center for community investment

Deals as System Events

AN INTRODUCTION TO DEAL REVIEW

When we review deals as system events, we can see what our systems need. When we create catalytic deals as system events, we can move our systems forward. Both of these activities can help shift community investment practice from a focus on what can be financed to what is important, from a transactional approach to a systems approach, from single projects to pipelines of projects, from projects that fill gaps to ambitious and scaled initiatives, from reductionist and siloed systems to integrative and adaptive systems. The result is more and better deals that ultimately support stronger and healthier communities.

Deals are the building blocks of community investment. Investable deals enable communities to accomplish their priorities: build homes affordable for people with low and moderate incomes, open supermarkets in food deserts, extend public transportation to underserved areas, create green spaces, and bring jobs to communities with high unemployment. But deals do not take place in a vacuum. Deals are the outputs produced by the way the community investment system functions. The conditions of the local community investment system can make deals easier or more difficult, which in turn affects the community's progress toward its priorities. Deals, in turn, can provide a lens for identifying improvements to the community investment system that will facilitate more and better deals to help communities achieve those priorities. **Deal review** is what we call this process of looking at deals as system events. Below, we explain why and how to do it.

A FEW KEY DEFINITIONS:

1. **Community investment:** investments intended to improve social, economic, and environmental conditions in disinvested communities with some economic return for investors (which can be recycled into additional investments to help create self-sustaining systems)

2. **Community investment system:** the set of actors, policies, practices, resource flows, platforms, and relationships that enable or constrain community investment activity in a given locale

3. **Deal:** an investment transaction or project that blends different sources of capital and in community investment aims to generate financial and social return
   - **Investable deal:** a deal that has a source of funds to repay the capital invested in it, typically with a return (e.g., a loan to build rental units, whose rent will provide funds for repayment)

4. **Impact investor:** an investor who wishes to create positive social or environmental impacts while also generating financial returns

COMMUNITY INVESTMENT DEALS: WHERE MISSION AND FINANCE MEET

Deals are how community investment accomplishes community priorities. One of the smartest investments we can make in our nation's future is to help all communities unlock the capital they need to thrive. For our society to prosper, we need to ensure that we all have the chance to live in places that promote health, provide opportunity, and allow each of us to reach our highest potential.

But in communities that have withstood decades of disinvestment, community investment deals can be challenging. Traditional investors focused on financial gain may be leery of investments that are designed first and foremost to meet community needs. Too often, this means the capital that flows into these communities finances projects designed to achieve returns without meaningful consideration of resident priorities; such deals can heighten gentrification and displacement pressures. Fortunately, community investments can access capital from a range of sources–such as public funding, philanthropic grants, and impact investors, which can include banks, insurance companies, philanthropies, individuals, and others–that are committed to social and environmental as well as financial returns.

Because community investment is designed to do the hard things conventional markets don't do, even as it uses many of the same tools as conventional finance, individual deals tend to be complex. Blending different funding sources and their particular constraints, along with different actors and their particular desires, means that structuring the details of deals can be arduous and discouraging. Well-constructed deals can move community priorities forward. However, if we do one deal at a time without shifting the system to make it easier to successfully structure deals for maximum community impact and lowest financial risk, we are unlikely to achieve those priorities.

ADVANCING COMMUNITY INVESTMENT SYSTEMS TO ACHIEVE COMMUNITY PRIORITIES

Deals do not exist in isolation. Rather, they are products of a system that stakeholders can influence so that it is more amenable to addressing community priorities and operating at a scale that can achieve those priorities. What we call the **enabling environment**, the context in which community investment deals are developed and executed, includes everything in a local community investment system–actors, policies, resource flows, relationships, skills, behaviors, etc.–that accelerates or impedes its deals. **That environment not only shapes our deals but can be shaped by our deals.**[1]

If we think about deals **systemically**, we can use them not only to organize financing and accomplish specific goals, but also as windows into and levers for strengthening our community investment systems so that we can achieve big picture success. In other words, we can use deals themselves to create a system that is able to generate more and better deals.

A first step toward creating better community investment systems is to review deals as system events. We can look back at past deals to examine how the local system functions and find ways we might strengthen it. We can look at deals in progress to identify pinch points and obstacles that changes to the system might overcome. We can also look forward and design new deals so that they both accomplish specific goals and advance the entire system.

[1] For more details, see Shaping the Enabling Environment: An Introduction at https://centerforcommunityinvestment.org/resource/shaping-enabling-environment-introduction

CONDUCTING A DEAL REVIEW

Conventional financial analysis examines the likelihood that a deal will produce profit. Community investors are certainly interested in financial return, especially as it facilitates financial sustainability, but they are equally interested in social and environmental impact. As a result, many more factors go into creating a successful community investment deal–not just the money, but all the elements of the enabling environment–which can make it hard to focus on the underlying system. Asking the right questions about a deal or set of deals can provide a lens for examining how your community investment system works.

In Focus: Land Acquisition

In a particularly hot real estate market, developers of affordable housing consistently found that they were unable to obtain financing quickly enough to compete with market-rate developers for land. By identifying this pattern, local stakeholders were able to come up with a solution–identifying owners of public land willing to prioritize affordable housing–which resulted in a new approach to land acquisition that significantly advanced the pace of development.

A deal review considers every deal as an instance of the system functioning. Reviewing a deal can show how the system functioned, what worked well, and what didn't. It can generate data that allows stakeholders to recognize patterns and brainstorm what they can do to improve the system. A deal review might reveal that the system is too small to achieve the community's priorities and suggest possibilities for expansion. It might show where the system is dysfunctional and highlight opportunities for change. When a deal review reveals what's working, it can point the way to elements of the system that could be amplified or replicated. Ultimately, deal review helps us make choices about how to shift our enabling environment–by taking actions such as enacting new policies, creating new funding streams, or engaging new stakeholders–and approach our next deals. Those choices can lead, in the short and long term, to a more effective community investment system, more and better deals, and a community that can achieve its priorities.

Who should lead a deal review?

Anybody who wants the system to function better. It could be the mayor, a community foundation, a CDFI that wants to play a larger role in making things happen in the community, a bank that wants to see different kinds of deals, or someone who sees a community priority that current investments are not addressing.

When do you review deals?

One way that communities can approach strengthening their community investment system is to get in the habit of doing an "after action review" [2] when a deal is completed. Participants in the deal, as well as other stakeholders in the community, can gather to examine what can be learned from the recently completed deal and what can be done in the future to make similar deals easier or deepen their impact. A regular opportunity to discuss deals helps participants see patterns and overcome barriers that slow or limit achievement of the community's priorities. "Before action reviews" are another option, providing a way to improve deals at the outset so they can have more impact and/or be designed to shift the community investment system. Reviewing deals in process can help stakeholders find immediate and systemic solutions to challenges as they occur.

[2] For more on the concept of after action reviews and their role in emergent learning, see Learning in the Thick of It by Marilyn Darling, Charles Parry, and Joseph Moore at hbr.org/2005/07/learning-in-the-thick-of-it or consult 4qpartners.com.

What deals should be reviewed?

Any deal that reveals the workings of the community investment system. It may be a deal that people feel is typical, a recent deal whose details are fresh in people's memory, a deal that went particularly well, or even a problematic deal from which there may be something to learn. It could also be a current deal that is stuck in some way or even a deal that is still in the planning stages. Ask people who participate in deals to suggest the ones that will be most instructive. Better yet, pick two or three and compare.

How do you review a deal?

1. Gather the Data
   - Who participated in the deal?
     - Who used the capital?
     - What were the sources of the capital?
     - Whose approval was required for the deal to proceed?
     - Who were the intermediaries?
   - What were the sources and uses of capital?
   - What policies and programs affected the deal?

2. Analyze the Data
   - Was this the first time these players worked together, or do they always work together?
   - What were the deal's key milestones and when did they occur?
   - What was tough and what were the challenges? What worked well?
   - What do we see in this deal that would help us if we could do more of it?
   - Is there anything innovative or exemplary about this deal?
   - Did this deal accomplish anything new?
   - What actions within the realm of possibility would have made the deal easier?

What can deal review teach us about a system?

- The stakeholders who are involved–and those who are not
- The sources of funding that are tapped–and where there are gaps
- The current boundaries of the system–and where it might be expanded
- What relationships exist–or would help if they did
- Where there are gaps in capacity or skills–and how they might be filled
- How long things take–and what could speed them up
- Where things get stuck–and how they might be unstuck
- How much progress is being made compared to the scale of the problem

This process can also be used to review a pipeline or portfolio of deals.

THE IMPACT OF DEAL REVIEW

Here are some examples of issues that deal review has enabled communities to identify and address–and in so doing facilitate more deals, advance systems, and move community priorities:

1. **Timing:** Public officials in a Midwest city discovered that their schedule of dates to apply for and award tax credits regularly caused developers to miss the construction season, lengthening the period they needed to hold land before development could be completed. By changing the calendar, they reduced holding costs, improving the feasibility and affordability of multi-family housing units and making it possible for additional developers to participate in deals.

2. **Chokepoints:** A group of stakeholders working on transit-oriented development in an urban region with a highly collaborative ecosystem realized that the predevelopment pool they had created was failing to revolve as intended, with funds "getting stuck" rather than being taken out by permanent financing for projects. The stakeholders created a regular forum where developers could present projects at an early stage to sources of both predevelopment and permanent financing, allowing issues to be raised and resolved before projects got too far along.

3. **Gaps:** An underwriter working on a deal in an older industrial city that included apartments with ground-floor retail discerned that the low rents prevalent at the time would be insufficient to service a standard 10-year loan. When stakeholders engaged in a postmortem discussion of the deal, they agreed to create a pool of capital with a 15-year term, unlocking a pipeline of eight deals that were then able to get financed successfully.

USING DEALS TO CATALYZE SYSTEM CHANGE

Once we better understand a system, we can build on its strengths and address its weaknesses. There are many ways to improve a community investment system: by influencing and implementing policies and regulations, identifying and aligning resources and funding flows, ensuring the availability of needed skills and capacities, fostering formal and informal relationships, building forums and platforms for ongoing collaboration, and generating and providing data.

We can also use deals to change the system itself. If a community investment system is non-existent, a deal can help jumpstart it. If the system is troubled or poised for growth, a deal can lay the groundwork for system evolution. Catalytic deals are designed not only to achieve specific social or environmental goals but also to spark change in the system. We can create catalytic deals by prioritizing deals already in the pipeline for their catalytic potential, intentionally adding catalytic elements to deals in the pipeline, or specifically putting together new deals that can help move the system forward.

In Focus: Credit Enhancement

A Community Development Corporation tried for years without success to attract a grocery store to its neighborhood. It finally entered negotiations with a store operator, only to find that the deal could not attract the necessary financing. The CDC decided to structure a loan with unusually favorable terms that allowed the new store to open and succeed. That deal demonstrated how credit enhancement for new grocery operators reduced financial risk enough to result in healthier options in food deserts. Three deals modeled on this transaction were then completed in the region.

Catalytic deals may:

- bring new actors into the system
- bring new types of resources into the system
- involve existing stakeholders in new roles (as when a health system that has previously only made grants becomes an investor or a local government agency not only provides subsidy but leases ground-floor office space)
- create durable new relationships among stakeholders
- effect breakthroughs in the system (for instance, a new level of scale, new type of product, or new location that was not previously considered feasible)

Although catalytic deals can be challenging because they involve a shift away from business as usual, they pave the way for the community investment system to function more effectively in addressing community priorities.

In Focus: Aggregating Capital

Since 2008, Nationwide Children's Hospital (NCH) in Columbus, Ohio has used grants from its community benefits budget to support the renovation of owner-occupied single-family homes near its campus. In 2018, NCH agreed to step into a new role in the community investment system by guaranteeing a portion of a $15 million fund being created by a CDFI partner, Ohio Capital Finance Corporation, for the acquisition, construction, and permanent financing of up to 170 units of single and multifamily rental housing. The South Side Renaissance Fund was catalytic in multiple ways:

- By including rental as well as owner-occupied units, the fund was able to finance homes for residents with a wider range of incomes.
- By structuring a guarantee from NCH, the fund was able to reduce risk and attract new financial investors.
- By creating a capital stack with multiple types of investors, the fund achieved a level of scale that will accelerate the pace of affordable housing development in the community.

For more on this story, see Accelerating Investments for Healthy Communities: Nationwide Children's Hospital.

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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