GREATER ROSELAND COMMUNITY DEVELOPMENT CORPORATION WORKSHOP

Chicago, Illinois
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Community and Economic Development and its Related Benefits

I'm very pleased to be here today to take part in this workshop on community and economic development. I know that some very innovative efforts are underway in the Roseland community, and today's activities should help build on those accomplishments.

Having spent more than two years with the U.S. Department of Housing and Urban Development, I've spent a lot of time dealing with issues relating to the economic development of urban areas.

When I was at HUD in the 1970's, I was involved with efforts to assist Neighborhood Housing Services, which was just getting off the ground. At that time, we also de-emphasized the construction of high-rise public housing projects and other subsidized housing and shifted to providing housing subsidies to individuals — an approach that seems to be getting more and more popular today.

Being relatively new to the Federal Reserve System, I'm really excited about getting an opportunity again to have an impact on community development issues.

In preparing my remarks today, it occurred to me that a lot of what we're discussing relates to a fundamental issue the Federal Reserve's founders confronted much earlier in this century — namely the issue of credit availability.

Back then, concerns centered mainly on the needs of farmers in rural areas versus the concentration of credit in large urban centers. Today, we're concerned with the development of low- and moderate-income neighborhoods in urban areas. Equal access to credit really gets to the heart of why we are here this morning.

What I'd like to touch on today is why, from a business perspective, access to credit is so crucial to developing communities and why equal access to credit is both good business and good public policy.

We all have a stake in community development and there are many ways to make it work. So today I'd also like to give you some examples of working partnerships that have been successful in providing credit to the community.

Years ago, many community development projects and initiatives were financed primarily with federal funds and, to a much lesser degree, by the private sector. Today's entrepreneurs, especially in areas like the Roseland and Pullman neighborhoods, face cuts in those federal funds. That's a trend likely to continue. People are looking more and more to the private sector to fill the financing gap. Frankly, I think that just might be the right place to look.

Why the private sector? Because private-market solutions tend to be more effective than government allocations. Government just cannot, and should not, carry the burden alone. Private sector involvement, indeed leadership, is essential.

One thing I think we've all learned is that government can't do everything by itself. Government alone can't make a neighborhood prosper. It can't bring a new dry cleaners into a low-income area. It can't build a new Jewel or Dominick's. Government provides the framework in which development can take place, but the private sector really has to be the foundation for growth, the force that prompts development and, more importantly, sustains it.

Community development initiatives are getting a lot of attention these days from the banking industry and regulators. That's because prosperous communities are in everyone's best interest: residents, businesses, and the community at large.

To foster strong neighborhoods, comprehensive community development lending is critical. That's sound financing for mortgages, home improvements, and small business development. When that kind of lending takes place, you have the basis for a prosperous community.

Too often we see the impact of disinvestment in our neighborhoods, not only here in Chicago, but across the Midwest and across the nation. How should all of us respond? It takes a commitment by all players involved to ensure that good economic investment opportunities are eagerly pursued.

We need to cooperate with each other through the sharing of information and ideas on how to utilize programs and subsidies so that loan deals with a strong potential for success are given fair consideration.

There are currently a number of initiatives being implemented with the goal of creating and maintaining healthy communities. Partnerships, whether among private parties or involving the public sector, are an essential component in promoting development, stabilizing neighborhoods, and creating an environment conducive to rebuilding and renovation.

While partnerships are not a new phenomenon, it is only in recent years that lenders have formed partnerships with local community-based organizations. This type of union is becoming much more common. Some of these partnerships are the result of lending agreements. Others are the result of loan consortia. In addition to forming partnerships, some lenders are increasingly proactive and creative in designing new, and modifying current, programs to address the needs of low- and moderate-income areas and the people who live there.

It's encouraging that every year the number of lenders involved in community development finance continues to grow. Lenders are also becoming more and more knowledgeable about these initiatives. Lenders are becoming more sophisticated in using federal, state and local programs, and leveraging public and private funds to make deals possible. The benefits of these initiatives are significant:

- For an individual — If a loan results in their buying or rehabbing a home.
- For a business — If the loan results in development and expansion.
- And for a community — If the loan addresses blight and fosters regeneration.

It's important that lenders view community development financing as a regular part of their business and integrate it as such. Many lenders who have been successful with these programs and loans are doing just that.

It's also important for lenders to remember that community development financing generally is a long-term investment. The results, the impact of the programs, become evident over a period of time.

Many people have questioned whether being involved in community development lending is profitable and whether those involved have experienced heavy losses. On the question of loan losses, our discussions with lenders involved in community development finance show that these loans are performing just as well, if not better, than their conventional portfolios.

A study conducted jointly by the Woodstock Institute and the National Association for Affordable Housing Lenders supported this conclusion. The study indicated that targeted reinvestment loans in low- and moderate-income areas were performing as well, if not better, than the industry averages for loans. And loan losses experienced by lenders participating in the study were extremely low. As for profitability, the Federal Reserve Board in 1993 issued a report to Congress indicating that community development financing can be profitable, but probably is not as profitable as non-community development financing.

Higher fixed costs and the labor-intensive nature of processing these loans come into play. That's also a situation that should improve over time as lenders develop systems, expertise and information bases that will ease the process.

There are numerous documented examples of lenders undertaking successful community development initiatives throughout the U.S. Let me highlight a few of these successful examples:

Right here in Chicago we have the Community Investment Corporation, which receives a significant amount of lender support. The CIC, through its loans and its public/private partnerships, financed $470 million in multifamily rehabs in low- and moderate-income neighborhoods between 1984 and 1994. Their loan losses —- less than three-tenths of a percent (0.3%).

First National Bank of Chicago and Harris Bank entered into lending agreements for housing and business loans in 1984 and 1989 with the Community Reinvestment Alliance, a group consisting of more than 30 community organizations.

First National, with a loan portfolio of over $250 million, had no loans in default and Harris' loans had the lowest loss rate in the bank, just one-tenth of a percent (0.1%).

Bank of America in California established its Neighborhood Advantage Program in 1990, using non-traditional underwriting criteria. Rent and utility payments are considered in lieu of credit history and administrators look at steady income streams in instances when an applicant has had multiple jobs over a two-year period.

These loans are at market rate, and Bank of America has generated over $6 billion in home loans since the start of the program.

In New York, Bankers Trust Company started a community development loan program in 1990. By 1994, it had committed over $116 million in loans and investments to low- and moderate-income communities in New York City, without any delinquencies.

Our discussions with community development organizations around Chicago also indicate that partnerships are indeed operating — and new ones are being established.

One relatively new partnership is the one here in the Roseland/Pullman community with the Greater Roseland Community Development Corporation. As some of you know, this CDC established an incubator. It currently has six micro-businesses operating within its space.

It is hoped that these businesses will continue to grow and eventually graduate out of the incubator. Small business economic development like this is needed in many areas on Chicago's South and West Sides.

Outside Chicago, but still within the Seventh Federal Reserve District, an innovative partnership is forming in Indianapolis under the leadership of Mayor Stephen Goldsmith. Private, not-for-profit community development corporations are counseling individuals on how to secure credit. CDC representatives then approach participating banks on the individuals' behalf. It's a program with real potential for success, especially since it's structured to help reduce the amount of paperwork banks have to carry out in processing the loans.

As you can see, the number of lenders involved is growing and many lenders are starting to see community development lending as an emerging and promising line of business activity.

It's important to remember that partnerships, like some of the ones I've described, not only result in community development deals, but help to minimize the risk of projects and allow funds to be leveraged with other sources. But for partnerships to work, all the players have to understand each other's roles and recognize that everyone has a stake in the project being a success.

It is also important for all players to work together to solve any issues that could negatively impact the project. Community-based organizations and lenders have to work side-by-side to address issues relating to the secondary market, appraisals, underwriting, and regulatory and documentation concerns.

We at the Federal Reserve support partnership efforts as a means for lenders to address the challenges of revitalizing our communities. We encourage lenders to reinvest in their communities through any approach and we have taken a number of steps to assist lenders in their efforts.

First and foremost, we have established a Community Affairs Program at each of the twelve Reserve Banks. The Federal Reserve Bank of Chicago's program has been operating since 1981 and we continue to evolve and reassess our goals and objectives to cater to the needs of our District lenders and community organizers. Currently, through the Community Affairs Program, we:

1) Provide technical assistance to lenders within the Seventh District on how to establish community reinvestment programs and on compliance and community reinvestment regulatory requirements;

2) Act as an information broker by meeting with lenders, community organizations and the general public and by sharing information on federal, state and local government programs and successful private and community initiatives;

3) Sponsor conferences and workshops on community reinvestment and economic development initiatives;

4) Develop publications and brochures on community and economic development and regulatory requirements; and

5) Facilitate partnerships between the private and public sectors.

Our latest endeavor is a newsletter, Economic Development News & Views, which premiered in January and features information on business and economic development in the District. Copies are available at the back of the room for those of you who would like to see the latest issue.

For the future, we're developing plans for economic research related to community development and credit availability. We also plan to establish forums bringing together major players to address issues related to credit availability.

Our Reserve Bank activities are complemented by some recent regulatory and legislative changes at the national level.

A recent Federal Reserve System initiative permits state member banks to invest in certain projects that promote community development — without prior approval from the Fed. This is one less regulatory hurdle, something that will lower costs by removing a layer of bureaucracy.

These activities, as outlined in Regulation H, must be specifically targeted for low-and moderate-income areas and people. They include: housing, nonresidential real-estate development, small business development, job training or placement, job creation, and technical assistance and credit counseling to benefit community development.

On the legislative front, state member banks will also be allowed to invest in community development financial institutions as defined in last year's Community Development Banking and Financial Institutions Act.

Bank holding companies have been permitted to engage in community development activities, with the Fed's approval, since the 1970's. Many of these activities were previously carried out either through establishment of a community development corporation subsidiary or through direct investments by the bank holding company.

Other recent rule changes permit bank holding companies to invest in community development projects or corporations that meet regulatory requirements — that, too, without prior approval.

In closing, I think it's important to reiterate that the private sector needs to sustain economic vitality by using its expertise and staying power to ensure that community development occurs. Government alone can't make neighborhoods prosper. Private business and private organizations have to do it. Government can set the guidelines and offer a helping hand, but the private sector really has to make it work.

Our challenge is to help re-establish positive, dynamic market forces in areas where they no longer exist. Whatever approach is used — whether a lending agreement, a community-development corporation, or some other type of initiative — each can serve as a catalyst to bring together a variety of resources, both public and private, to spark private economic activity.

We are here today to develop new ideas and learn from each other about those techniques that work and why. Prosperous local communities are building blocks to maintaining a strong economy, probably our most important area of concern at the Federal Reserve. Strong and healthy neighborhoods are vital to a strong and healthy nation.

The private sector, with appropriate guidance and support from the public sector, has to be a leader in keeping our neighborhoods prosperous through successful community development initiatives. The key is building solid working relationships among all sectors. To have a strong economy, everyone must participate.

Workshops like today's will only enhance that effort. Thank you very much.