Analyzing, Building, and Executing a Pipeline

THE CAPITAL ABSORPTION FRAMEWORK: PART 2

INTRODUCTION

Communities across the country need similar things to thrive: access to good jobs, affordable homes, safe places to gather and play, healthy food options, and opportunities for residents to have a voice in decisions that affect the community. Research shows that outcomes like life expectancy and economic mobility are deeply influenced by where we live. Yet many places suffer from chronic disinvestment, resulting in communities where the most basic conditions necessary for a decent quality of life are not met.

Disinvestment has its roots in structural racism and intentional policies and practices that have left some communities economically and socially isolated– disconnected from opportunity. Systematic practices like redlining, in which racial composition and other factors were used by public and private actors to designate places as not fit for investment, were major contributors to the problem. Such policies and practices have impacts that reverberate even today. Many formerly redlined communities are places where poverty is concentrated and vulnerability to forces such as climate change is especially acute. Community efforts to transform such places are made that much harder because conventional financial investments often take the path of least resistance, flowing most readily to places that are already thriving.

The well-being of our communities is tied to how we invest in them. 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 everyone has the chance to reach our highest potential. This is the goal of community investment.

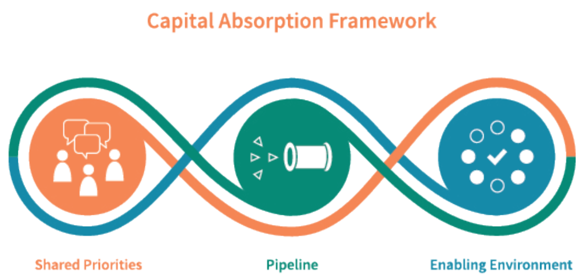
We define community investment as transactions designed to improve social, economic, and environmental conditions in communities that lack adequate investment, while producing an economic return.

Community investment is critical to creating and preserving affordable homes, promoting health and wellness, growing businesses, and fueling economic vitality. We use community investment as an umbrella term for a large spectrum of transaction types–including loans, bonds, tax credits, structured investment vehicles, and more–that draw on public funding, philanthropic grants and investments, and capital from banks and insurance companies, individuals, and other impact investors.

The goals of community investment differ from those of traditional financial investment and so its approaches differ too. Traditional financial investments seek to maximize the return on investors' money, with any resulting public good being purely incidental. Community investment seeks to serve the public good and may result in varying degrees of financial return.

Community investment attempts what the conventional finance system cannot or will not do, directing resources to people and places that would otherwise be left out. It does so by putting together out-of-the-box deals that are often complex, time-consuming, and politically sensitive, and that require participants to balance the interests of many stakeholders and blend different sources of capital with varied constraints and requirements. Practitioners often speak about their work in metaphors like filling gaps (where markets aren't working), providing cushions (to absorb risk that others won't bear), and taking haircuts (to adjust prices to "market" rates). These metaphors suggest the high level of expertise and the values required to complete these deals.

Since 2011, the founders of the Center for Community Investment have been testing and refining a framework for better organizing and deploying community investment. Called the **capital absorption framework**, it approaches community investment as a system.



We believe that working at the level of the community investment system–looking broadly not only at who is involved but also who could be involved, creating opportunities for continuous learning and improvement, pooling resources and batching deals to create efficiencies–can help reduce transaction costs, increase the scale and impact of investment, and assist local leaders to better understand and strengthen their local community investment system. It can also help to engineer a context that is more supportive of achieving community priorities.

Although many community investment efforts focus on increasing the supply of capital, we believe that this alone is not enough. Equally critical is a more coordinated, strategic approach to **organizing the demand for capital**. This belief arises from our experience with impact investors who want to invest in a certain place but can't find investable projects, sometimes because there aren't any deals in progress, other times due to a lack of clearly articulated community priorities that could guide the creation of such projects. We developed the capital absorption framework to help make communities investment ready, that is, capable of receiving and effectively using community investment.

Instead of focusing on individual transactions or particular subsets of community investment practitioners, the capital absorption framework casts a much wider net, reframing all investment activity designed to advance the public good–the deals, the players, the resources–as part of a larger community investment system.

The idea of investment-ready communities is critical to the capital absorption framework. Anyone active in community investment knows that the aspirations of communities cannot be achieved by any single project or by grant funding alone. The scale of problems like a lack of affordable homes, health disparities across racial and economic lines, and unequal access to economic opportunities is such that communities need to use not just government subsidies or foundation grants, i.e. funding that does not expect to be repaid, but also the much larger pools of capital available from banks, anchor institutions, pension funds, motivated individuals and other impact investors that expect some form of repayment and/or economic return.

In order to attract the broadest range of resources and be ready for unexpected opportunities, communities must have in place a shared understanding of their goals, a set of deals and projects that will help achieve those goals, and the policies, practices, and relationships that can make those deals and projects happen in ways that advance community interests and protect community assets. This is what it means for a community to be investment ready.

The capital absorption framework centers on these three core functions: establishing shared priorities, creating a pipeline of investable projects, and strengthening the enabling environment of policies and practices required to achieve the desired results. The functions are highly interdependent, with each function evolving in response to new information and progress throughout the course of the work. The framework is meant to be applied iteratively, as effectively implementing the capital absorption framework hinges on aligning the three functions so they are mutually supportive.

In this brief–the second of three in a series on the core functions of the capital absorption framework–we examine in more detail what it means to establish a pipeline of investable deals and projects, and why it is an important precondition to an efficient, effective community investment system. Our goal is to share what we have learned to date about surfacing and executing a pipeline, provide examples of the capital absorption framework in practice, and offer guidelines for tailoring the framework to an individual community's unique needs and objectives.

WHAT IS A PIPELINE OF DEALS AND WHY IS IT IMPORTANT?

Community investment deals tend to be complicated and time consuming, so community investment practitioners often focus on only one project at a time. Yet successfully addressing pervasive problems like affordable housing shortages, lack of access to economic opportunity, and health inequities requires investment at a larger scale.

To unlock opportunity at a scale that cannot be reached through one-off projects, CCI's capital absorption framework focuses on creating a set of deals and projects that can synergistically advance a community towards achieving its shared priorities. This set of deals and projects is what we call *the pipeline*.

Thinking about investment opportunities in terms of a pipeline of projects serves two distinct yet complementary purposes. First, working on a pipeline of deals, as opposed to working on one deal at a time, moves a community more efficiently, quickly, and successfully toward the achievement of its shared priorities. Second, analyzing a community's pipeline provides crucial data and impetus for improving its enabling environment.

By working on a pipeline of deals, a community can:

1. See all potential opportunities.

Community investment practitioners generally see only those deals in which they themselves participate, and so may be unaware of other developing deals that seek to achieve similar goals in the same community. This lack of awareness can lead to missed opportunities to leverage parallel efforts to achieve a community's strategic priorities or take advantage of the potential for multiple benefits along the way. For example, an investment in complete streets may require the installation of new sidewalks in a neighborhood that is also slated for new road infrastructure to improve drainage. Sharing information about these planned investments and coordinating efforts can reduce the cost and disruption of the work. Surfacing a community's pipeline can also facilitate partnerships, encourage resource sharing, and create momentum by providing the opportunity to sequence transactions most sensibly.

2. Ensure deals address shared priorities.

Looking at a community's pipeline of deals allows stakeholders to see whether the deals being executed align with a community's shared priorities and concentrate money and attention on the highest priority deals. For example, a community might have a shared priority targeting several new transit stops for development, but only one or two stops may have deals underway. Another community may be focusing on housing affordability across incomes while only producing housing for 80-100% of area median income. Reviewing the focus and location of existing transactions can help spot gaps and focus current and planned investments on shared priorities.

3. Reduce costs and increase efficiencies.

When focusing exclusively on individual deals, there is a tendency to want every project to offer every possible feature. While this is an understandable desire, it increases costs and can overcomplicate a project. By placing the deal in the larger context of other deals that advance the same shared priorities, features can be distributed among projects to reduce costs, increase efficiencies, and better utilize resources. Surfacing the pipeline can also identify ways to aggregate and advance deals as a batch, reducing transaction costs and potentially speeding the progress of deals through the system.

4. Identify where the system is stuck.

By identifying projects in progress and analyzing them as a group, stakeholders can assess which deals are moving forward—or not—and why. For example, there may be patterns in delays, such as an inefficient permitting process, that have gone unnoticed but become apparent when studying the deals together. Analyzing a pipeline of deals can surface chokepoints and allow stakeholders to address the policies and practices that may cause delays.

5. Expand the community investment system.

Analyzing deals in progress is an excellent way to see who is engaged, and who may be missing from a community investment system as it is currently constituted. By looking at the participants in current transactions, stakeholders may be able to identify and engage potential investors, intermediaries, or other actors who could play a larger or more constructive role in achieving the community's shared priorities.

Focusing on a pipeline of deals represents two shifts in how we practice community investment. The first three items in the list above show how a community that has identified its shared priorities can organize a set of deals that together have the potential to make meaningful progress toward achieving those priorities. The last two items on the list show how deals can be used to build a stronger community investment system. In the sections that follow, we focus primarily on the first shift; for a closer look at the second, see our brief *Strengthening the Enabling Environment*.

Case Study: Pipeline in Coachella Valley, California

In 2018, CCI launched **Connect Capital**, an initiative that assists communities to attract and deploy capital at scale to improve residents' health and increase their access to opportunity. Six teams were competitively selected to receive customized coaching, facilitated peer learning, and a two-year grant to fund a local staff position dedicated to advancing the team's work.

In Coachella Valley, California, the Connect Capital team is using the capital absorption framework to help address the region's massive shortage of affordable housing. The team began its work by examining the region's need for affordable housing and trying to understand its pipeline by assessing how many additional units were being produced each year. Looking at the gap between the growing need and the rate of development suggested that a new approach was required.

The team then asked how it might intervene to expand the capacity of the community investment system. Team members began engaging other stakeholders, including a range of for-profit and non-profit housing developers that had completed deals in Coachella Valley but had been inactive in the area in recent years, as well as those that were currently active in the region and might consider doing even more. They also reached out to various public agencies to inquire about unused or underutilized parcels of public land that might be available for development.

When they turned to identifying their pipeline, that is, putting together a list of deals in progress, the team was surprised to see more housing-related activities and opportunities in Coachella Valley than they initially believed. If they batched these potential deals, they would be more likely to attract the interest of Los Angeles banks and community development financial institutions (CDFIs), whose potential interest in the region had previously had been deterred by the prospect of driving long distances for a single transaction. They also noticed that affordable housing was frequently being sited in locations without good access to quality jobs, nutritious food, and other building blocks of good health and economic stability. In response, the team is strategizing how best to engage actors in higher-opportunity communities to increase the availability of affordable housing in their areas, including exploring the possibility of mixed-use developments.

By identifying their pipeline of active housing deals and opportunities for new projects and making that information accessible to all relevant parties, the team has increased the likelihood that they will achieve their shared priority. At the same time, the pipeline analysis is serving as a tool for engaging a wider range of stakeholders and identifying new resources that will improve the local community investment system as a whole.

Ultimately, the pipeline approach asks us to move away from a model of scarcity, in which individual deals compete for a fixed pool of resources, toward a collaborative model, in which we share our resources in order not only to maximize them but to generate more resources, more deals, and better outcomes for the short and long-term.

To look at community investment in the terms of the old folk tale, Stone Soup: with a pipeline, "You have a carrot, I have a potato, and together we have soup."

WHAT DOES A GOOD PIPELINE LOOK LIKE?

A good pipeline is characterized by sufficiency, efficiency, and impact. What do each of these attributes look like in practice?

1. A **sufficient** pipeline has enough deals to address the community's shared priority, and those deals match the priority's focus sector, geography, and scale. If the shared priority relates to small businesses and most deals in the pipeline are focused on affordable housing, then the pipeline is insufficient. If the pipeline's deals are not in the targeted neighborhood(s), they are not a good fit for the pipeline. Given that not all deals will reach completion, there need to be enough transactions in the pipeline to ensure that the desired impact can be achieved.

2. In an **efficient** pipeline, deals progress smoothly and quickly. An efficient pipeline requires a supportive enabling environment. This means that stakeholders have identified and addressed obstacles and chokepoints, like high transaction costs, incompatible application deadlines, or prerequisites for funding that can't be properly sequenced.

3. When a pipeline has **impact**, its deals achieve the shared priorities they are designed to address, which, in our experience, they usually do. A pipeline with impact reflects the community's voice and commitment to achieving its shared priority.

These are ideal attributes, of course, and pipelines are works in progress. As deals are surfaced, moved forward, and completed, stakeholders should intentionally consider what lessons have been learned, what adjustments might be made in future deals, and how the pipeline needs to evolve in response to market conditions, changing community needs, and new opportunities. All stages of work on the pipeline should inform—and be informed by—the community's ongoing work on shared priorities and enabling environment.

ANALYZING, BUILDING, AND EXECUTING A PIPELINE

Work on pipeline in the capital absorption context occurs in three ways: identifying and analyzing existing deals in the pipeline, expanding the pipeline by generating new deals, and executing the pipeline more effectively by prioritizing and batching. As with the other functions in the capital absorption framework, the challenges posed by the pipeline vary according to an individual community's constraints and opportunities. Recognizing that different communities come to the work from different places, these steps are not sequential, nor will every community engage in all aspects of each step.

Identify and analyze the deals already underway

Understanding the pipeline starts by taking a snapshot to figure out what deals and activities are already underway. It is rare that deal information, especially for active projects, is publicly available in a central place, so identifying the existing pipeline will require talking to people about their current and potential deals in order to create a more complete picture of what is happening, where, and to what end. There is no need to gather reams of detailed data on each project or ask stakeholders to divulge confidential information. Rather, you simply need enough information to gain a baseline sense of what's in motion.

Based on our experience, it is helpful to gather four key data points on each deal:

1. **Type:** What is it? Mixed-used development? Multi-family rental housing? Refinancing of expiring subsidized housing? Focus on deals that match the community's stated priorities.

2. **Scope:** How big is the project? If it's housing, how many units? If it's commercial space, how many square feet will be developed?

3. **Stage:** Is the project still just an idea, or is it two weeks away from completion? For a real estate transaction, is there site control? Has financing been secured?

4. **Location:** If you can't get an address, a general location is sufficient.

Once you have gathered the deal data, take a step back and assess how much activity is already going on, and its relevance to the community's shared priorities. Having a group doing this analysis, rather than an individual, can help prompt a deeper discussion about investment activity and the community investment system in your community.

Analyzing the aggregated data is useful in three ways.

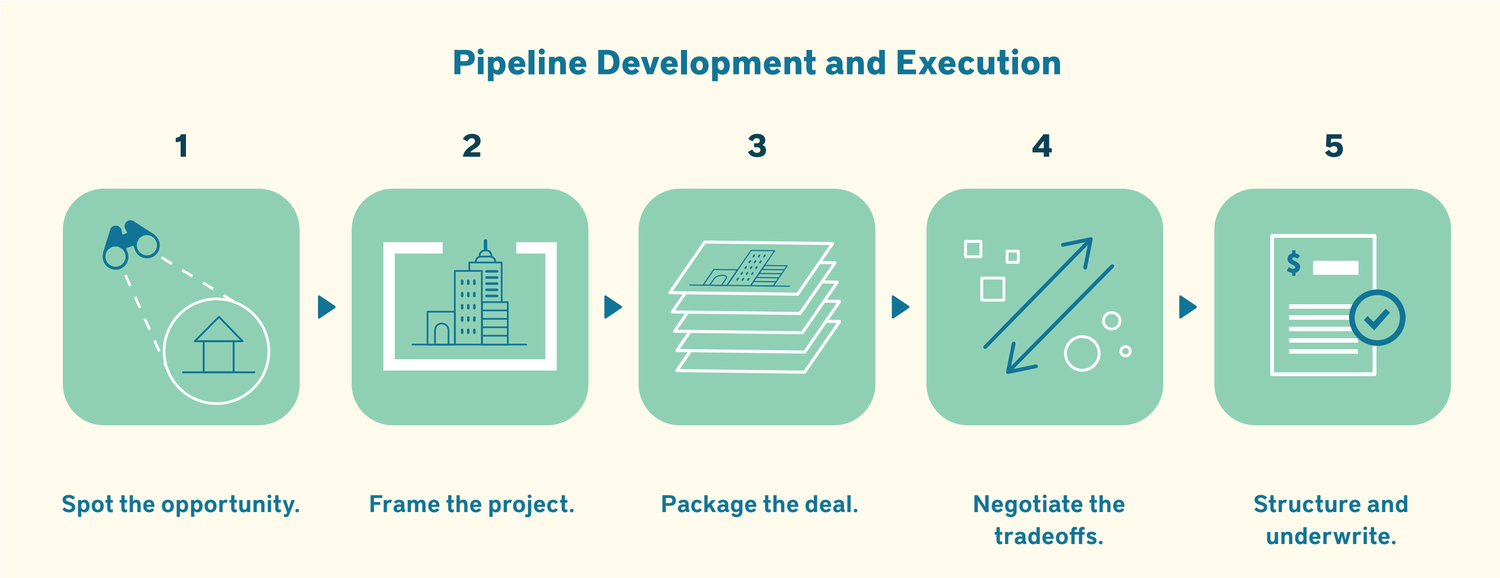
1. **First**, it enables you to spot gaps in current investment activity, which helps inform the work necessary to expand the pipeline.

2. **Second**, it can highlight opportunities to enhance the execution of the pipeline by prioritizing deals that contribute the most to achieving community priorities and batching deals that can best be executed as a group.

3. **Third**, it can highlight chokepoints: recurring problems in the enabling environment that prevent the smooth, efficient progress of community investment deals to completion. The first and second points are discussed in the next two sections; for more detail on the third, see our brief *Strengthening the Enabling Environment*.

Questions to ask about a pipeline include:

- Is there more or less activity than you expected?
- What seems to be working well?
- Where are the challenges?
- Where are you seeing common trends in project type, location, etc.?
- Are there common actors? Conversely, are there investors you expected to see that are not involved?
- Are investments stuck in similar places?
- What data is missing?



Expand the pipeline by generating deals

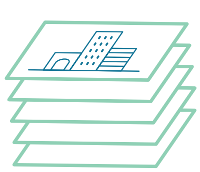
Many communities do not have enough existing deals in their pipelines to achieve their shared priorities. Existing deals may not match those priorities, or there simply may not be enough deals in progress. In these cases, expanding the pipeline to generate new deals and projects becomes a critical need and requires the following steps:

1. Spot the opportunity

All deals start with an idea. Someone has to take the initiative to identify how an unmet community need could be addressed through an investment. For example, if the need is for mixed-use development near transit, someone needs to identify a vacant or underutilized parcel near a targeted station and think it would be a great place for housing, a grocery store, the new library, or whatever else the community might be looking for. One way to encourage this sort of "opportunity spotting" is to organize an inventory of possible sites in the targeted area that are owned by the city, county, school district, a land bank, or any other entity that might have land that could be used for public purpose. Such an inventory can be the basis for conversations with developers, community groups, and other stakeholders who may have ideas for how to use the land to help realize the shared priorities. A similar process can help identify local businesses in need of capital or other targets for investment.

2. Frame the project

Once an opportunity has been spotted, the next step is to frame the project, to determine the most appropriate and feasible use of that resource in the context of the shared priorities. If, for example, you've identified a piece of vacant land, and your priority is to increase the availability of affordable housing, you may want to ask whether the land would be better used for a 30-story apartment building or an 8-unit multifamily project. Those two deals would have different impacts on the community and would require vastly different resources. Framing projects appropriately–sizing the effort and determining the best mix of features to include–is critical both to getting deals done and to ensuring they achieve their intended impacts. Deciding how to frame a project will often involve a formal process of community engagement to solicit the opinions of the stakeholders most affected by it.



3. Package the deal

After a deal has been framed, multiple activities may be required to move it forward and turn it into an investable transaction. These activities may occur simultaneously or in various sequences. For example, the steps for packaging a real estate deal might include gaining control of the site, selecting key project participants (such as developers, architects, and engineers), applying for tax credits or other public resources, and assembling required capital. Financing a small business might involve planning for growth by identifying a new location or additional equipment, applying for government incentives, and seeking a bank loan or line of credit. This is an excellent stage at which to reach out to engage previously uninvolved community, regional, or national players with relevant interests and/or expertise.

4. Negotiate the tradeoffs

Most community investments involve overcoming barriers, which can range from funding gaps to incompatible demands from stakeholders. Success often requires nimble negotiations and complex tradeoffs between what is feasible and what is desired, between the demands of investors and those of the community, and between what can be accomplished now and what would involve delay. Deals that are worth doing must contribute to achieving the community's shared priorities, but it is unrealistic to expect a single deal to fulfill every aspiration.

5. Structure and underwrite

Before a deal can close, investors generally need the approval of their investment committees. Obtaining such approvals usually requires preparation of a formal investment recommendation that includes the terms of the deal, a description of what is being financed, an assessment of the risks and how they are being mitigated, a description of the impact the deal is expected to have, reporting requirements, and procedures for repayment or termination of the deal.

It's worth noting that **different people and organizations may do the heavy lifting for each one of these steps**. For example, spotters typically need deep knowledge of and connection to a community, while framers need expertise in the dynamics of shepherding projects from start to finish. The entire process of generating and executing deals requires a combination of technical skills, many of which may be sparse or absent in some places. Gaps in capacity may be bridged by importing capable regional or national actors, engaging different local stakeholders, and/or by building up the skills of local players.

Prioritize and batch deals

Some communities are blessed with an abundance of deals at varying stages of execution. However, given the complexities of community investment transactions, most communities lack the capacity—the time, attention, and resources—to do all possible deals at once. Consequently, stakeholders need to develop criteria for prioritizing the deals they care most about and consider moving deals in batches, rather than individually, to bolster the pipeline's efficiency and accelerate deal completion.

1. Prioritizing

In developing criteria for prioritizing deals, stakeholders should take into account two different types of impact: the impact the deal will have on the community's shared priority and the impact the deal will have on the community investment system itself.

To assess the impact on a community's shared priority, stakeholders might consider the extent to which a particular transaction would help them address the need they have identified, whether it be for affordable housing, access to healthy food, or capital for locally owned businesses. Sometimes it helps to dig a little deeper than the first level of impact. For example: will a new unit of affordable housing be affordable to people in the targeted income range? Is it located in an area of opportunity, with good schools and proximity to transit? No community investment transaction will satisfy every need and desire, but it is important to understand which transactions will contribute the most to achieving the community's goals.

Another way to look at deals is to consider their impact on the community investment system.

Deals are system events, i.e. they are products of, and contributors to, the nexus of actors, resources, and experiences that add up to a community's investment capacity.

Some deals are breakthroughs: they prove the concept for a new financing approach, finance something in a neighborhood or sector that was not previously considered creditworthy, or bring a new source of capital into the system. Such deals not only finance housing, businesses, or facilities, but also leave the community investment system more robust and able to tackle the next challenge. We call these deals **catalytic** for the valuable contributions they make not only to their specific purpose but to the functioning of the community investment system as a whole.

2. Batching

Batching deals can be a useful way to accelerate their completion and overcome chokepoints in one fell swoop. For example, at a time when investment in Detroit was frozen and the community investment system lacked capacity, a community development corporation called Midtown Detroit Inc. identified eight potential mixed-use and affordable housing projects with similar financing challenges. Working together, a group of stakeholders including the Kresge Foundation analyzed the deals, the impact they could have, and what it would take to get them done.

Armed with this information, the stakeholders were able to attract the interest of Capital Impact Partners, a capable national CDFI, which agreed to help create and manage the Woodward Corridor Investment Fund. Investors in the fund, which included Kresge as well as two financial institutions, agreed to unusual terms designed to meet the particular needs of the Detroit market. The Fund was successful not only in getting the deals done, but also in catalyzing greater involvement in Detroit by a number of investors and intermediaries. A second fund was raised several years later, with broader targets–a testament to the power of batches.

COMMON MISTAKES

As with any skill, the ability to analyze, build, and execute a pipeline improves with practice. But to help get you started on the right foot, in this section we review the most common mistakes we have observed in our fieldwork and how to avoid them.

1. Overly detailed analysis

Don't drive yourself crazy trying to gather every bit of information about every deal you want to include in your pipeline snapshot. The purpose of the snapshot is to gain perspective on the current state of the community investment system as it relates to the community's shared priority, not to provide an exhaustive account of all aspects of all investment activity everywhere. A good rule of thumb is to make sure you spend more time analyzing the data and acting on what it tells you than you spend gathering it. In addition, deal participants are more likely to share information about their deals if they don't feel they are being pressed to disclose confidential details.

2. Generating an insufficient volume of deals

In many communities, deals come together–or don't–as a result of stakeholders acting in isolation. The result is often a pipeline that is too small. If analysis of the pipeline suggests that it is insufficient to address the shared priorities, stakeholders need to brainstorm how they can stimulate deal generation. This may require identifying potential sites for real estate development, inventorying small businesses with growth potential, or building deal framing capacity by importing regional actors and investing in local organizations.

3. No threshold criteria for execution

In our experience, stakeholders often fail to articulate the criteria both for including deals or projects in the pipeline and for prioritizing among available opportunities. Establishing concrete qualifications in these areas holds stakeholders accountable and ensures that their energies and resources remain focused on the deals that most closely align with the community's desires.

A pipeline of deals is the mechanism by which a community's shared priorities become a different tomorrow.

Building an appropriate pipeline and executing it efficiently is the mark of an effective community investment system. By understanding deals in motion, filling in gaps with additional projects and transactions, and accelerating the progress of priority deals by processing them in batches, stakeholders can strengthen the ability of community investment to achieve results for their community.

CONCLUSION

The systematic approach to pipelines outlined here is a departure from more traditional approaches to community investment work, which tend to be grounded in the assumption that the system would work well if only there were more money to finance projects. We have seen firsthand that money is actually not the missing piece, or, at least not the only missing piece, of a healthy community investment system. Sometimes the problem is a shortage of investable deals or a lack of understanding of the deals that are in the pipeline. Analyzing the pipeline helps to diagnose what is happening in the system and consider avenues to resolve issues. Building the pipeline helps to ensure that the community has sufficient deals in process to achieve its goals. Executing the pipeline efficiently and strategically, by prioritizing and batching deals, further enhances the likelihood of success and can improve the community investment system as a whole at the same time as it accomplishes the community's goals. In the end, the pipeline is where community investment becomes much more than the sum of its parts.

We are excited by your interest in CCI and the capital absorption framework. To learn more about the framework, please see our *Community Investment: Focusing on the System* paper. The three functions of the framework are interdependent, so it is important that you read the other two briefs in this series: *Defining Shared Priorities* and *Strengthening the Enabling Environment*. If you have questions, please feel free to contact us. We will be happy to assist you.

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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