BRIDGES | SPRING 1998
https://www.stlouisfed.org/publications/bridges/spring-1998/rockefeller-foundation-supports-arkansas-development

Rockefeller Foundation Supports Arkansas Development

During Winthrop Rockefeller's term as governor of Arkansas (1967-71), he was an advocate for human rights, government reform, and economic and cultural development, as well as education. He believed that the quality of life for all Arkansans could be improved. The 24-year-old Foundation created in his honor works to fulfill Rockefeller's desire to ensure that Arkansas becomes free of economic, social and educational barriers.

With the passing of the foundation's president, Mahlon Martin, in 1995 and the hiring of Dr. Sybil Jordan Hampton in October 1996, the Winthrop Rockefeller Foundation (WRF) board and staff has had an opportunity to reaffirm the Foundation's mission and values. During 1997, the WRF program officers and president spent 14 days traveling around the state to visit organizations exemplifying best practices and to meet informally with some of their stakeholders. This exercise proved invaluable as the WRF staff examined past grant-making practices and the organization's internal capacity. The process is still unfolding, but it is clear that the same values will be demonstrated in the new ways the Foundation's work takes place.

No matter the changes that take place, the work of the Foundation will always focus on improving the quality of life for all Arkansans in three interdependent areas—education, economic development and citizen participation (see chart below). Using this holistic approach, the WRF will no longer issue grant guidelines but will use the request for proposal model as its future grant solicitation strategy.

Given the fact that more philanthropic organizations locally, regionally and nationally are funding Arkansas' nonprofits and educational institutions than ever before, WRF plans to partner with these foundations to seed best practices and to build a viable and sustainable nonprofit sector.

In 1997, the WRF provided more than $4 million for continuing grants. The Foundation places a priority on identifying and providing seed funding for organizations engaged in best practices. Increased collaboration with other grant makers will offer new leveraging opportunities and a larger network for nonprofits.

Dr. Hampton recognizes that over the past 24 years, the Foundation's role has evolved from being one of a precious few to being one of many funding sources. Looking ahead, this role shift will offer the Foundation an opportunity to work in new ways. National philanthropic organizations are beginning to solicit information about best practices in Arkansas. Therefore, the Foundation can become a resource for network building and for linking potential partners.

Winthrop Rockefeller Foundation Areas of Concentration

Education: Funding for projects that involve teachers and parents in making decisions about what happens in their schools; enable university faculty and public school teachers and administrators to work together to train student teachers; and promote stakeholder participation in the development of educational policy.

Economic Development: Funding for projects that strengthen local economic development efforts; provide access to capital, management and technical assistance for small businesses; strengthen agriculture as an economic resource; and improve the economic status of women and minorities.

Citizen Participation: Funding focuses on strengthening community-based organizations working to improve their communities, develop leaders, and advance minority and equity issues.

BRIDGES | SPRING 1998
https://www.stlouisfed.org/publications/bridges/spring-1998/community-development-loans-and-the-secondary-market

Community Development Loans and The Secondary Market

Keith Turbett

New advances in the community development lending field have opened up opportunities for increasingly creative lending tools. Some are not necessarily new but are utilizing products once thought only applicable with "typical and routine" lending. One product that has been developed is packaging community development loans from entities and selling them to investors to recycle capital. This has created a unique secondary market. This market is small but could make a serious impact over the next few years as public funds begin shrinking and the need for recycling scarce capital becomes greater. Several entities are responsible for developing this market, setting it up in much the same way that a mortgage company buys home loans from lending institutions.

Examining the credit system for single-family mortgages demonstrates the tremendous possibilities offered by an organized secondary market. More than two-thirds of new single-family mortgages originated in the United States are sold on the secondary market. According to Fannie Mae, the outstanding balance of residential mortgages pledged to instruments such as mortgage-backed securities (MBS) in mid-1996 was $1.6 trillion, or 43 percent of total residential mortgage debt outstanding.

In the same way the single-family market has provided for the recycling of funds throughout the mortgage industry, the recent development of an efficient financing system for community development loans serves the needs of community-based borrowers, lenders, investors and the public. It does this by providing a renewable, ongoing source of capital for community-based lenders, and supporting the efforts of federal, state and local government and the philanthropic community to sustain affordable housing and economic development programs by leveraging existing assets over time.

One such fund is the Community Reinvestment Fund (CRF), which is located in Minneapolis. Its core service is the creation of a secondary market for community development loans. It buys loans from development organizations, giving them cash to reinvest in their communities.

More than two-thirds of new single-family mortgages originated in the United States are sold on the secondary market.

The loans are bundled and used as collateral to issue bonds. The bonds are sold to private investors, thereby matching private investment with public funds. Since 1989, CRF has purchased or committed to purchase 864 loans, totaling more than $52 million, from 57 organizations in 13 states and Washington, D.C. In purchasing these loans, CRF has provided more than $46 million in cash to local development lenders for reinvestment in their communities. In addition, seven organizations have signed Advanced Commitment agreements to sell $6 million in future loans during the next two years. All clients agree to reinvest their loan sale proceeds into small businesses and related development projects. About 65 percent are small business loans, and the rest are for housing assistance and rehabilitation. The default rate is less than 2 percent, and the delinquency rate is 1.5 percent.

CRF works to develop a well-functioning secondary market for community development loans in three ways:

- It promotes access to a steady source of funds for borrowers by purchasing loans from community-based lenders, such as local revolving loan funds, city governments, and housing and economic development authorities;
- Community Reinvestment Services, CRF's loan-servicing organization, strives to ensure that borrowers repay their loans as agreed.
- It issues loan-backed securities with competitive rates and a low risk-profile, factors that are attractive to investors and promote the long-term viability of the market.

Another entity in this field is the Local Initiatives Managed Assets Corporation (LIMAC), which focuses primarily on housing loans with an emphasis on tax credit equity bridge loans. Based in New York, LIMAC began in 1987 with an investment from The Ford Foundation, which also established the Local Initiatives Support Corporation (LISC). LIMAC purchases loans that were originated to:

1. finance the development or acquisition of low- and moderate-income housing;
2. help revitalize deteriorating neighborhoods and/or stabilize low-income communities;
3. finance the acquisition or development of property for commercial, retail and community service use benefiting low-income communities; or
4. create employment opportunities for low-income persons. LIMAC initially purchased its housing loans exclusively from LISC but now purchases from a wide variety of originators, such as the Low Income Housing Fund, state housing finance agencies, and other community development financial institutions.

Neighborhood Housing Services of America (NHSA) also is in the market for community development loans, primarily in support of its network of more than 170 NeighborWorks organizations. Under its two primary programs, NHSA buys rehabilitation loans originated by local NeighborWorks programs. It also buys home mortgage loans originated by local lenders on behalf of nonprofits. NHSA has purchased about $35 million in loans annually, with a cumulative total of more than $200 million in loans in its 23-year history. The majority of NHSA's investors are insurance companies and financial institutions.

Secondary market entities should be looked upon as good opportunities for investors to make an impact on their community.

Intermediaries such as CRF, LIMAC and NHSA prove that community development loans can be good investments. They have never been delinquent on a bond or other scheduled payment, and there have been few defaults. Investment returns have been attractive as well. In the case of CRF, for example, investors have obtained returns ranging between 160 and 200 basis points above comparable Treasury rates. Underwriting criteria are high by any standard, and risk is mitigated by excess collateral, excess cash flow, credit enhancements and other structural safeguards.

These intermediaries offer avenues for the recycling of community dollars that make an impact on the growth of the community as a whole. Whether it be for small business development, affordable housing, or economic development, these secondary market entities should be looked upon as good opportunities for investors to make an impact on their community.

Endnotes

1. Information found on the CRF website at www.crfusa.com.

2. Information found on the Neighborhood Reinvestment website at www.nw.org.

FEDERAL RESERVE BANK of ST. LOUIS
CENTRAL TO AMERICA'S ECONOMY®

BRIDGES | SPRING 1998
https://www.stlouisfed.org/publications/bridges/spring-1998/seven-principles-for-reducing-delinquencies

Seven Principles for Reducing Delinquencies

David Boehlke

For some lenders, delinquency rates in special lending programs are consistently higher than for conventional loans. Yet good performance on affordable mortgage products is vital to the long-term success of these programs.

National studies have shown that very small down payments, coupled with limited monthly reserves and past credit problems, can lead to higher delinquency levels on home mortgages. The central issue isn't the trend toward higher delinquency. The focus should be on reducing this rate, because we must continue to serve this home ownership market.

Finding Some Answers

One possible answer comes from Battle Creek, Mich., a small industrial city recovering after years of decline. City leaders, local lenders and residents are restoring older neighborhoods through innovative strategies that rely heavily on special lending programs.

The strategies involve large-scale initiatives to demolish abandoned buildings, repave streets, repair substandard houses and attract new businesses and institutions. The principal strategy emphasizes lending for home purchase and for home repair. In less than five years, Neighborhoods Inc. has made more than 700 loans that have helped create more than $10 million in direct investment. These loans have significantly increased the percentage of home ownership, while creating higher standards for home maintenance.

With lending at its core, good loan performance is critical. Local leaders decided to build good performance into the design and delivery of loan products. To accomplish this, my staff and I committed ourselves to flexible but sound underwriting and to seven principles for reducing delinquency:

1. Maximize the buyer's responsibility.

It isn't beneficial to hold a buyer's hand through every aspect of the purchase. Each borrower needs to work hard to buy if ownership is to be valued. Neighborhoods Inc. expects borrowers to resolve their own credit problems, to track down missing records, and to establish and follow a good day-to-day budget. Neighborhoods Inc. also tries to include some modest sweat equity, so home buyers develop a stronger sense of personal involvement.

2. Prepare customers to make sound choices.

If counseling starts after the signing of a purchase contract, we have lost the best opportunity to help buyers. Buyers need to think through whether home ownership is right for them, what features the house should have now and for resale later, and what role the neighborhood plays in the purchase decision. Because lower-income buyers don't have as many choices, helping them make a well-considered one is even more important.

Higher-priced houses usually benefit from more active real estate agent involvement in the education process. We need to build the same training investment into the purchase of more affordable properties.

3. Remind borrowers they are buying a house and a neighborhood.

Encourage informed buyers to study the dynamics of the local real estate market. Borrowers need to analyze trends in the neighborhoods. A home purchase isn't done just to acquire good housing; it is a major investment and should show equity growth. An attractive house in a neighborhood of declining value usually ends up on an economic sidetrack. The resulting frustration can undermine good payment behavior.

4. Promote the goal of being "house proud."

Being proud of one's home is a powerful impetus to action. Affordable housing programs that only bring houses to a code-compliant condition may undermine a sense of pride in ownership. We've never met the buyer who proudly points to a house as meeting minimum standards. Home buyers need to feel their homes are special: an oversized kitchen, a gracious porch, or even just an outstanding paint job. If borrowers face some tough payment decisions, pride in the home is a compelling force to assure we get paid.

5. Provide counseling about the decision to buy, not just about the process of buying.

Deciding about buying a home and committing to pay the mortgage on time should be the focus for counseling. The mechanics and jargon of buying--title searches, right of recision, the distinction between a note and a mortgage--are important only if the fundamental decision to borrow is a sound one.

Too often a loan is approved contingent on reading a home-buying guide or attending a class. Yet much of what is learned will soon be forgotten. The important lesson: when borrowers know why they are buying, they will know why it is important to pay.

6. Structure financing as close to conventional as possible.

Even when Neighborhoods Inc. was involved in financing, we made every effort to place part of the financing with a conventional lender. Because most special programs are for people with a deficiency--too little down payment, insufficient earnings, shaky credit--these lending programs might imply a second-class status. We need to mitigate this by showing that a conventional lender is enthusiastic about taking on part of the loan. Having a nonprofit agency approve your loan is one thing; having a bank approve it is quite another. Reinforcing a standard bank relationship will strengthen the borrowing and lead to a long-term customer who pays.

7. Continue a positive relationship after closing.

In most conventional loans, lenders pay close attention to borrowers at purchase or at delinquency. This is reasonable. However, in a truly comprehensive affordable-lending program, the borrower is critical as an ongoing element in the neighborhood.

Committed, enthusiastic home buyers encourage others to buy a home and reinforce current homeowners who are considering property improvements.

A borrower committed to the neighborhood is more likely to be committed to loan repayment. Therefore, a good counseling program keeps an ongoing relationship with the borrower and encourages involvement in the community. There is a positive relationship with the counselor if payments become a problem.

Shared Expectations

Do these principles pay off? I believe they do. Of course, good underwriting is critical to a good loan, but delinquency control also must be built into every aspect of the purchase and mortgage process.

Is Neighborhoods Inc. pleased with the results? No. At any given time, troubled loans account for 2 percent to 3 percent of the group's portfolio. This is unacceptably high for a conventional lender. For a nonprofit organization lending to buyers who don't qualify for conventional lending, Neighborhoods Inc. expected higher percentages.

However, expecting higher delinquency and accepting poor loan performance are not the same thing. Neighborhoods Inc. continues to work hard to strengthen performance, not just to guard its portfolio or its borrowers, but to protect neighborhoods.

In today's highly competitive business environment, most lenders can't reasonably attempt the sorts of initiatives used every day by Neighborhoods Inc. Fortunately, most lenders have a relationship with a similar nonprofit already. What is absent isn't the opportunity but the expectation that nonprofit groups set high performance standards and meet those standards.

It is far too easy for both nonprofit groups and conventional lenders to accept poorer performance from special lending programs. The challenge is to set higher goals and then to structure the programs and resources to attain the goals.

Excerpted from an article in *Banking & Community Perspectives*, First Quarter 1997. Reprinted with permission from the Federal Reserve Bank of Dallas.

FEDERAL RESERVE BANK of ST. LOUIS
CENTRAL TO AMERICA'S ECONOMY®

BRIDGES | SPRING 1998
https://www.stlouisfed.org/publications/bridges/spring-1998/new-housing-organization-unites-mortgage-finance-system

New Housing Organization Unites Mortgage Finance System

The housing finance industry has created a new national organization to transform the homeowner education and counseling field. The American Homeowner Education and Counseling Institute, an independent national nonprofit based in Washington, D.C., held its first meeting in May 1997. Private business, national and local nonprofit community organizations, government, industry trade groups, lenders, mortgage insurance companies, and individuals formed the institute. It brings all segments of the mortgage finance system together to work in a collaborative process to transform fragmented and under-funded homeowner counseling activities into a professional industry that can achieve a scale that is recognized by the mortgage industry nationwide.

Specific goals of the institute are to:

- Create a nationally recognized program for the professional certification of homeowner educators and counselors;
- Establish a core curriculum for homeowner education and counseling that couples the need for nationally accepted standards with the need for local flexibility;
- Identify the costs and benefits of homeowner education in business terms and determine how education and counseling services can be financed on a self-sustaining basis; and
- Provide technical assistance to homebuyer education providers and create a central clearinghouse of materials and information on "best practices."

Homeowner education and counseling are widely regarded as the primary means for meeting demand in the rapidly expanding homeownership market. It benefits the housing industry by increasing certainties and decreasing risks associated with making homeownership opportunity more available, and it helps homebuyers and homeowners become better able to deal with the obligations and responsibilities of homeownership. The Institute may be contacted at (888) 243-2499.

BRIDGES | SPRING 1998
https://www.stlouisfed.org/publications/bridges/spring-1998/renaissance-kentucky-addresses-downtowns

Renaissance Kentucky Addresses Downtowns

Penny Young

A new approach in addressing the economic difficulties of Kentucky's downtowns is on the horizon. In September 1997, Governor Paul Patton announced the creation of the Renaissance Kentucky Program.

Many communities lost their downtown appeal when businesses moved outside of our cities decades ago to attract residents in outlying subdivisions. Now Kentuckians are recognizing and appreciating the aesthetic values and currently untapped potential of our rundown or abandoned downtowns. The Renaissance concept is designed to recapture the spirit of our local heritage, to recreate pride in our downtown centers, to promote tourism, to attract new businesses and jobs, to encourage cultural growth and to develop attractive housing convenient to successful businesses.

Before our cities can create successful redevelopment, they need assistance in locating funding sources and working through the maze of regulatory requirements. An alliance has been formed that consists of Kentucky Housing Corporation (KHC) as the lead agency, the Department for Local Government, the Kentucky Heritage Council and the Kentucky League of Cities to assist a Renaissance community with a redevelopment vision. To gain involvement at all possible levels of state government, Governor Patton will appoint a Renaissance representative from each cabinet to serve as an informational and/or financing resource to a Renaissance community.

State government resources will be identified and Renaissance communities will receive funding priority when appropriate. In addition to these priority funding resources, such as Community Development Block Grants (CDBG), the HOME Investment Partnerships Program, Low Income Housing Tax Credits (LIHTC) and the Intermodal Surface Transportation Enhancement Act (ISTEA), the state budget currently under review by the General Assembly includes matching grants for infrastructure and facade improvements. The Renaissance Alliance is also working on a state tax credit incentive program for rehabilitation of income-producing properties similar to the National Historic Tax Credit Program.

This opportunity for rebirth in Kentucky's downtowns will be an extraordinary collaboration that will be nurtured through all phases of progression. A mandate has been given to all branches of state government to work in unison to provide technical assistance and funding resources to a Renaissance community.

For additional information regarding Renaissance Kentucky, please contact Penny Young at (502) 564-7630, ext. 305.

BRIDGES | SPRING 1998
https://www.stlouisfed.org/publications/bridges/spring-1998/spanning-the-region

Spanning the Region

St. Louis Fed Names Poole New President

The Federal Reserve Bank of St. Louis named William Poole as president, effective March 23, 1998. Poole joins the St. Louis Fed after a 24-year career at Brown University in Providence, R.I., where he was the Herbert H. Goldberger Professor of Economics.

He twice has served as chairman of the economics department and was the director of the university's Center for the Study of Financial Markets and Institutions for five years.

"A Reserve Bank presidency carries with it special responsibilities in the community," Poole said. "As a citizen of the Eighth Federal Reserve District, I will contribute wherever I can to improving economic education and promoting economic and community development. I know that economic change often brings into the open many conflicting interests. The Fed can serve as an honest broker in bringing people together to resolve policy disputes."

Poole began his career at the Board of Governors of the Federal Reserve System in 1964 and worked as a senior economist there from 1969 to 1974. He was a member of the Council of Economic Advisers from 1982 to 1985 during the first Reagan Administration. Before joining the St. Louis Fed, he was a member of the Academic Advisory Panels of the Federal Reserve Banks of New York and Boston.

Mortgage Credit Certificate Program Available in Rural Missouri

The Missouri Housing Development Commission (MHDC) is offering a new program for rural areas throughout the state. The Mortgage Credit Certificate (MCC) program offers home buyers of newly constructed properties in rural Missouri a federal tax credit. The maximum MCC credit is the lesser of 25 percent of the mortgage interest paid per year or $2,000.

Only first-time home buyers may participate in the program unless the home to be purchased is in a target area (an area in which 70 percent of the families have an income that is 80 percent or less of statewide median). In addition, borrowers must meet MHDC's income eligibility guidelines.

The MCC is issued to a specific borrower in conjunction with a mortgage loan obtained through a participating lender. Any type of loan financing is acceptable, with the exception of a balloon loan.

For more information about the MCC program, contact the MHDC at (816) 759-6800.

SIRDP's List of Partners Continues to Grow

As previously reported in Bridges, the Southern Indiana Rural Development Project Inc. (SIRDP) has brought together partners from all across Indiana to support development of affordable housing. SIRDP's pilot effort in

Scott County resulted in the formation of the Scott County Housing Partnership and helped to establish alliances with developers, realtors, businesses, all levels of government, low-to-moderate income residents, banks and nonprofits.

SIRDP approached Indiana Housing Finance Authority (IHFA) and Cinergy/PSI Energy for support in creating a homeownership program and manuals to educate potential homeowners on buying a home. Both IHFA and Cinergy/PSI Energy were extremely receptive to the proposal and committed $32,785 and $22,385, respectively, to the project. SIRDP is:

- creating and printing a homeownership users' manual and accompanying instructors' manual;
- arranging to receive requests over a toll-free number for the manuals and to distribute them upon request;
- planning to conduct statewide publicity on the availability of the materials, while also educating potential organizers about appropriate usage; and
- planning three statewide presentations that detail the steps needed for holding local homeownership education programs.

For more information, contact Michael J. Traylor of SIRDP at 1-800-816-0019.