2002.

Addressing the Need

The overarching goal of the ABCD initiative is to build a comprehensive and

sustainable financing system for high-quality child care facility development with the objective of creating 15,000 spaces in five years with a particular focus on low-income communities. The initiative adopts a four-pronged approach of finance, technical assistance, construction advice and advocacy to achieve this goal. The Low Income Investment Fund (LIIF), a community development financial institution, was chosen to assume leadership of the initiative in 2003 (see box 1).

The ABCD initiative adapts a proven model drawn from the affordable housing financing system of using private capital to leverage public funds. Even in good economic times, it is doubtful that the public sector could sufficiently supply the capital investment to support construction of the number of child care facilities required. As such, ways must be found to attract and sustain new sources of private investments, including loans. The ABCD initiative operates from the hypothesis that increased involvement of private capital will expand public dollars and increase the commitment of lenders and investors who have historically been involved in other areas of community development such as housing and small business. As the financial industry increases their commitment, their overall support and interest in children and child care will become not simply philanthropy but "good business." In other words, just as private investors have joined government funders for today's affordable housing initiatives, the private sector will come to value the investment potential in child care facilities development through ABCD.

Since its inception in January 2003, ABCD has made solid progress, including:

- committing approximately $4 million in grants and loans that will support development of nearly 1,800 child care spaces;
- raising $10 million from a consortium of insurance companies for the ABCD Fund, through the New Markets Tax Credit program; and

- receiving a $3 million grant over three years from the First 5 California Commission for ABCD Constructing Connections (see box 2).

Getting Involved

In order for the ABCD Initiative to be successful, LIIF will require the participation of financial institutions in the following ways:

1. lending the ABCD Fund, low cost, flexible capital to be used to make child care center loans;
2. providing grants to LIIF for re-granting to child care centers for planning facility projects; and
3. providing grants to LIIF for the operations of the ABCD Fund.

The ABCD Fund is currently capitalized at $10 million with an additional $10 million currently being closed with a consortium of insurance companies. LIIF's goal is to grow the Fund to between $30 and $40 million in capital available for lending.

Because traditional financial institutions do not typically have experience in making loans for the development of child care centers, LIIF can play a critical role in serving as the intermediary between the financial institutions that have the capital to lend and the borrowers developing child care centers. In most instances, the borrowers are first time borrowers, unfamiliar with the loan underwriting process. Over the years, LIIF has developed an expertise in lending for the purpose of child care center facilities development and by lending to LIIF --an established CDFI with a strong track record-- rather than to individual child care center, financial institutions can take advantage of this experience and expertise.

Additionally, such characteristics as often being unsecured, having high loan-to-value ratios when secured by real estate, lower than typical debt service coverage ratios, and cash flow that is dependent on annual appropriations of

child care subsidies tend to make them weaker than usual borrowers from a financial perspective. By lending to LIIF, many of these risks can be mitigated because of LIIF's expertise in lending to this field.

The ABCD Initiative as a Model for Other States

The ABCD initiative is most concerned with putting into place key elements that will ensure a sustainable system for child care facility financing and serve as the underpinning of affordable child care facilities development for years to come. These elements include:

- enlisting new and diverse partners such as employers, health care providers, and housing owners to provide support such as sites or other resources;
- working to ensure that investors see childcare center financing as an attractive community development opportunity;
- mobilizing substantial new public and private dollars for facility development and organizational support of the child care sector; and,
- increasing financing options for childcare providers.

The four components of the ABCD Initiative summarized in Box 2 are an attempt to address the elements that are believed to be critical to the system building that we have identified as being necessary for accomplishing the overall goals of the ABCD Initiative.

Box 1

Who is LIIF?

Since its inception in 1984, LIIF has provided capital and technical assistance totaling over $353 million in 35 states across the nation to hundreds of community organizations serving the nation's hardest-to-reach populations. LIIF's assistance, in turn, has leveraged investments in poor communities of more than $3.2 billion.

LIIF, which operates nationally, has developed expertise in lending to borrowers with unconventional revenue streams and provides financing for all phases of a development project (including permanent mortgages), as well as operating lines of credit for nonprofit organizations. A prominent board of directors, drawn nationally from the banking industry and the national housing development and policy fields, governs LIIF.

To learn more about LIIF's role in facilitating community development finance and investments, visit their website at www.liif.org

Box 2

The Four Components of the ABCD Initiative

Experience has shown that it takes more than just funding to accomplish these goals. That is why the ABCD Initiative utilizes the expertise and capacity of existing community organizations while employing four interrelated strategies:

ABCD Fund – Provides technical assistance, grants and loans for child care centers, feasibility planning, acquisition, and construction costs, and long-term real estate financing needs.

ABCD Development Assistance – Utilizes the expertise of regional community developers to increase statewide the construction of child care facilities within educational, health, and housing facilities. Partners include Bridge Housing, Los Angeles Community Design Center (LACDC), Mercy Housing California and Child Development, Inc. (CDI).

ABCD Constructing Connections – Strengthens the facilities development expertise of child care center operators and intermediaries, and improves

the regulatory and funding environment to support child care facilities as a priority.

ABCD Campaign to Sustain Child Care – Brings together new coalitions of representatives of a variety of sectors to advocate for increased child care program operating subsidies from state and local governments.

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[1]Link to proceedings from the The Economics of Early Childhood Development: Lessons for Economic Policy conference. (http://www.mcknight.org/cfc/news_detail.aspx?itemID=355&catID=55&typeID=2)

[2]The Chicago Longitudinal Study (CLS), a report completed by the University of Wisconsin and published in August of 2000, investigates the educational and social development of 1,539 low-income children who grew up in high-poverty areas in Chicago. (http://www.waisman.wisc.edu/cls/index.html)

[3]Child Care Portfolio, 2001; a bi-annual report analyzing the supply and demand for child care by county in the state of California created by the California Child Care Resource and Referral Network. (http://www.rrnetwork.org/rrnet/index.htm)

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