Density and Diversity: Evaluating One CDFI’s Place-Based Revitalization Strategy in Detroit’s Underwater Market

by

Diana Cristina Searl

B.A. Public Policy
University of Michigan, 2009

SUBMITTED TO THE DEPARTMENT OF URBAN STUDIES AND PLANNING IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE DEGREE OF

MASTER IN CITY PLANNING
AT THE
MASSACHUSETTS INSTITUTE OF TECHNOLOGY

© 2016 Diana Cristina Searl. All rights reserved.

The author hereby grants to MIT permission to reproduce and to distribute publicly paper and electronic copies of this thesis document in whole or in part in any medium now known or hereafter created.

Signature of Author: ____________________________

Department of Urban Studies and Planning
May 19, 2019

Certified by: ____________________________

Karl Seidman
Senior Lecturer in Urban Studies and Planning
Thesis Supervisor

Accepted by: ____________________________

P. Christopher Zegras
Associate Professor of Urban Planning and Transportation
Chair, MCP Committee
Density and Diversity: Evaluating One CDFI’s Place-Based Revitalization Strategy in Detroit’s Underwater Market

by

Diana Cristina Searl

Submitted to the Department of Urban Studies And Planning on May 19, 2016 In Partial Fulfillment of the Requirements for the Degree of Master in City Planning

ABSTRACT

This client-based thesis provides a review of three Detroit-based loan funds with the aim of understanding what developers have been able to access financing for multifamily and mixed-use developments in select neighborhoods. Though a great American city, Detroit has faced a declining population and dwindling economic base that has resulted in an upside down development market. Projects require complex capital stacks and high levels of subsidies, as rents alone cannot support development costs.

The client, a national CDFI with expertise in health care, education, and senior-living facilities financing, was invited to Detroit to support a private sector and philanthropic initiative to re-densify strong neighborhoods with amenity-rich, market rate housing. Through a series of interviews and surveys with developers, fund investors and partner organizations, as well as a review of projects financed, this research determined that the majority of Detroit developers were high net worth individuals with significant experience in the market and that the majority of funds concentrated in the Midtown neighborhood. While this finding is not surprising, it does serve as a counterpoint to the CDFI’s other goals of building local and minority developer capacity and expanding into new neighborhoods. The report highlights challenges noted by newer developers and provides recommendations for how this CDFI can support strong deals while fulfilling mission drive goals around inclusivity and affordability.

Thesis Supervisor: Karl Seidman
Title: Senior Lecturer in Urban Studies and Planning
ACKNOWLEDGEMENTS

This thesis would have been infinitely more difficult to produce without the incredible support of many people. My gratitude to the following folks:

Karl Seidman, my thesis advisor, for your support throughout this process, your willingness to take on a new type of thesis, for sharing your extensive knowledge and insight on economic development and finance, and for always making time,

Bradford Frost, for proposing an engaging and interesting project, facilitating introductions and meetings with key stakeholders, and providing thoughtful feedback,

All of the interviewees who took time out of their hectic schedules to share their thoughts on real estate development and the Detroit finance ecosystem,

My thesis-writing group, for always being there and sharing your wisdom,

The rest of my classmates for making this program a rich and rewarding experience and inspiring me on a daily basis,

My parents, Thom and Cecilia, for their unwavering support, cross-country cheerleading, and proofreading services,

and to Steve, for always making me laugh, for helping me maintain perspective, and for supporting me throughout this adventure.
# Table of Contents

EXECUTIVE SUMMARY ........................................................................................................... 7

INTRODUCTION ......................................................................................................................... 9
  LOCAL CONTEXT: DETROIT, MICHIGAN ................................................................................. 9
  CAPITAL IMPACT PARTNERS’ INVOLVEMENT IN DETROIT .................................................. 10
  RESEARCH FOCUS .................................................................................................................... 12
  METHODOLOGY AND DATA .................................................................................................... 13

THE LENDING PROCESS ......................................................................................................... 15
  DEAL SCREENING + BUSINESS DEVELOPMENT .................................................................... 15
  TRIAGE + ORIGINATIONS ...................................................................................................... 16
  UNDERWRITING + ORIGINATIONS ......................................................................................... 17
  CLOSING + CLOSING TEAM .................................................................................................. 18
  CONSISTENCY + VARIATION IN THE LENDING PROCESS ...................................................... 18

DETROIT FUNDS PORTFOLIO ................................................................................................. 20
  Overall Impact ......................................................................................................................... 20
  COMMUNITY IMPACT STANDARDS ....................................................................................... 23
  WOODWARD CORRIDOR INVESTMENT FUND PORTFOLIO .................................................. 21
  DETROIT NEIGHBORHOODS FUND ....................................................................................... 23
  DETROIT PREDEVELOPMENT FUND .................................................................................... 25

DEVELOPER PROFILES .......................................................................................................... 26
  CAPITAL IMPACT’S DEVELOPER POOL ............................................................................... 26
  UNSUCCESSFUL DEVELOPERS ............................................................................................... 28
  DETROIT DEVELOPER POOL ................................................................................................. 30

STAKEHOLDER ASSESSMENT ................................................................................................. 36

STAFF ASSESSMENT ................................................................................................................. 40

RECOMMENDATIONS ............................................................................................................. 43
  STRATEGIC ............................................................................................................................. 43
  INTERNAL ............................................................................................................................... 46
Executive Summary

This report provides a review and evaluation of Capital Impact’s three Detroit-based loan funds and its place-based revitalization strategy with the aim of understanding how project character, project quality and developer capacity have impacted fund deployment. Though a great American city, Detroit has faced a declining population and dwindling economic base that has resulted in an upside down development market. Projects require complex capital stacks and high levels of subsidies, as rents alone cannot support development costs. The following report provides a review of the lending process and loan portfolios; the evaluations of staff, borrowers, partners and fund investors on the deployment of the funds; and a set of recommendations for current and future work.

Key Findings

- Loans made to date ($47 million) will support 689 housing units, 107,000 square feet of new commercial development, and $122 million in new development.

- The majority of loans have been made to very experienced, high net worth, white developers in Midtown and adjacent areas. This profile is not representative of the diversity of developers that exist in Detroit.

- The only Community Impact Standard that has been achieved on a large scale is the rehabilitation of vacant properties. Few projects have affordable units or are sponsored by minority developers.

- Detroit projects face multiple sources of complexity: 1) developers have varying levels of experience and equity; 2) projects require multiple public and private funding sources due to low market rents, and 3) as an older, industrial city, most properties have some level of environmental remediation that is required. These risks combined result in high standards of underwriting that can be difficult for developers, especially newer developers, to meet.

- A review of all 12 closed loans found that almost no borrowers were able to submit construction plans before the closing phase. Approximately 50% of projects utilized an alternative to payment and performance bonds. Only two projects negotiated reduced guarantees.

- The majority of projects that have been declined by Capital Impact are due to loan or project size.

- Capital Impact has a strong and positive reputation in Detroit. It is perceived to be cautious, risk averse, and similar to a traditional bank, while also gaining praise for its flexibility and willingness to work with local developers.

- Capital Impact’s staff is committed to the place-based revitalization strategy in Detroit, even though it represents a departure from the organization’s previous work.

- Staff is also engaged and committed to the goal of building local developer capacity. Funders, however, did not express capacity building as an objective of the funds.
Recommendations

The recommendations are designed to support Capital Impact in addressing challenges highlighted through the stakeholder and staff assessments, as well as issues revealed in the review of the loan portfolio and developer pool. The recommendations fall into two categories: Strategic and Internal.

Strategic

Capital Impact has an interest in positioning itself as a leader on inclusivity, with a focus on affordability and income mix, and local and minority developer participation. The portfolio review revealed a gap between this inclusive growth framework and the resulting projects. This presents an opportunity to expand Capital Impact’s focus in Detroit to actively include inclusive growth goals in addition to density targets. True progress in these areas will require a stronger development ecosystem as any single actor can only have a limited impact. As a market leader, Capital Impact should consider developing a formal collaboration with other market actors to research and gather support for a new initiative around inclusivity.

- Create a formal collaboration between key partners and set a goal and strategy for inclusivity across the ecosystem.
- Create definitions and metrics for inclusive growth and affordability, and for building minority developer capacity through working groups with funders and financing partners. Operationalize into lending criteria.
- Collect data on minority developer activity and interest
- Create new data-driven products and programs

Internal

These recommendations focus on process and communication modifications that can support current work, and should provide value regardless of Capital Impact’s adoption of the strategic recommendations. The recommendations cover four areas: Research and Analysis, Education, Developer Communication, and Remaining Loan Funds.

- Conduct an internal review of the highest risk projects and workarounds that allowed for approval in order to better understand tolerance and mitigation approaches
- Determine the circumstances under which Capital Impact would allow multiple loans to a developer and explore the implications of those circumstances
- Identify the five most frequent sources and seek to streamline processes through mid-level managers
- Create neighborhood learning opportunities for staff to build familiarity and gain confidence in new geographies
- Improve borrowers’ confidence regarding the stringent underwriting process and likelihood of securing loan
- Shift messaging approach to borrowers with limited experience to combat negative anecdotes
- Prioritize underperforming Community Impact Standards for remaining loan funds
Introduction

In August of 2015, Capital Impact Partners, a national Community Development Financial Institution with a mission to transform underserved communities into strong, vibrant places of opportunity, submitted a project proposal for Massachusetts Institute of Technology Course 11.437 Financing Economic Development. The focus of the proposal was to conduct a review and evaluation of Capital Impact’s Detroit-based funds. In December of 2015, the project proposal was accepted as the basis for a client-based thesis for the author, a Master in City Planning Candidate. The following report provides a review of the lending process and fund portfolios, the evaluations of staff, borrowers, partners and fund investors on the deployment of the funds, and a set of recommendations for current and future work.

Local Context: Detroit, Michigan

Geography + Population

The City of Detroit is Michigan’s largest city in both population and area. Currently the city has a population of 680,250 and a geography that spans 138.75 square miles. It is bordered on one side by the Detroit River, which forms a border between the United States and Canada. The city’s residents are predominantly Black or African American at 82%, while the metropolitan area is 71% White. Detroit is similar to Atlanta, Georgia; Philadelphia, Pennsylvania; and Portland, Oregon in land area and similar populations to El Paso, Texas; Seattle, Washington; and Washington, D.C.

Detroit reached its peak population of 1.8 million in 1950, and until 2000, it was one of the top ten most populated cities in the United States. It is the only U.S. city to reach a population of over 1 million and then shrink below that figure. Population loss is the precipitating factor behind many of the challenges Detroit faces today, including high housing vacancy and a lack of funding for critical city services.

Economy + Government

Detroit has long been known as the Motor City, as home to the “Big Three” U.S. automobile manufacturers: Ford, General Motors, and Chrysler. Like all places across the country, Detroit and Michigan had significant job losses during the Great Recession of 2008-09. Detroit had entered into an economic downturn much earlier as a result of changing dynamics in the automobile industry. Today, employment is increasing in downtown

---

Detroit, and the city has a more diverse economy with health care and financial services companies playing large roles\(^2\).

The State of Michigan appointed an emergency manager for the City of Detroit in 2013 as it faced $18 billion in unfunded debt obligations. The emergency manager forced the City of Detroit to file for municipal bankruptcy, resulted in $7 billion in debt forgiveness and reductions in pension payments to retired city workers. At the end of 2013, residents elected a new mayor, Mike Duggan, who came to the city after serving as the CEO of the Detroit Medical Center, the top employer in Detroit. The bankruptcy ended in December 2014 and the reorganization plan allowed the city to spend additional funds to bolster city services\(^3\).

**Real Estate Market**

Due to decades of population decline, Detroit’s physical infrastructure is outsized for its current population. While Downtown and Midtown areas were impacted, they have fared better due to years of sustained planning and advocacy efforts as well as a concentration of cultural and institutional assets. It is far from a strong market however, as historian and Wayne State Professor George Galster writes in his 2012 book *Driving Detroit*:

"Instead of grandeur, the dominant impression is of abandoned retail stores and immense tracts of empty land occupying what in most cities would constitute prime locations. These glimpses of nothingness from Woodward are but the tip of the abandonment iceberg." (Pg. 35)

Today, thanks in no small part to Capital Impact and the Detroit funds, there are cranes in the air and construction underway. While there has been an increase in activity, real estate still requires complex capital stacks as rents mostly remain below the cost of development. Construction and permanent financing sources are still limited in most neighborhoods, where risk is high due to a lack of demonstrable demand. The majority of development occurring outside of Downtown and Midtown is small scale and completed without financing.

**Capital Impact Partners' Involvement in Detroit**

In 2011, due to its expertise in structuring complex commercial real estate financing transactions in a variety of markets across the country, Capital Impact was invited to participate as the Catalyst Fund’s lending intermediary for Detroit’s Woodward Corridor Initiative (WCI), a Living Cities Integration Initiative site. This work, led by Midtown Detroit, Inc., was focused on bringing density back to the city’s core and encouraging the area’s anchor institutions to live, hire and buy local in order to support existing businesses.

---

\(^2\) The Detroit Economic Development Corporation provides ongoing data on Detroit’s Major Employers.

\(^3\) For a brief but comprehensive review of Detroit’s bankruptcy, Think Progress provides a helpful synthesis: http://thinkprogress.org/economy/2014/11/08/3590576/detroit-bankruptcy-conclusion-numbers/
and residents. The $20.5 million fund was focused on a pipeline of community facilities, charter schools and mixed-use/mixed-income developments that would have catalytic impacts on neighborhood transformation. This work launched in a market place with much greater need than could be satisfied with the existing funds.

Having gained new expertise, knowledge, and comfort in Detroit, Capital Impact established the Woodward Corridor Investment Fund (WCIF) in November 2013. WCIF was capitalized by several local and national entities, including, Prudential, MetLife, Woodward Corridor Investments, LLC and the Max M. & Marjorie S. Fisher Foundation, as senior lenders to the fund, and, Capital Impact, Calvert Foundation and the Kresge Foundation, as subordinate lenders to the fund to bring a total of $30 million in long term, permanent debt financing to the Midtown area. The fund was launched in February 2015. Capital Impact also serves as the servicer and program manager for the fund.

In June 2014, Capital Impact formed the Detroit Neighborhoods Fund (DNF), the purpose of which is to finance mixed use and/or multifamily rental housing, and to finance healthy food projects, in Detroit, Michigan through construction loans, permanent loans and New Markets Tax Credits leverage loans. Capital Impact joined with JPMorgan Chase & Co, to capitalize and launch the fund. As a part of JP Morgan’s $100 million, five-year commitment to Detroit, DNF committed $20 million in senior debt to the fund, and Capital Impact committed $10 million in subordinate debt to the fund. Similar to the WCIF, DNF generally acts as senior debt on mid-size multifamily redevelopments, with a maximum loan amount of $6 million.

In February 2014, the Ford Foundation was approached by Capital Impact to help fill another market gap: financing for predevelopment activities. Ford made a $3 million program-related investment (PRI) in Capital Impact, which allows Capital Impact to provide loans to community development organizations, municipalities, for-profit and non-profit housing developers and other organizations to promote the development of mixed use and mixed income real estate projects that promote density and diversity in the Woodward Corridor area of Detroit, Michigan. Thus, the Ford PRI is used to pay for site and construction plans, conduct environmental review while freeing up developer equity that is required to secure construction and permanent financing.

These funds all compliment Capital Impact’s other nationwide sector lending in charter schools, healthy foods, health care, and dignified aging. While all of these sectors have been financed in Detroit, the multi-family, mixed-use funds formed by Capital Impact specifically for the purpose of revitalizing Detroit, Michigan represent Capital Impact’s first venture into place-based revitalization. With the proceeds of the funds having been almost fully allocated, Capital Impact was interested in a review and evaluation of the place-based strategy and the two loan funds and the related PRI with a focus on how project character, project quality and developer capacity impact fund deployment.

Assessment, evaluation, and adjustment represent a virtuous cycle that helps address two constant questions in community development finance: Are the products and services producing the desired outcomes? What adjustments can be made to be more responsive to
the needs of the community while ensuring the sustainability of the fund? Changing needs in the community may require adjustments to loan terms, service areas, or to the definition of eligible projects. Through a review of loan applications and activity, Capital Impact and its partners can start to understand the gaps and opportunities present in the community.

**Research Focus**

The primary objective of the place-based strategy is re-densification of Detroit’s core in order to bring back and sustain vibrancy, diversity, and opportunity for new and future residents. As a result of its experience with the WCI, Capital Impact and its partners modified WCIF structure to be more responsive to the community; this included higher loan-to-value ratio, longer loan terms, lower debt service coverage requirements, and fixed interest rates for the first 10 years of the loan.

Currently, the demand (as evidenced by loan applications) for Capital Impact’s loans is twice the supply of capital. The demand for Capital Impact’s loans signals that the products are meeting the desires of developers. With a pipeline of projects in place, Capital Impact requested a detailed assessment of the relationship between the lending criteria, the origination and underwriting process and the resulting approved projects. Given the combination of an area with weak market demand and high subsidy needs, and the reality that even mission-driven capital requires projects to produce positive cash flow, this research set out to understand the following questions:

1. **What is the process for origination, underwriting and approval of Detroit projects?**

   Real estate financing in Detroit’s weak market is arguably a difficult task. Between below market rents and degraded building stock, few projects can be financed by a single source. There is also a variety of building typologies, from two-story storefronts to 12 story high rises. Within an environment where standardization seems very difficult, what consistency exists in the underwriting process? Where in the process does variation and customization take place? Do different borrowers experience the process in the same way? If not, along what lines are differences manifested? Are the expectations consistent across the various stages of the underwriting process?

2. **What projects and borrowers have successfully secured funds?**

   Both WCIF and DNF are focused on multifamily rental projects and mixed-use developments, and both funds indicate a desire for affordable units or expanded economic opportunity. While it is beyond the scope of this report to determine if an expansion of economic opportunity has occurred, it will aim to understand who has directly benefited from approved projects and the number of affordable units put on the market.

   There is an internal concern that successful borrowers are not reflective of a city that is 82% African American, and that minority and high-risk borrowers have been less able to access Capital Impact’s loans. A detailed review of projects and applicants will generate
empirically based profiles of successful and unsuccessful projects and developers. This will aim to reveal if there are any systemic barriers to projects or certain types of developers.

3. **How is Capital Impact perceived in Detroit by its borrowers, partners and investors? What changes are necessary, if any, to meet the needs and objectives of Capital Impact and its stakeholders?**

As a relative newcomer to Detroit, Capital Impact is interested in gaining feedback from its stakeholders about both its lending process and directions for the future. While high demand for its loans is one indicator of performance, a more robust understanding of the market ecosystem and Capital Impact’s role will allow it to be more responsive to stakeholder needs and increase its impact and influence.

**Methodology and Data**

A mixed methods approach was utilized in order to answer the above questions regarding the relationship between process, outcomes, and perceptions. This included: inventory and review of Capital Impact’s loan pipeline and approved projects, financial analysis, process mapping, semi-structured interviews, and an online, self-administered survey. Written, published materials, such as press releases and websites, were combined with interviews, loan files, and the results of a developer survey to gain a comprehensive understanding of Capital Impact’s work in Detroit. The following section will outline important details regarding the interviews, loan selection, and developer survey.

**Interviews**

Capital Impact’s Director of the Detroit Corridor Initiative, who initiated the study, was instrumental in identifying and providing connections to stakeholders. Interviews were conducted over the phone and in person between January 2016 and March 2016. Interview guides were developed for each group of stakeholders in order to ensure similar data was collected from each individual. Interview responses were compared within and across groups to identify themes and discrepancies.

*Capital Impact Staff* – Overall, nine Capital Impact staff participated, including two business development staff, 3 loan officers, and four senior managers (two from originations, two from credit). Interviews with staff helped illuminate the stories behind each loan, the challenges and opportunities presented by the lending process and underwriting criteria, and lessons learned about loan performance in the Detroit market. Staff interviews were also used to build a baseline assumption about developer capacity (e.g. cash reserves, debt coverage ratios, etc.) necessary to be eligible for a Capital Impact loan.

*Borrowers* – As the users of Capital Impact’s loan products, the developer perspective is critical in informing an understanding of the functioning of the product, the impacts of modifications, and the potential market for a redesigned fund. Capital Impact staff was asked to provide information on borrowers who they believed could provide insight into the developer experience in Detroit and in working with Capital Impact. The list came from both business development and credit officers. Of the eight developers suggested, four were
interviewed. The sample was a convenience sample based on responsiveness. The goal of the interviews was to understand: the developer’s experience in the lending process, challenges they faced in borrowing from Capital Impact, broader challenges present in the Detroit market, and modifications that Capital Impact could make to better support projects throughout to project delivery and operations. After conducting the interviews, it became apparent that the four interviewees all had professional banking experience, and may not provide the most representative perspective. This recognition was part of the impetus to derive a more diverse perspective through the developer survey.

**Investors** – Given the high demand for Capital Impact’s loans, the organization was also interested in understanding the potential for future funding and tolerance in modifications. While fund investors are not regularly involved in the loan process, the underwriting criteria and credit standards are in part a reaction to the risk tolerance set out by the investors. Understanding their current view on the market and on the role of the funds is especially important on questions of new directions and product modifications. One investor from WCIF and one investor from DNF were identified, and both were interviewed. The interviews were conducted over the phone and in person. There were four main goals for these interviews: identify the purpose and objectives of the funds, provide a review of the process and resulting portfolio, identify areas of strength and weakness with Capital Impact’s process and within the Detroit market, and discuss areas of future work.

**Partners** – Today, between the Detroit funds and balance sheet lending, Capital Impact can play an outsized role in determining what development occurs in Detroit. In the past, Capital Impact relied on local partners in order to quickly understand the complexities of the market, gain insider knowledge, and rapidly build credibility. Detroit deals still require multiple sources, and Capital Impact’s partners are critical to closing the gap and financing deals. Interviews with three partner organizations focused on a review of Capital Impact’s process and products from the co-lender perspective, areas of opportunity and need, and market challenges.

**Loan Files**
Capital Impact’s Detroit loan files were used to build the loan inventory and financial model. Key documents included the triage and underwriting memos, as well as sources and uses statements, and personal financial statements. The objective of utilizing this data was to pull out key information that would allow a comparison across approved and denied projects. For those projects still in underwriting, the most up to date information was used.

**Developer Survey**
As previously noted, there was some concern that the developers interviewed were not representative of borrower experience. An online, anonymous 40-question survey was developed in an attempt to incorporate more data on Detroit developers and projects, and gain additional feedback from those with experience working with Capital Impact. Capital Impact staff circulated the survey to over 300 developers in the Detroit market. After a two-week period, with three reminder emails, the survey yielded 24 responses. Of those, seven were Capital Impact applicants.
The Lending Process

Capital Impact has a four-stage process to evaluate and finance proposed loan applications: deal screening, triage, underwriting, and closing. As a national lender, this process is generally consistent across markets and sectors, although the focus on multifamily rentals in Detroit has shifted the metrics used for evaluation. From initial conversation to closing day, the process should take between 4 to 6 months, assuming the project is adequately finalized and ready for development. Depending on the complexity of the financial structure, the number of funding sources, and the preparedness of the borrower, projects may take significantly longer to close.

Deal Screening + Business Development

The first phase of the lending process is known as deal screening and is primarily conducted by Business Development officers who are local to Detroit. Potential projects come to Capital Impact through three main mechanisms: outreach, referrals, and Capital Impact’s website. Business development officers engage in a variety of outreach and networking opportunities wherein they are promoting Capital Impact and its products. With more than five years in Detroit, Capital Impact has also built a client base and engaged in high-profile deals, resulting in many projects that seek out Capital Impact products directly or through referrals from other borrowers. Finally, Capital Impact sees some borrowers come through their website, where there is information about WCIF and DNF.

Once a developer expresses interest in Capital Impact, the deal screening phase begins. This process generally takes two to three weeks and primarily consists of communication between the developers and the business development officer. The goal is to understand if the proposed project meets the basic criteria of the Detroit loan funds. The threshold criterion concerns the use of the development; it must either be multi-family rental housing or mixed use with a residential component. The other criteria are also important, but more flexible:

- Development Plan/ Size: between 20 and 100 units, but some projects are as small as 6 and others as large as 199
- Cash Flow: initial projected rents in line with Capital Impact’s market experience
- Loan Size: between $1 million and $6 million. Select projects as low as $700,000 have also been funded.
- Geography: along the Woodward Corridor or in one of five target neighborhoods where there is also activity by other funders. Capital Impact has also considered “catalytic” mixed use projects in a new neighborhoods that are expected to jumpstart the revitalization of a neighborhood retail core.
• Existing Site Control: not a grounds for denial, but Capital Impact prefers to become involved once the developer has site control
• Equity: equity contribution of 10% of the total development cost via cash or grants
• Project team: information on development team, including architects and general contractor if known. While Capital Impact prefers to work with developers with experience in Detroit and with multifamily or mixed-use developments, their current portfolio has a range of experience levels that skews toward the very experienced.

In this phase, information is exchanged verbally or via email. Capital Impact limits requests for formal documentation from the developer in this screening phase. Once the business development officer has a strong sense of the project and its current stage, fit within one of the products, and impact, they prepare a screening memo with the pertinent details. The project and memo are then presented to the Director of Lending and Senior Credit Officer. These senior managers verify the fit of the project and assess the capacity of Capital Impact and appetite for the deal. This phase has been described as a “gut check” that reviews the deal before requesting too much of the borrower or investing too much of Capital Impact’s time and resources.

Triage + Originations

Triage is second phase of the lending process, and this phase distinguishes Capital Impact from many other lending processes. This phase is something of a preliminary underwriting and generally takes about four weeks. Similar to other national CDFIs, Capital Impact uses a hub-and-spoke model, where there is an on the ground presence provided by the business development officers in Detroit, but other phases of the process are completed by staff around the country. A loan officer from the originations team is assigned to the project, and begins to cultivate a relationship with the developer. At this point, Capital Impact begins to request written information from the developer, including project pro forma, budgets, other financing or funding, examples of previous developments, and personal or corporate financials.

"In triage, we look at the project budget, more details, cash flow, and try to understand 'Can they afford the debt?'"

The goal of Triage is to understand the project, the developer, and the likely risks and potential mitigation before undertaking a more thorough underwriting. Based on the information provided by the borrower and other market assessments, the Loan Officer will complete a financial analysis of the project, develop the loan structure, and prepare a triage memo. This memo outlines the project, developer experience, potential risks, and makes a recommendation on whether the project should proceed. This information is presented to the Triage Committee, which includes Capital Impact’s Chief Executive Office, Chief Lending Officer, and Chief Risk Officer. If approved by the committee, the Loan Officer provides the borrower with a term sheet for the proposed loan. With the signed term sheet, the borrower must also provide a $10,000 deposit, which is used for third-party expenses incurred by Capital Impact during the underwriting process.
Underwriting + Originations

The underwriting phase builds off the knowledge and information provided during the triage phase. The same loan officer continues working with the project, and information and documentation requirements expand beyond the borrower to other entities. Environmental reviews, property assessments and appraisals come from third party vendors, as well as credit reports on borrowers, personal and corporate. Some proof of funding is also required from other sources. Construction documents and project budgets are also reviewed in detail, and are often adjusted to ensure the required reserves and contingencies are provided. These adjustments can result in financing gaps:

“We are usually trying to increase the flexibility wherever we can, but we have to maintain sufficient reserves to mitigate risk. We can’t move numbers that would impact the credit of the deals. Removing too many safeties isn’t really a good way to fill the gap”

Depending on the risk level of the credit, additional guarantees or additional credit support may also be necessary. This could require developers to find additional funding or project sponsors, which can add time to the process. A target closing date and timeline are set at the beginning of the underwriting phase. Most projects are in the underwriting phase for four to eight weeks. Much depends on the number and nature of the other sources in a project, which can range from grants to subordinate debt to tax credits. As the senior lender in most cases, Capital Impact works with borrower to ensure that other sources fall within Capital Impact’s credit guidelines, making exceptions when necessary. For example, Capital Impact’s guidelines require that subordinate debt does not mature before Capital Impact’s senior loan. Since Capital Impact is some of the most patient capital in the Detroit market, this sometimes requires adjustments and negotiation between the parties.

Based on the information collected and the analyses produced, the loan officer creates an underwriting memo and updated financial model. This memo provides detailed information on the real estate, the borrower, the project, the finalized loan amount and structure, the local market and impact to the triage committee. Since the project has been reviewed before, the committee’s approval is generally concerned with the loan structure, rather than the project. In many cases, senior management has been consulted prior to committee review on any conditions or workarounds that may be out of the ordinary. Once a project is in the underwriting phase, the focus is on the identification of critical strengths and weaknesses that may impact the final underwriting decision; staff and management work together to develop flexible, practical solutions to weaknesses identified during this process as often as possible. The underwriting phase ends with the issuance of a commitment letter to the borrower.
Closing + Closing Team

The commitment letter outlines the final loan amount and terms, and sets out the closing conditions. The loan officer transfers the project to the closing team, which consists of a closing manager and Capital Impact’s legal team. The closing process is the most document heavy of the phases, and many of the documents require some level of negotiation between sources and the borrower. This phase generally can take between four and six weeks. In addition to complications from the coordination of and between all funding and financing sources, delays often result from the preparation of construction plans, general contractor bidding, and securing of permits. In an environment with limited equity and developer liquidity, construction plans are often generated only once there is sufficient confidence that the project will receive financing. Bidding and permitting can only occur once there is a finalized set of construction plans. Title searches, bonding, insurance and construction review all occur during the closing phase as well. The closing occurs once all conditions are met or exempted and all other funding is provided. Once the closing has occurred, the project is transferred to a portfolio loan officer, who handles disbursements, reporting requirements, and compliance with covenants.

Consistency + Variation in the Lending Process

Generally speaking, the four stages indicated above are the same for all loans, regardless of product or market. The level of review is also consistent, regardless of the loan amount, loan position, or fund source. While the stages are the same, there also appears to be a significant amount of variation in the process as well. As Capital Impact staff explained about lending in Detroit:

“Each project is a story, its own unique situation, and we work with our partners and the borrower’s partners to figure out how do we make this one project work. It is not at all formulaic.”

“We always start with the high standards, but it is not always possible to keep them and is not market practice in Detroit. Developers need to continue to do business and financing can't be so restrictive that it deters development.”

Detroit projects seems to be complex for three main reasons: 1) developers have varying levels of experience and equity; 2) projects require multiple public and private funding sources due to low market rents, and 3) as an older, industrial city, most properties have some level of environmental remediation that is required. In other words: developer risk, market risk and property risk. As Capital Impact staff indicated, the standards for risk mitigation in Detroit are high, and because they are not standard practice for all lenders in the area, can be difficult for developers to meet. Newer developers were particularly sensitive to the stringent underwriting criteria, which is likely a result of a steep, and sometimes expensive, learning curve to development in an inverted market.
Capital Impact also performs a number of sensitivity analyses to test the assumptions underlying the financial projections of each development. Through this exercise, Capital Impact identifies how various risks, should they be realized, will impact the health of the project and the ability to repay debt. With that information, they identify mitigations to protect against the risk. Much of the variation in the process seems to come from negotiating and securing risk mitigation through creative solutions on a project-by-project basis. Some reoccurring risk mitigations and workarounds included:

- Limited developer experience mitigated by highly experienced general contractor
- Deferral of plan and cost review to closing phase due to limited developer equity
- Scenario analysis and substantial reserves and contingencies to account for financial impact of weak market, delays, and construction uncertainties from environmental remediation

A review of all 12 closed loans found the following patterns regarding exceptions:

1. Almost no borrowers were able to submit construction plans before the closing phase. The two projects that did submit final construction plans during the underwriting phase were the largest projects.
2. Only two borrowers secured shorter or reduced guarantees. Some less experienced developers received more stringent liquidity restrictions on their guarantee.
3. Developers of all experience levels negotiated for payment and performance bond alternatives. A total of five were approved to utilize a letter of credit in place of bonding.

Risk tolerance and mitigation will be further explored in the section on stakeholder assessments.
Detroit Funds Portfolio

This section provides a catalogue of the projects financed through WCIF, DNF, and Ford PRI, as well as those likely to be funded. It is intended to provide a snapshot of what each fund has accomplished as of March 2016. This empirical assessment will be particularly important as it provides the data on the loans funded, as compared to other sections, which will reveal interpretations and perceptions about the functioning of the programs.

**Figure 1: Comparison of Funds**

<table>
<thead>
<tr>
<th>Detroit Neighborhoods Fund (DNF)</th>
<th>Woodward Corridor Investment Fund (WCIF)</th>
<th>Detroit Predevelopment Fund (DPF) (Ford PRI)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Geography</td>
<td>Woodward Corridor, Midtown</td>
<td>Woodward Corridor, Midtown</td>
</tr>
<tr>
<td>Loan Type</td>
<td>Permanent only</td>
<td>Predevelopment only</td>
</tr>
<tr>
<td>Eligible Projects</td>
<td>Multi-family rental housing or mixed-use; committed take out</td>
<td>Multi-family rental housing or mixed-use; greater than 10 units</td>
</tr>
<tr>
<td>Healthy Food Access</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Maximum Loan Size $6,000,000</td>
<td>$6,000,000</td>
<td>$500,000</td>
</tr>
<tr>
<td>Loan Term</td>
<td>No later than 2029 (~13 years)</td>
<td>No later than 2031 (up to 15 years)</td>
</tr>
<tr>
<td>Amortization</td>
<td>Up to 30 years</td>
<td>Up to 30 years</td>
</tr>
<tr>
<td>DSCR Minimum</td>
<td>1.15</td>
<td>1.25</td>
</tr>
<tr>
<td>Equity Minimum</td>
<td>10% of Total Development Cost</td>
<td>10% of Total Development Cost</td>
</tr>
<tr>
<td>Maximum LTV^</td>
<td>120% Loan to Value</td>
<td>120% Loan to Value</td>
</tr>
</tbody>
</table>

**Overall Impact**

Combined, these three funds have supported over $122 million in development in Detroit across 13 projects. These funds will support at least 689 new housing units, including 96 affordable units, and over 107,000 SF of new commercial development. These figures will only grow as projects supported through the Ford Predevelopment Fund are able to secure financing and come online. Of the $47 million allocated thus far, $8.27 million has supported projects from local community development corporations, and $6.14 million has gone to developers with limited experience.

^ Capital Impact’s Internal Loan to Value Ratio is 90%. While program guidelines allow for higher ratios, Capital Impact must make an exception to its internal underwriting standards if a loan exceeds 90%. The exceptionally high loan to value ratio of 120% is consistent with the expectation that these projects will help transform the market, bringing additional development and higher property values.
Woodward Corridor Investment Fund Portfolio

As of March 2016, there were seven (7) projects in the Woodward Corridor Investment Fund (WCIF), totaling approximately $23.5 million of the $30 million fund. As a permanent loan fund, many of the projects that will eventually be refinanced by WCIF are still under construction or in the process of meeting threshold requirements for refinance. The information below uses the anticipated permanent loan totals for all calculations.

### Project Scale and Location (7 projects)

<table>
<thead>
<tr>
<th></th>
<th>Permanent Loan Amount</th>
<th>Housing Units</th>
<th>Affordable Units</th>
<th>Neighborhoods</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total</td>
<td>23,612,768</td>
<td>246</td>
<td>16</td>
<td>New Center x 4</td>
</tr>
<tr>
<td>Average</td>
<td>3,373,253</td>
<td>35</td>
<td>3</td>
<td>Midtown x 2</td>
</tr>
<tr>
<td>Minimum</td>
<td>1,400,000</td>
<td>12</td>
<td>0</td>
<td>Downtown x 1</td>
</tr>
<tr>
<td>Maximum</td>
<td>6,000,000</td>
<td>58</td>
<td>11</td>
<td></td>
</tr>
</tbody>
</table>

### Project Financing and Costs (7 projects)

<table>
<thead>
<tr>
<th></th>
<th>Permanent Loan Amount</th>
<th>Ratio of Loan to Appraised Value</th>
<th>Ratio of Loan to Total Development Cost</th>
<th>Developer Fee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total</td>
<td>23,612,768</td>
<td>--</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td>Average</td>
<td>3,373,253</td>
<td>59%</td>
<td>54%</td>
<td>6%</td>
</tr>
<tr>
<td>Minimum</td>
<td>1,400,000</td>
<td>40%</td>
<td>39%</td>
<td>0%</td>
</tr>
<tr>
<td>Maximum</td>
<td>6,000,000</td>
<td>84%</td>
<td>88%</td>
<td>13%</td>
</tr>
</tbody>
</table>

### Developer Requirements and Risk Mitigation (7 projects)

<table>
<thead>
<tr>
<th></th>
<th>Reserves to Total Costs Ratio</th>
<th>All Reserves</th>
<th>Ratio of Loan Value to Net Worth</th>
<th>Value of Net Worth</th>
<th>Equity</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total</td>
<td>--</td>
<td>1,561,030</td>
<td>--</td>
<td>121,000,000</td>
<td>--</td>
</tr>
<tr>
<td>Average</td>
<td>3.5%</td>
<td>223,004</td>
<td>154%</td>
<td>17,286,229</td>
<td>32%</td>
</tr>
<tr>
<td>Minimum</td>
<td>1.6%</td>
<td>72,300</td>
<td>7%</td>
<td>350,000</td>
<td>13%</td>
</tr>
<tr>
<td>Maximum</td>
<td>5.5%</td>
<td>459,509</td>
<td>386%</td>
<td>54,000,000</td>
<td>59%</td>
</tr>
</tbody>
</table>

### Equity Sources

<table>
<thead>
<tr>
<th></th>
<th>Developer Experience</th>
</tr>
</thead>
<tbody>
<tr>
<td>Borrower Cash</td>
<td>Limited</td>
</tr>
<tr>
<td>State and Local Grants</td>
<td>Experienced</td>
</tr>
<tr>
<td>Historic Tax Credits</td>
<td>Very Experienced</td>
</tr>
<tr>
<td>Deferred Developer Fee</td>
<td>Experienced CDC as developer or partner</td>
</tr>
</tbody>
</table>

---

5. This figure is somewhat misleading, as the personal guarantees are project by project, not portfolio wide. Minimum and Maximum are rounded figures.
DATA NOTES

Reserves to Cost
This is the percentage of the total development cost that is allocated to project reserves. These figures include lease-up, replacement, operating, and interest reserves as outlined in the most recent budgets. This does not include construction contingencies. The purpose of this calculation is to understand how reserves are used as risk mitigation.

Loan Value to Net Worth
This is a percentage of the total personal net worth that could be claimed by Capital Impact if the loan were to go into default. Full and unconditional guarantees are required from each and every entity or individual with more than a 20% stake in the borrower. The purpose of this calculation is to understand the risk created by a project to the borrower’s financial standing. Capital Impact has indicated that it sees guarantees as a distant source of repayment, after cash flow from rents and property resale value.

There are several interesting takeaways from the current portfolio.

Loan to Value: while the program guidelines allow for up to 120%, the maximum is at 84%, and the average LTV is 59%, half of the allowable cap. The chart also shows that across projects, the Loan to Value is relatively close to the Loan to Total Development Cost figure. This indicates that there are not large differences between the appraised value and the cost of redevelopment. This points to the strengthening of the Midtown market and the availability of comparable developments.

Affordable Units: the program guidelines state that projects with an affordability component are to be shown preference. Of the seven projects, only two include set aside affordable units for a total of 16 new units, or 6.5% of the units financed through WCIF.

Loan to Net Worth: a closer look at this ratio reveals a bi-modal trend; three projects have loans that equal less than 20% of the developers’ total net worth, while the other four projects have a total net worth that is less than half the value of the loan. These higher risk loans tend to be small and to less experienced developers, or to developers with community development corporation (CDC) involvement.

Equity contribution across projects: the average equity injection is three times the minimum required contribution, and in at least one case, the equity accounts for almost 60% of the project. A large number of projects also utilize Historic Tax Credits, which indicate added complexity from both a financing and construction perspective.

Taken in sum, these results show the picture of many extremely financially strong and experienced borrowers who are able to provide significant guarantees through personal net worth and secure multiple sources of funding.
Community Impact Standards

The following standards are part of the Woodward Corridor Initiative Fund Underwriting Guidelines:

*Eligible Borrowers include multifamily rental housing and mixed-use facility developers with projects located within the Woodward Corridor boundaries. Preference is given to projects that make at least 20% of units available to people with low and moderate incomes. In addition, preference is given to projects that most meet the community impact standards set by the Fund's Community Impact Committee. Projects with high Community Impact Standards could include:

- Proximity to public transit
- Situated in a visible and/or critical location along Woodward Corridor
- Rehabilitate formerly vacant or otherwise blighted property
- Utilizing a minority developer or a developer of color
- Provide over 20% of the project units are affordable to residents living at or below 80% AMI
- Provide over 50% of the project units are affordable to residents living at or below 120% AMI

According to Capital Impact staff, the Detroit Neighborhood Fund is basically identical to the Woodward Corridor Initiative Fund in its underwriting criteria, with the exception of geography. The following chart provides an assessment of how all projects that have received any of the Detroit loan funds compare to the standards. While funded projects have excelled in reutilizing vacant building, the majority of projects have not achieved any other impact standard.

<table>
<thead>
<tr>
<th>Community Impact Standards</th>
<th>Projects</th>
</tr>
</thead>
<tbody>
<tr>
<td>Situated in a visible and/or critical location along Woodward Corridor</td>
<td>4 of 16</td>
</tr>
<tr>
<td>Rehabilitate formerly vacant or otherwise blighted property</td>
<td>15 of 16</td>
</tr>
<tr>
<td>Utilizing a minority developer or a developer of color</td>
<td>2 of 16</td>
</tr>
<tr>
<td>Provide over 20% of the project units that are affordable to residents living at or below 80% AMI</td>
<td>2* of 16</td>
</tr>
<tr>
<td>Provide over 50% of the project units that are affordable to residents living at or below 120% AMI</td>
<td>1* of 16</td>
</tr>
</tbody>
</table>

*Described in underwriting as "affordable" but do not necessarily have future rent restrictions in place
Detroit Neighborhoods Fund

As of March 2016, there were six projects in the Detroit Neighborhoods Fund (DNF), totaling approximately $24 million of the $30 million fund. As a construction to permanent loan product, the loan will roll over without a sale and secondary closing as under WCIF.

### Project Scale and Location (6 projects)

<table>
<thead>
<tr>
<th></th>
<th>Permanent Loan Amount</th>
<th>Housing Units</th>
<th>Affordable Units</th>
<th>Neighbors</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total</td>
<td>23,654,000</td>
<td>443</td>
<td>80</td>
<td>Midtown x 3</td>
</tr>
<tr>
<td>Average</td>
<td>3,942,333</td>
<td>74</td>
<td>13</td>
<td>Northwest x 1</td>
</tr>
<tr>
<td>Minimum</td>
<td>710,000</td>
<td>3</td>
<td>0</td>
<td>Woodbridge x 1</td>
</tr>
<tr>
<td>Maximum</td>
<td>12,700,000</td>
<td>199</td>
<td>80</td>
<td>West Village x 1</td>
</tr>
</tbody>
</table>

### Project Financing and Costs (6 projects)

<table>
<thead>
<tr>
<th></th>
<th>Permanent Loan Amount</th>
<th>Ratio of Loan to Appraised Value</th>
<th>Ratio of Loan to Total Project Cost</th>
<th>Developer Fee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total</td>
<td>23,654,000</td>
<td>--</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td>Average</td>
<td>3,942,333</td>
<td>76%</td>
<td>72%</td>
<td>4%</td>
</tr>
<tr>
<td>Minimum</td>
<td>710,000</td>
<td>65%</td>
<td>59%</td>
<td>0%</td>
</tr>
<tr>
<td>Maximum</td>
<td>12,700,000</td>
<td>98%</td>
<td>100%</td>
<td>11%</td>
</tr>
</tbody>
</table>

### Developer Requirements (5 projects)

<table>
<thead>
<tr>
<th></th>
<th>Reserves to Cost</th>
<th>All Reserves</th>
<th>Ratio of Loan Value to Net Worth</th>
<th>Value of Net Worth</th>
<th>Equity</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total</td>
<td>--</td>
<td>1,996,601</td>
<td>--</td>
<td>88,219,300</td>
<td>--</td>
</tr>
<tr>
<td>Average</td>
<td>8%</td>
<td>399,320</td>
<td>29%</td>
<td>17,643,860</td>
<td>22%</td>
</tr>
<tr>
<td>Minimum</td>
<td>5%</td>
<td>68,903</td>
<td>10%</td>
<td>6,000,000</td>
<td>0%</td>
</tr>
<tr>
<td>Maximum</td>
<td>17%</td>
<td>1,258,602</td>
<td>52%</td>
<td>40,000,000</td>
<td>41%</td>
</tr>
</tbody>
</table>

### Equity Sources

<table>
<thead>
<tr>
<th>Source</th>
<th>Number</th>
<th>Experience</th>
<th>Developer Experience</th>
</tr>
</thead>
<tbody>
<tr>
<td>Borrower Cash</td>
<td>5</td>
<td>Limited</td>
<td>1</td>
</tr>
<tr>
<td>State and Local Grants</td>
<td>2</td>
<td>Experienced</td>
<td>2</td>
</tr>
<tr>
<td>Historic Tax Credits</td>
<td>3</td>
<td>Very Experienced</td>
<td>3</td>
</tr>
<tr>
<td>Deferred Developer Fee</td>
<td>1</td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>No Equity</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

---

6 Loan to Value and Loan to Cost exclude project where only subordinate debt was provided.
7 Project reserve information was unavailable for one project. A separate project did not yet have Personal Financial Information on Guarantors.
8 This figure is somewhat misleading, as the personal guarantees are project by project, not portfolio wide. Minimum and Maximum are rounded figures.

---

24 | Density and Diversity: Evaluating Place-Based Revitalization in Detroit
In the above summary, some interesting trends are revealed.

**Loan to Value:** while the program guidelines allow for up to 120%, the maximum so far is 98%, and the average LTV is 80%, which is 2/3 of the allowable cap. The chart also shows that across projects, the Loan to Value is relatively close to the Loan to Total Development Cost figure. This indicates that there are not large differences between the appraised value and the cost of redevelopment. Appraised values are likely to decrease as the fund supports more projects in newer geographies, while costs will likely remain the same.

**Affordable Units:** with a 100% affordable project financed through the fund, the portfolio achieves approximately 25% of its units as affordable.

**Project Size** represents another interesting variable for DNF; housing units range from 3 to 199. Developments actually represent three distinct clusters: two projects with less than 10 units, three projects with between 58 and 96 units, and one project with 199 units. This indicates that half of DNF loans are outside the desired project size.

The intersection of **Equity** and **Loan to Net Worth** across projects: while compared to WCIF, the equity share is lower; the loan to guarantee represents projects that provide high levels of guarantees and therefore better security for the loan. This may be due to smaller loans under DNF.

In sum, these results point to guarantors who are financially strong but borrowers who are less liquid.

**Detroit Predevelopment Fund**

To date, the Detroit Predevelopment Fund has closed five loans for $500,000 each. All five loans have gone to very experienced developers. Two of the loans have supported CDCs and another two have also received permanent financing through WCIF or DNF, as originally intended. The three projects that are in the predevelopment phase range from 22 units to 102 units. All five projects are in or adjacent to the Midtown neighborhood.
Developer Profiles

As seen through the summaries of each loan fund, there is a wide range of projects that have successfully received financing. Reviewing all projects together reveals three distinct profiles for successful developers.

Capital Impact’s Developer Pool

To date, $47 million (79%) has been allocated from the $60 million available through the Woodward Corridor Initiative Fund and Detroit Neighborhoods Fund.

Experienced and Well-Capitalized | 6 Projects – 55% of total funds
Developers fitting this profile have completed many projects in Detroit, can provide high levels of guarantees, and are undertaking projects that are large scale, catalytic or prominent in nature. Loans range from $2.5 million to $12.7 million, and equity contributions are primarily between 30 to 50%.

Small Scale | 5 Projects – 10% of total funds
Developers in this profile have a wide range of experience and capitalization. The loan size is between $1 and $1.5 million and projects have a small or simple scale of the redevelopment. Among these developers, equity increases as guarantees decrease. Developers with more experience tend to provide less equity but significant guarantees. Developers with less experience had an experienced general contractor or consultant on the project.

CDCs | 2 Projects – 14% of total funds
Projects led or supported by community development corporations are sufficiently different from the sole and joint partnerships to merit their own category. Guarantees are generally low, and the Loan to Value Ratios are below 50%. CDCs almost exclusively take on the provision of affordable units.
Unsuccessful Developers

Based on the information provided by CIP on rejected projects, the most common reasons were loan size and project size. In some cases, deals were deemed to be “too small” and attached to an inexperienced developer. Of the 25 cases provided, only one was rejected solely because of developer capacity. CIP also turned down several projects from developers that already had an active project under their financing.

Denied Deals by Cause

As seen from the pipeline assessment, there are several smaller projects and loans that have been successful. It is conceivable that these rejections were the result of poor timing; CIP has only recently gained sufficient comfort in the market to do smaller deals. It is also worth noting that CIP’s smallest projects are mixed-use residential developments rather than small scale multifamily only.

In order to better understand the landscape and magnitude of eligible and ineligible projects and developers, a survey was created and circulated. The results are discussed in the following section.
Detroit Developer Pool

An online, anonymous 40-question survey was developed in an attempt to gain more data on Detroit developers, active projects, and financing strategies. The survey was shared with over 300 developers and commercial property owners in Detroit, and yielded 24 responses. This section compares the survey results with the profiles of CIP’s developers.

Projects

Developers were involved in a range of project types. Of the 24 respondents, 10 were involved in multifamily residential or mixed-use projects with a residential component. Six were involved exclusively in commercial development. Respondents that had other employment obligations (i.e. part time developers) were primarily involved in commercial projects and 1-4 unit single-family homes.

Developers were asked to describe two active projects in the city. Half of the projects described were non-residential developments, and another quarter were described as 1-4 unit developments. Of the 48 projects described by developers, only five meet CIP project focus of multifamily rentals between 20 - 100 units. These five projects are being carried out by three developers.

<table>
<thead>
<tr>
<th>Projects by Unit Count</th>
<th>Number of Projects</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 Units</td>
<td>24</td>
</tr>
<tr>
<td>1-4 units</td>
<td>13</td>
</tr>
<tr>
<td>4-10 units</td>
<td>3</td>
</tr>
<tr>
<td>10-20 units</td>
<td>3</td>
</tr>
<tr>
<td>20-50 units</td>
<td>2</td>
</tr>
<tr>
<td>50-100 units</td>
<td>3</td>
</tr>
</tbody>
</table>
Who are Detroit’s Developers?

These charts provide comparison of developer characteristics of those with eligible projects and ineligible projects to the characteristics of Capital Impact’s funded projects. Eligibility refers to project type. Eligible includes only developers involved in multifamily and mixed-use projects per Capital Impact’s current products. Data is based on Survey Results and Funded Projects.

* Net worth information was not provided by 5 eligible developers and 2 ineligible developers. CIP Developers net worth is an average of all individuals involved in borrowing entity.
**Structure**

Across the board, the majority of developers in Detroit appear to be small entities formed for the purposes of specific development projects. Sole proprietors and joint partnerships rely on individual financial health and capacity to secure financing and support development activities.

**Experience**

As previously noted, Capital Impact’s financing has primarily gone to experienced developers with a track record in Detroit. The greater developer pool is significantly less experienced among ineligible developers, and slightly less experienced among eligible developers. Of the eligible developers, 15% did not seek financing, citing reasons such as: “the answer is always no”, and “speed, terms and availability”. These respondents were part-time developers and engaged in small mixed-use projects with less than 3,000 SF and 1-4 units. These results do demonstrate that there is a large market of developers with limited experience who likely need technical assistance and capacity building to participate in larger scale projects.

**Net Worth**

Net worth in both eligible and ineligible developers showed relatively even spreads, so there does not appear to be a capitalization gap among developers surveyed. What is striking is the vast difference between the eligible group and the funded group, where 92% of developers receiving Capital Impact financing are higher net worth developers.

While developers at all levels of net worth were undertaking all types of projects, lower net worth developers (under $500,000) were more likely to be engaged in smaller projects. Lower net worth developers almost exclusively had completed five or less projects, categorizing them as limited experience. Higher net worth developers showed a range of experience. This indicates that net worth and financial capacity can and does act as a substitute for experience.

**Race and Minority Participation**

Minority developers and white developers are participating in the same types of projects. From the survey set, there does not seem to be a barrier of minority exclusion. While there is limited set of respondents who included data on net worth, they show that there is similar variation in net worth between minority developer and white developers. Across all project types, minority developers reported seeking financing at a slightly lower rate than white developers.
Capital Impact does have less minority involvement than the market overall. Minority exclusion could become a larger issue as funds are deployed into weaker market segments where anecdotally, there are more active minority developers, but with less experience. Specifically, Capital Impact should review the issue more carefully as it looks at the interaction between net worth, experience and minorities.

The trend within the Detroit loans has been for the majority of funds to support higher net worth developers. The high level of personal guarantees may pose a challenge for expanding the developer pool. It is important to remember that efforts to improve Midtown have been ongoing for 30 years, and that the strong level of assets and experience is unlikely to be present elsewhere in Detroit. Since Capital Impact is committed to new geographies, it must carefully consider how certain requirements and restriction could be prohibitive and hinder goals around capacity development.

**Financing Challenges**

Of the eligible developers, 15% did not seek financing, citing reasons such as: “the answer is always no”, and “speed, terms and availability”. These respondents were part-time developers and engaged in small mixed-use projects with less than 3,000 SF and 1-4 units. These results do demonstrate that there is a large market of developers with limited experience who likely need capacity building support and technical assistance.

There was also an expression of the difficultly in securing loans for “neighborhood development”. Other partners also indicated they are seeing primarily small projects and limited experience developers as they move into new geographies away from Midtown and Downtown.

This presents a marketing and framing challenge for Capital Impact, who needs to be explicitly clear on precisely what type of development is eligible. It also affirms what others have expressed, which is the need for a vision, strategy, and products for the small-scale development that at one point made up of 68% of Detroit’s housing stock. While this challenge is not Capital Impact’s alone, it is an opportunity to collaborate with others and work towards a future that is inclusive of all of Detroit.
STAKEHOLDER ASSESSMENT

Nine stakeholder interviews, with borrowers, partners (co-lenders), and investors/funders were used to assess the perception and performance of Capital Impact in the Detroit market. The interviews, in conjunction with the responses to the developer survey, were compiled and analyzed. Four crosscutting themes were revealed:

1. The majority of stakeholders are pleased with Capital Impact and the role it is filling in the market. Capital Impact is seen as a good partner and market leader, a fair lender, and as making safe and strong investments.

Partners appreciate that Capital Impact is open to many projects, but has also set clear and consistent parameters around project type. As one partner said, “You don’t need to offer everything to everyone. You have to focus on what makes sense based on your funding sources and risk tolerance, and figure out how you can be effective in the market and leverage your resources.” Developers and partners alike praised Capital Impact for coming into a difficult market and moving development forward. Funders indicated satisfaction with the portfolio thus far, and could not recall any deals they felt were problematic or too risky.

2. Stakeholders perceive Capital Impact’s process and standards as close to a traditional bank, cautious and risk averse, but also acknowledge that Capital Impact also has made attempts at flexibility in within its risk profile.

This has been somewhat verified by staff indications that Capital Impact operates with higher standards than those to which the market is accustomed. One partner sees the amount of risk mitigation required as hurting the ability to fill gaps in the market. One third of Capital Impact borrowers surveyed² believe Capital Impact is too cautious and see the underwriting conditions as difficult to meet. They argue that the level of risk mitigation is costly—in resources and time—in proportion to the likelihood of that risk. The following requirements were mentioned as challenging: level of reserves, third party review of appraisal, and high level of guarantees. Other borrowers lack confidence in the process and the high level of standards, causing them to attempt to secure as many exemptions as possible, leading to longer transactions. A small percentage of developers acknowledge the requirements as protection for both the lender and the borrower.

² This is based on both interviews and survey results from developers who have applied to or secured financing from Capital Impact.
Some developers and partners pointed to Capital Impact’s nationalized underwriting structure as a driver for some of the risk aversion. The satellite nature of the organization was pointed to as causing delays in underwriting, adding tension to the market place, and causing borrower insecurity.

"If your decision makers are outside, the decision makers rely on the boots on the ground, and even if the people on the ground advocate for a project, getting to that final commitment can still be hard. I felt like we had it; but I wasn’t sure that we were going to get the loan commitment."

"When you have a centralized underwriting process where people don't know the market players, it can create tension when the underwriting process is not fully informed by the relationships on the ground."

Others discussed Capital Impact’s work on strengthening the capacity of minority developers in the market, as well as trying to make deals work even if they don’t meet every requirement or condition as a sign of their flexibility and commitment to the market:

“They still have to be careful around underwriting, but willing to work with homegrown developers who may not have a big balance sheet. They will overlook some of the more stringent underwriting criteria that can make it really difficult for small, and especially minority developers, to get in to business. So that has been a huge benefit of them being here in the market.”

Some developers acknowledged Capital Impact as flexible and open to arguments of why conditions may not be necessary. As a stakeholder group, there were a variety of perspectives on what modifications would be desirable. Two mentioned the high reserve requirements; another discussed insurance and bonding requirements in light of project size; still others mentioned high guarantee levels. Since there is not a single, systematic requirement or condition that is challenging, one partner concluded that Capital Impact’s approach is completely appropriate:

“There is a reason each of these deals has to be custom. Even if they take the typical exceptions and include it in the program design, I guarantee you there will be another set of exceptions that come up. But if they can recognize those, have a strategy to manage them, and continue to tweak the model, that would be great.”
3. Most stakeholders agree that Detroit is an especially complicated place for development due to the weak market, and are concerned about the future of the city’s recovery.

Stakeholders are in agreement that market rents are low and that much of the risk mitigation that is required is a result of that condition. This demonstrates a level of sophistication in developers who recognize the challenges present in the entire ecosystem. While there are indicators from funders that they want to see more movement, their primary metric for success, at least in the long term, is the ability to exit. As stated by one investor, a successful fund will be demonstrated by the ability to exit at year 15:

"The risk in these funds is about market recovery. While strong underwriting is important, project and program success is really dependent on growth in the market. "How can we better ascertain those early market indicators?"

In addition to ensuring strong credits, this indicates the need for Capital Impact to think more about the overall market. The return of traditional capital to some areas is one indicator of the strengthening market. With that, investors want to see Capital Impact be nimble and reactive to ensure they continue to fund the projects that others won’t:

"Capital Impact needs to continue to reassess the market and ensure the cost and terms of the funds are just restrictive enough to be slightly less attractive to developers who have other options. "

Funders and a few developers also agree that progress has been slow. This has two elements: fund deployment and project financing. Funders note that allocation of the Detroit funds has moved more slowly than desired, while acknowledging that some of the pace is due to a lack of shovel-ready projects. Some developers indicate that the process for securing financing is long and costly due to requirements that are difficult to meet or require negotiation of alternatives.

4. There are still many market gaps, and a variety of possible avenues for Capital Impact to extend its involvement in the market place.

As one developer described, the Detroit market is so open that there is a need, and the opportunity, for everything. While no single gap was unanimously identified by stakeholders, the need for small project financing was noted by approximately 50% of those interviewed and surveyed. Small-scale multifamily buildings of four to eight units, as well as loans under $1 million were specifically identified. As one investor stated:
“The reality is that there are not enough 50-units developments to come close to getting us back to what we need in terms of a population base. We have to bring back the small 4 to 8-unit split flats, otherwise we are never going to get there. In other cities, it is pure equity that finances these 4 and 8 units buildings, or in some cases, a community bank. Neither of those will work in Detroit, so the funding community is going to have to get in there.”

Large project financing, between $10 and $15 million was also identified by a few developers and partners as a need that a national entity with local knowledge, such as Capital Impact, could help fill. Many of these stakeholders also discussed the need for Capital Impact’s funds to be eligible for projects downtown.

Approximately a third of developers indicated the need for more subordinate debt, as well as a product that required lower guarantees. As one developer noted:

“There are systemic problems in the market that precludes smaller, private-led developers to make a living and build a team to focus full-time on the endeavor. This is why the city is being developed largely by individuals with net worth’s north of eight figures. Beyond needing cash to acquire properties, 100% of the bank financing sources require liquidity and net worth that is unreasonable for most people”

Of the 13 projects that Capital Impact has approved for financing, 30% have guarantors or developers with a personal net worth of over $10 million; 50% have a personal net worth or corporate asset balance of over $1 million.

Working capital for small developers is another market gap noted by partners for exploration. There is also a desire for Capital Impact, as a national entity, to aggregate funds for community amenities that add vibrancy and value, but are often left out in a market that already requires complex capital stacks.

“Capital Impact could help aggregating grant funds from national players for “soft tissue” stuff, like community gardens or pocket parks. It is so hard to get a project funded in Detroit that there is no money left to do something interesting, especially doing amenities that are on a neighborhood level. Initiatives that create shared spaces. It is the stuff that helps keep people here.”

This proposal identifies one avenue by which Capital Impact can begin to support efforts outside of the individual project level that help rebuild the market at large.
STAFF ASSESSMENT

Nine interviews with senior managers and loan officers were used to assess the perception and operations of Capital Impact’s Detroit funds, in conjunction with written materials about the funds. The interviews were compiled and analyzed using a SWOT (Strengths – Weaknesses – Opportunities – Threats) framework. Where appropriate, the results also include responses to the stakeholder findings.

Strengths

Staff was in agreement that the primary goal of the Detroit work is to increase density across a mix of incomes. While this may seem basic, it is an important finding given that the Detroit work is a departure from Capital Impact’s typical sector-based lending focused on underserved communities. As one senior manager put it:

“This work is more tangential in its benefits to low-income people. There is such a high level of poverty in the city that we need to do mixed income projects that attract people who don’t require subsidized housing, because that is the only way that the services that are so important to the city are going to exist.”

In the beginning, some loan officers struggled with this market-rate focus. Through experience and internal communication, today, there is both understanding and excitement about the strategy. For developers, this translates to a committed staff with a willingness to make deals work.

Notwithstanding the market reality within Detroit—which compels some investment in market rate projects—staff expressed a continued commitment to supporting underserved communities consistent with Capital Impact’s mission. In Detroit, this is manifested as a desire to ensure that Capital Impact is supporting local and less experienced developers and helping build market capacity. While the goal of building local capacity is widely shared, it is not formalized in any of the program statements or underwriting criteria.

Finally, there is wide spread agreement that the deal screening phase has been a useful addition to the process. Many loan officers acknowledged that they haven’t seen any bad deals, thanks primarily to the work of the business development team.
Weaknesses

Some staff expressed similar, but more nuanced, frustrations with the underwriting criteria and process as described by some developers. There was a belief that there was room to formalize some of the flexibility and adjustments that were continuously made, which could, in turn, improve communication to borrowers and further improve Capital Impact’s response times.

While there is agreement around the density goal, interviews and written documentations demonstrated a lack of metrics outside of density and financial soundness. There was some discussion of “catalytic projects”, but no criteria for how that should be defined. While both funds also discuss impact, as seen in the community impact standards in the Detroit Funds Portfolio section, there is no prioritization of these impacts or operationalization of them across the portfolio. As a result, a developer’s ability to “sell” a project may have an outsized influence, and there is a greater reliance on interpretation in the evaluation. As shown in the portfolio review, there are also wide interpretations of density when applied to mixed-use projects.

While staff was in agreement on their interest in supporting more local developers, not all staff felt equally confident about moving away from the Woodward Corridor into other neighborhoods. There is a confidence and familiarity with Midtown that does not exist with other geographies. This may lead to more caution and risk mitigation in underwriting DNF developments.

Opportunities

Many staff members expressed an interest in connecting with and integrating the research work conducted through the Detroit Corridor Initiative. The Detroit Corridor Initiative (DCI) was a strategic cross-sector partnership that worked to accelerate economic opportunity and create quality mixed-income districts and job growth in Detroit. DCI’s research work focused on understanding and identifying potential areas for “inclusive growth”, or development that increases density and provides for a healthy income mix at the neighborhood scale. DCI produced a 2015 report that looked at population dynamics and income mix in Detroit’s mixed use corridor areas. This interest also indicates that there are mechanisms inside the organization for building more familiarity and confidence outside of the Midtown market.

Some of the stronger critiques of Capital Impact’s requirements and conditions came from developers with limited experience, with small projects in new geographies. These developers tended to believe that as a CDFI, Capital Impact should be willing to take on more risk than a traditional bank, without completely acknowledging that all of Detroit—much less small projects—was without significant traditional bank activity. This indicates that a different communication strategy may be needed for projects that do not meet many of Capital Impact’s initial criteria if the organization intends to continue to finance these types of developments.
As a senior lender on many of the projects occurring in Detroit, Capital Impact is well positioned to take on a leadership role in the market to improve ecosystem and streamline complex capital stacks. Almost every staff member spoke about the complexity of Detroit projects, with two recurring external challenges: developer capacity and preparedness, and coordination and negotiation of multiple sources of funding. According to staff, developer delivery of construction plans and insurance were two recurring sources of long delays. Many loan officers also mentioned that internally, it was their goal that the process be borrower driven with quick turn around so that borrowers were never “waiting” on Capital Impact. If Capital Impact is already striving for fast internal response times, it may be appropriate to work with other common sources to find possible process improvements that will allow deals to move more quickly.

**Threats**

The primary threat to Capital Impact’s work is a seeming misalignment between additional programmatic goals and the stated interests of funders. Many staff members expressed a concern about gentrification and an interest in financing projects with more affordable units and supporting local and minority developers. While there was widespread interest in these additional goals, there were no clear metrics included in the screening or underwriting processes to recognize and track projects that would support these goals. Although affordability targets are included in the written program materials, investors did not acknowledge the targets are a defining feature of these funds. Investors had no discussion of local and minority developer capacity building as goals for the funds. This disconnect points to the need for further discussion with funders about these goals, as well as metrics that allow the goals to be operationalized in the approval process.
Recommendations

The following recommendations are designed to support Capital Impact in addressing challenges highlighted through the stakeholder and staff assessments, as well as issues revealed in the review of the loan portfolio and developer pool. The recommendations fall into two categories: Strategic and Internal.

STRATEGIC

Based on this review, interviews, and program information, it is clear that Capital Impact has an interest in positioning itself as a leader on inclusivity. Thus far, the inclusive growth framework has focused on affordability and income mix, and local and minority developer participation. The portfolio review revealed a gap between the inclusive growth framework and the resulting projects. This presents an opportunity to expand Capital Impact’s focus in Detroit to actively include inclusive growth goals in addition to density targets.

True progress in these areas will require a stronger development ecosystem as any single actor can only have a limited impact. As a market leader, Capital Impact should consider developing a formal collaboration with other market actors to research and gather support for a new initiative around inclusivity. The following recommendations identify the key next steps and considerations for ultimately increasing the inclusivity of the entire development ecosystem.

Set a goal and strategy for inclusivity across the ecosystem

First, Capital Impact must determine if it is willing to play a role in strengthening the system. If so, Capital Impact needs to develop a goal and strategy in collaboration with its funders and financing partners for building minority developer capacity and achieving income mix across neighborhoods. This strategic initiative will require that someone from Capital Impact in Detroit be empowered to lead conversation, make commitments to local partners, and guide the strategy.
Create definitions and metrics for inclusive growth and affordability, and for building minority developer capacity through working groups with funders and financing partners. Operationalize into lending criteria.

As seen in the threats section, funders are not focused on questions of displacement. While affordability targets are set up in the program descriptions, it is not clear if there are goals across the portfolio or how affordability ranks among other goals. It is important for Capital Impact to create a robust vision around this in conjunction with its funders and project financing partners.

Funders are also not clear participants in Capital Impact’s work to build minority developer capacity. Although utilizing minority developers is part of the Community Impact Standards, it is not clear if there are goals across the portfolio or how work with minority developers ranks among other goals. While partners praised this work, it is at risk of being marginalized without a clear strategy and mechanism for communicating its importance.

Collect data on minority developer activity and interest

While the developer survey conducted for this report did not show the exclusion of minority developers in mixed-use and multifamily developments, Capital Impact does have less minority involvement than what is seen across the market. In order to understand barriers to financing or participation in larger scale development, better data is needed. At this point, there is only anecdotal information on minority developers or contractors who are wish to take on larger projects, but face limitations, such as: access to acquisition and pre-development capital, packaging and securing financing for their first large project, or experience and expertise limited to redevelopment of 1-4 unit properties.

In order to design programs, technical assistance, and financing to support minority developers in scaling up, Capital Impact and other partners need to collect and share data on: geography, project size, previous development experience, expertise (construction, community development, finance, etc.), and potential problem areas for current loan programs (equity, guarantee, etc.). Analyzing this data across all lenders and organizations will create an understanding of the size and distribution of minority developers, and allow capacity building efforts to focus on solutions that will have the largest impact. Capital Impact also needs to monitor data sources to prevent over and under representation of areas that might bias results.
Create New Data-Driven Products and Programs

As seen in the stakeholder assessment, there isn’t consensus about what is needed in the market. Each stakeholder group provides multiple directions on what other roles or products Capital Impact could provide to the market. With a goal of creating a more inclusive market, Capital Impact and its partners should use a data driven approach to determine new products and programs that will address barriers to affordability and minority developer participation.

If developer inexperience is the challenge, the initiative might consider agreeing to common underwriting criteria, packaging financing around an agreed-to agenda, or common applications for all partners as steps that can help reduce complexity for the developer. Promoting joint ventures with more experience developers, architects, and contractors is another option that Capital Impact has previously used to mitigate developer inexperience.

While the following needs to be confirmed through additional market data, there is a perception that there are many minority developers who have experience with redevelopment of 1-4 unit buildings, and are interested in scaling up. There is a need for an entity that is willing to fund the first larger scale project. Capital Impact, or a collaborative of local financing organizations, might consider a small projects fund as a precursor that would allow developers and lenders to establish a working relationship and track record. However, with a smaller scale of projects, the number of eligible projects will likely increase significantly, and therefore it will be necessary to include additional parameters beyond minority developers—such as higher affordable set asides, green building or energy efficiency, or specific neighborhoods—in order to focus limited resources.

Key Partners
Invest Detroit, Detroit Economic Growth Corporation, IFF, City Departments (Buildings, Housing and Revitalization, Detroit Building Authority)

Start off with partners that expand across geographies to set strategy and priorities. While it will be important to engage with more focused organizations, especially when it comes to data collection, Capital Impact needs to initially limit those with very specific agendas in order to ensure that your strategy is data driven.
INTERNAL

These recommendations focus on process and communication modifications that can support current work, and should provide value regardless of Capital Impact’s adoption of the strategic recommendations.

Research and Analysis

Conduct an internal review of the highest risk projects and workarounds that allowed for approval

As a separate attachment, the researcher will provide a list of high risk projects based on the intersection between equity, guarantees, size and experience. This can act as a starting point for review, as negotiations around requirements and alternatives were difficult to recreate from the finalized loan files. Based on the developer interviews, it seems possible that persistence, familiarity with finance, and preparedness played a role in a risker project securing financing, but that does not come through in the documentation. It will be especially important to look for unconscious biases, such as persuasiveness, that played a role in moving higher risk projects. This review should aim to understand what risks were unacceptable, what risks were tolerable, and what risks had to be mitigated. Once there is an awareness of how these risks are perceived, there can be additional attention given to consistent application of tolerance and mitigation.

Determine the circumstances under which Capital Impact would allow multiple loans to a developer and explore the implications of those circumstances

The logical progression of building developer capacity is developers with multiple projects. So far, the majority of developers in the Detroit funds have been higher net worth individuals with guarantees that exceed the loans. Given that the funds are for permanent financing over many years, Capital Impact needs to explore and understand its interest in allowing current borrowers to conduct further development. This is especially important for those lower net-worth developers who have pledged full guarantees.

Capital Impact has indicated that it sees guarantees as a distant source of repayment, and unlikely to impact borrowing ability. If there is consensus on this matter, borrowers should be informed that well performing debt will not hinder their ability to engage in future development. This can also help boost borrowers confidence and commitment to Capital Impact.
Identify the five most frequent sources and seek to streamline processes
(If Capital Impact is not prepared to take a leadership role on ecosystem improvements)

Given Capital Impact’s market share, and the reoccurring challenges posed by coordinating with other sources, there is an opening for more intentional collaboration between reoccurring sources. This likely needs to be conducted at the management level, rather than the loan officer level. However, it can also be supportive of improvements to the ecosystem that would benefit more minority participation.

**Developer Communication**

**Improve borrowers’ confidence regarding likelihood of securing loan**

Some developers expressed a level of uncertainty about moving through the process. While they had high hopes that their proposals would be approved, there was some anxiety about the final result.

Capital Impact’s process is slightly different, than that of traditional commercial banks, which as previously noted, can add some tension to the market. Informing borrowers of the parameters and standards against which their loan applications will be measured and clarifying the application process, could help inject more confidence in the borrowers and in the process. This may also help build trust between borrowers and staff as they work through complications in order to make the deal fundable.

**Shift messaging approach to borrowers with limited experience**

The most vocal and critical developers also had weakest balance sheets, were in new geographies, and were smaller projects than investors initially targeted. Even though these developers were a small fraction of the total number of developers surveyed, a negative anecdote tends to be more pervasive than a positive one. There is some value in Capital Impact creating a new message to address the critiques around risk aversion, high guarantees, and redundant requirements.

As a borrower with banking experience indicated, “I’d say to whiny developers, ‘zero is totally an option’”. While this is somewhat extreme, the underlying truth is important for Capital Impact to deploy strategically. Capital Impact is taking on market risks where no other CDFI or bank is; it is reasonable to claim that in the face of critiques. There is a high demand for the various Detroit loan funds, and no mandate to always take on the most complex, most challenging, or most interesting deals.

Potential Messaging:
So far, Capital Impact has focused its funding on projects in the Midtown area, and with relatively strong and experienced developers. With a strong and secure portfolio in hand, we are increasingly interested in expanding our products to benefit new
geographies and less experienced developers. While we won’t change our rigorous underwriting process, we are committed to supporting borrowers through the process and strategically testing the market in more neighborhoods. We will continue to balance a sustainable portfolio with high impact projects.

*Intervention Point:* With projects in business development phase that have high potential impact, but are weaker on developer experience. Help problematic borrowers understand that as a exception to program design, the underwriting may be particularly challenging.

**Education**

Create some neighborhood learning opportunities to build familiarity and gain confidence

Some staff indicated concern about moving into new geographies, and some partners indicated the tension that could result from underwriting at a distance. To help build familiarity with new areas and confidence in those markets, local staff—or a summer intern—could develop internal neighborhood guides or brochures that support national staff in understanding the broader context. Rather than trying to replace any of the analysis, these guides could be more visual and sensory, attempting to help capture the “feel” of a place. One simple and low barrier option is using a smart phone to record and share short, placed-based videos. Encouraging staff to spend a week working from the Detroit office is another option.

**Remaining Loan Funds**

Prioritize Community Impact Standards for Remaining Funds

As seen in the portfolio review, almost all projects have achieved the community impact of rehabilitating blighted or vacant properties. With the quarter of the loan funds remaining, Capital Impact should focus on projects that further advance the remaining standards around affordable units and minority developer involvement. Capital Impact should consider at 30% achievement target across projects for each of the community impact standards. This rate could be achieved across standards if Capital Impact commits the balance of the funds to meeting these standards.

This will likely include doing targeted outreach in communities where affordability targets are within market rents, and publicizing an interest in working with minority developers. Capital Impact might also reconsider projects that meet the community impact standards, but were turned away due to size, as it has previously financed some projects under 10 units.