Place Matters

How Community Development Departments Are Rediscovering Communities

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New market realities and developments in public policy hold the potential to transform community development lending in banks from a regulatory requirement to a community-revitalizing profit center. To accomplish this, community development lenders must return to the place-based thinking that inspired the Community Reinvestment Act (CRA). A sustained and focused effort by banks, utilizing all of their product lines, has the potential to help low-income communities thrive economically while adding new customers and depositors at the same time.

As enacted by Congress in 1977, the Community Reinvestment Act (CRA) was fundamentally a place-based legislation. By drawing regulator attention to under-served geographic areas, it aimed to connect these communities with mainstream financial services and concentrate lending activities within them. Ideally, the resulting inflow of capital would both mitigate the historic effects of redlining, and stimulate perceptible change in the communities.

It was a bold vision and by most accounts, the CRA has been effective at spurring lending to low-income households. But few would argue that the CRA, or the community development departments that major banks created to carry out their CRA obligations, have fulfilled their potential for neighborhood transformation. Although the vision of the CRA was decidedly place-based, its implementation and impacts have been more diffuse.

This failure to permanently transform neighborhoods does not stem from an exhaustion of capital or over-estimation of bank capacity. Banks represent vast and varied pools of capital: home mortgages, home equity and improvement loans, lines of credit, small business loans, commercial real estate loans, college education funds, savings and retirement accounts, and so on. Arguably, no other institutions – public agencies included – possess a bank's capacity to alter the economic trajectories of low-income communities.

Unfortunately, there are internal barriers within banks that prevent community development departments from liberating, deploying, and leveraging the banks' financial resources. Four such limitations are described below:

Marginalized Status: Community development departments are too often marginalized within their own banks. At best, they are seen as "interesting philanthropic outgrowths;" at worst, they are considered parasitic drains on the bank's bottom line whose resources are "throw-away money," or a "necessary cost of doing business." They are often isolated or at odds with the individuals in charge of the bank's core investing, lending, and service functions.

Market Irrelevance: Community development departments have little voice in product development or marketing activities. Typically, community development officers have few opportunities to propose innovative products and services that could achieve "early market penetration" in untapped markets. Nor can they participate in crafting underwriting or risk management strategies. Instead, they must resort to coaxing and cajoling colleagues to make loans or participate in deals that do not fit comfortably within existing business models.

Non-Aligned Resources: Over time, many community development departments established for CRA compliance came to house a range of other corporate functions: community relations; public relations; volunteerism; financial literacy delivery; and sometimes foundation grant making. Too often, these functions have been narrowly defined as charitable or regulatory activities that do not align tightly with the overall mission of community development. Perhaps more importantly, banks do not employ these tools for the larger challenges of customer development and market expansion.

Lack of Geographic Focus: CRA-related loans and investments are too often made on a deal-by-deal basis, dispersing resources across a bank's region or service footprint, diluting their effect on specific communities. CRA lenders have failed to situate their investments in the context of neighborhoods. And they have missed opportunities to cluster investments in close proximity to one another to dramatize their effect or create synergies.

Increasingly, however, community development managers at major banks have stepped up to address these obstacles and to engage in a more expansive vision of the role their department can play in bank performance and in the comprehensive revitalization of low-income communities. Far from focusing merely on regulatory compliance, they are embracing a new paradigm closer to the spirit of the CRA.

A New Market Orientation

This new era for community development departments has been made possible by a widespread shift in perception: low-income neighborhoods are being viewed less as problem areas to be endured, and more as untapped, "emerging markets." From policymakers to nonprofit practitioners, the challenge is no longer defined as a social need to be met through charity or corporate citizenship, but as a set of "market imperfections" to be addressed so that resources will flow freely.

In public policy, the role of market forces in developing land and producing affordable housing is now better appreciated, and many policy frameworks have been modified to improve the functioning of these markets for low-income populations. Federal "New Society" programs, designed around notions of an urban underclass requiring subsidized housing and services, have been replaced by investment approaches, from Enterprise Zones, Empowerment Zones, and New Markets Tax Credits to the more recent efforts to create an "Ownership Society."

Philanthropic and nonprofit sectors have also begun to embrace a market-oriented approach. Social problems like inadequate healthcare, childcare, or educational opportunities, are increasingly seen as root causes of poverty, and community groups that formerly emphasized direct care or relief services aim to help their clients attain economic

Case Study

Box 2.1

Wells Fargo Bank in Pacoima

Wells Fargo established a place-based "emerging markets initiative" in Pacoima, a low-income immigrant community in Los Angeles' San Fernando Valley. Relying on traditional and innovative market research, Wells Fargo opened Pacoima's first new bank branch in 17 years. Residents were hired to operate the branch, and local businesses engaged as suppliers.

Then, coordinating an array of innovative social marketing and customer development strategies, Wells Fargo:

- Launched a home-based grassroots financial literacy campaign using a peer-to-peer model that touched more than 200 hundred households, of which 50% become account holders within three months;
- Assigned bankers to carry out "guerilla marketing" strategies at swap meets, chamber of commerce meetings, church and school events, soccer matches, and block clubs, driving increases in savings accounts by a factor of 10;
- Sponsored off-site account enrollment at a neighborhood churchyard, in conjunction with the Mexican Consulate. Accounts opened in one morning doubled the branch's daily average;
- Piloted a new international wire transfer product aimed at cultivating non-account-holding immigrants sending money regularly to Mexico;
- Capitalized a $200,000 micro-loan fund with a local business assistance center and established a "loan pipeline" to graduate borrowers into Wells Fargo customers;
- Seeded a $250,000 fund for down payment assistance and home repairs at the local housing assistance nonprofit; and
- Helped finance a community-owned credit union set up to help individuals with credit or naturalization issues to build a banking record.

In the context of this initiative, Wells Fargo's Pacoima branch has surpassed performance goals and proven wrong all who doubted its viability. Other banks are now reconsidering Pacoima as a market.

Hard evidence demonstrates that these market development strategies have directly contributed to increases in transactions and loan volume. By tracking participants in financial literacy or micro-loan programs, for example, Wells Fargo knows that many ultimately became Wells Fargo customers.

The Wells Fargo Community Development Department, with its double bottom-line emphasis, has become central to the business model.

self-sufficiency. Foundations have replaced traditional grants with program related investments, small business loan funds, land trusts, individual development accounts, and other creative, economic strategies. Large-scale philanthropic investment strategies, sometimes termed "comprehensive community initiatives," now target entire low-income neighborhoods, stimulating every facet of their socio-economic development.

This shift has overtaken the private sector, too. As the economy expanded in the late 1990s, many industries faced increasingly saturated markets and recognized that low-income target areas often represent their last untapped customer bases.

Consider, for example, the market potential of immigrants. For banks, the key to gaining market share is banking urban immigrant groups, especially Latinos, who represented massive numbers of people and dollars being forced to choose between the underground and mainstream economy. These prospective customers tend to concentrate in geographic areas with few or no bank branches and where banks have little practice doing business. To reach these market segments, then, banks must immerse themselves in the communities, develop products and services that meet local customer needs, and construct new delivery systems for serving them.

Successful efforts by banks to bring immigrant customers into the mainstream include using foreign identification, such as the controversial Matricula Consular, to enable immigrants without citizenship to use foreign identification to open bank accounts. Similar innovations have been developed for remittances and mortgages. And while Latinos receive the most attention, there is tremendous interest in developing products for African Americans, Asian Americans, and Native Americans, too.

Adapting Existing Capacities to the New Paradigm

As it turns out, many capacities and competencies required to accomplish these tasks are already in place within the banks– in community development departments.

Most community developers at banks have in-depth familiarity with at least some low- and moderate-income (LMI) neighborhoods in their markets, usually those where they have historically made CRA investments. By disaggregating existing market research to the neighborhood level and combining it with other formal and informal research– including interview and focus group data from local leaders– CRA officers can compile and publish comprehensive guides to these micro-markets. Packaged properly, this research can be invaluable to colleagues on a bank's retail side.

Case Study

Box 2.2

Bank of America in Westlake/Pico Union

Since 2000, Bank of America has targeted a small neighborhood west of downtown Los Angeles that serves as a "portal community" for Central America immigrants. Although there is already a Bank of America branch in Westlake, rapid demographic change has called for reinvented community relationships.

As part of its array of strategies, Bank of America:

- Mobilized more than 100 bank volunteers to deliver financial literacy classes at every area school, reaching 2,000 students, many serving as "financial agents" for their parents;
- Crafted a small business training program for informal sector entrepreneurs seeking to transition to the mainstream economy, graduating over 175 individuals in two years.
- Initiated "homebuyer clubs" and short-term adult financial planning sessions at multiple nonprofit locations throughout the community, helping to increase consumer savings accounts by a factor of 14 between years one and five;
- Partnered with business assistance agencies to conduct outreach, provide technical assistance, and refer loan applicants. SBA loan approval rates rose by a factor of 10;
- Organized three adult education agencies into a workforce pipeline, graduating as many as 1,200 individuals per year from ESL and computer classes, and moving some into bank jobs; and
- Invested $15 million in multiple housing developments, producing more than 500 new, affordable homes to residents.

Based on the early double bottom-line results of this initiative, Bank of America has expanded its effort to focus on two additional Los Angeles neighborhoods over the next five years.

Neighborhood-level research is most useful to the bank's profit centers if it directly addresses specific business challenges faced by new or under-performing branches. To boost business in these branches, community development managers have begun to advocate for their neighborhoods to be treated as test markets for customer focus groups, new product or product suite development, and the piloting of broad marketing initiatives.

Focusing on small geographies yields benefits. It allows bankers to achieve saturation-level marketing, explore the interdependencies of different banking strategies, and exploit cross-selling opportunities. Small target areas permit risk-taking and short-term, measurable outcomes that would be impossible at a large scale. New products can be tested with little long-term risk and bankers can observe connections between various investments. The successful performance of a business loan, for instance, depends on the success of nearby businesses, and vibrant business districts increase home values in adjacent residential districts.

Once the bank sets business objectives in a low-or-moderate-income neighborhood, the community development department can allocate and align its resources to help meet those objectives. Existing nonprofit relationships, for example, take on new light. Reaching untapped markets often requires the formation of a loose configuration of community-based organizations, informal associations, and natural helping networks. Once in place, this network can play multiple roles related to popular education, marketing, and product delivery.

For example, homeowner associations, block clubs, neighborhood watches, and parent associations can tap into vast numbers of prospective homebuyers. Merchant associations, business improvement districts, trade groups, and emerging chambers of commerce comprise hundreds of business leaders. Social service agencies, civic associations, and faith-based organizations can serve as in-take valves for new account holders. Taken together, this decentralized system can engage thousands in education and counseling around financial literacy, personal banking, tax preparation, and retirement planning, dramatically expanding a bank's market.

One implication of developing a "Neighborhood Delivery System," as our firm calls it, is that banks need to move away from scattershot grant making – giving too little funding to too many grantees in order to maximize visibility. Instead, banks should choose a handful of strategic nonprofit partners in which they invest in significant ways, ensuring that those agencies can perform their partnership functions. Investments may include grants, loans, equity equivalent investments, board leadership, or volunteerism. Partnership structures can be varied, depending on the goals, which can include deal sourcing arrangements, managed loan funds, referral compacts, marketing agreements, and off-site account enrollments.

In choosing affordable housing or retail projects to invest in, community development managers can direct resources to sites in close proximity to one another, creating transformative effects and strengthening the overall economic productivity of the area. To catalyze new projects, managers may enlist local residents and researchers to map every developable property in the target area and then bring these to the attention of nonprofit and for-profit developers.

The goal is to demonstrate double bottom-line outcomes: to find profitable business opportunities in LMI neighborhoods, and help those neighborhoods gain overall economic benefit from this process.

To guide other financial resources into the area, managers may convene a time-limited working group within the bank, one that assembles representatives of all business lines – small business lending, home mortgage, retail banking, and private client services, as well as marketing and corporate communications. The goal of this group is to channel the full range of business strategies in a way that meets the community's banking needs.

Bringing all of these strategies together, community development managers can mount major initiatives that comprehensively develop specific neighborhoods. The goal is to demonstrate double bottom-line outcomes: to find profitable business opportunities in LMI neighborhoods, and help those neighborhoods gain overall economic benefit from this process.

Tracking Outcomes and Assessing Progress

To demonstrate these double bottom-line outcomes, community development managers need to become adept at data collection and management. Bank performance data must be disaggregated to the granular level of the target area and "scrubbed" to exclude irrelevant figures. Charitable grants and marketing agreements that fund neighborhood-level activities in the neighborhood must be inventoried, ensuring that nonprofits headquartered outside the community zip code (but delivering services within it) are not overlooked. And baseline data from external sources, such as the Census, should be compiled.

But collecting data is only the beginning. The next step is to articulate a logical series of inferences that connect the dots between data sets, incrementally building the business case for neighborhood initiatives. The following questions can help:

What new capacities now exist in the bank (e.g. interdepartment teams, localized marketing, targeted grantmaking)? Did these lead to market-related partnerships with neighborhood groups?

Have the partnerships measurably improved the economic capacity of individuals, households, or firms? For example, can we count the number of individuals who addressed credit problems, couples that completed homebuyer workshops, or businesses that adopted a business plan?

Did the bank experience an aggregate increase in new accounts, loan volume, or investments in the target area? How much of this growth resulted directly or indirectly from partnership activities?

At the neighborhood level, are there detectable changes in baseline levels of homeownership, income, employment, local spending, or savings? Did bank interventions leverage more capital or in any way contribute to these trends?

Taken together, the answers to these questions can constitute a forceful argument that financial literacy, microloan funds, and other community development activities drive growth in deposits and loan volume. And armed with insights into the relative profitability of different population groups in the community (and the most effective way to tap into each), community developers can participate meaningfully in marketing and product development discussions.

A New Vision for Community Development

Taken to its logical conclusion, this kind of initiative implies a wholly re-imagined community development department, one that leads the charge into previously underserved markets. In addition to its regulatory and compliance functions, it creates and markets new products that bridge customers from the un-banked to the traditionally banked. Over time, it may develop its own set of financial products, just like any other business line.

The goal is not for these departments to abandon their social goals or CRA origins. It is to discover the double bottom-line benefits that are possible when a bank channels its many resources into an LMI neighborhood. The vision is driven not only by federal regulations, but enlightened self-interest.

In the long-term, community development departments will become more important players within their banks and demand greater resource allocations. And when bankwide resources are aligned, communities benefit. And the vision of the CRA is fulfilled. CI

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COMMUNITY INVESTMENTS

Endnotes

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