Federal Reserve Bank of Boston

Communities & Banking

Volume 17, number 4 Fall 2006

Also Inside:

Insights from Chairman Bernanke

Providence Group Does the Impossible

Free Life Insurance for Education

The New Win-Win in Public Pensions

When Industry Improves the Environment

Contents

Cover Illustration by Kirk Lyttle

Communities & Banking magazine aims to be the central forum for the sharing of information about low- and moderate-income issues in New England.

If you would like to submit an article for a future issue of *Communities & Banking*, please contact the editor.

Caroline Ellis
Editor, *Communities & Banking*
Federal Reserve Bank of Boston
600 Atlantic Avenue
Boston, MA 02210
(617) 973-3187
caroline.ellis@bos.frb.org

For free subscriptions, contact:
Public and Community Affairs
Federal Reserve Bank of Boston
600 Atlantic Avenue
Boston, MA 02210
(800) 409-1333
bostonfed.publications@bos.frb.org

Available on the web at
www.bos.frb.org/commdev/c&b/index.htm

FEDERAL RESERVE
BANK OF BOSTON™

Industrial Ecology

Environmental and Economic Boon

by John Ehrenfeld
International Society for Industrial Ecology

Illustration by Kirk Lyttle

Industrial pollution often affects low-income neighborhoods disproportionately. But a well-established development in Denmark points to a long-term solution that in time could benefit neighborhoods located near industry.

Kalundborg, Denmark, boasts an unusual industrial park that has grown up over 35 years. In an approach known as *industrial ecology*, its factories use the by-products of neighboring factories as raw materials. The first exchanges between Kalundborg plants were initiated to conserve water from scarce local sources. Some years later the local wallboard plant began to use by-product gas from the nearby oil refinery to heat its drying kilns. Bit by bit, more such exchanges were added.

Although environmental regulations created indirect incentives, no direct public subsidies or other interventions played any part. The industrial park grew quietly for decades, with the world at large hardly noticing. After about 20 years, the community woke up and began to promote the remarkable development, which epitomizes ideas about industrial ecology that were forming simultaneously elsewhere.

Given population increases and the concomitant stress on the environment, we have to decrease current consumption by two to 50 times. We have to run two to 50 times faster just to stay in place.

Production, Consumption, Pollution

Industrial ecology is not a familiar concept to Americans. The field emerged in the late 1980s, catalyzed by Robert Frosch and Nicholas Gallopoulos in a *Scientific American* article. The authors observed that energy and materials flows in industrial networks resembled flows in the food webs of natural ecosystems.[1] But natural ecosystems were doing better than human systems at recycling wastes and getting the most out of their primary energy source, the sun. Nature was providing a lesson.

Historically, industrial networks have operated primarily in "once-through" mode. That is, materials are extracted from the earth, converted into economically useful products, and then discarded back into landfills, air, and water: They go once through the process, and that's it. Superfund sites in New England and elsewhere are a direct consequence of once-through practices.

The unsustainable aspects of today's industry are closely related to massive levels of consumption in both affluent and developing nations, and scholars and critics have long called for drastic reductions. Contemporary heirs of the 19th century political economist Thomas Malthus (who worried about population growth outstripping growth in agricultural productivity) see a relationship between affluence and environmental sustainability.[2] They express that relationship in a formula, I = PAT. *I* is a measure of the stress on the global support system, and it equals *population* times *affluence* (gross domestic product per capita, roughly proportional to consumption) times *T*, which is a measure of the relative impact per GDP unit.

Because population and affluence are bound to grow for some time, impact must decrease proportionally. Estimates of the amount of material reduction necessary to keep current environmental-stress levels from rising run from a factor of two to a factor of 50. In other words, given population increases and the concomitant stress on the environment, we have to decrease current consumption (and/or negative impact) by two to 50 times in order not to increase stress. We have to run two to 50 times faster just to stay in place.[3]

Industrial ecology offers hope for reversing current trends.

A New Dawn

Industrial ecology makes a twofold contribution to environmental sustainability. First, it improves understanding of material flows and how they impact the environmental system. Second, it offers ways to redesign products, services, and production methods. It can reduce stress at every industrial stage: resource extraction, production, use, and disposal.

Applying the industrial-ecology principle to product and production redesign reduces environmental impact and leads to more efficient use of materials and energy. Greater efficiency, in turn, helps both individual companies and whole economies grow.

To apply this simple but elegant principle regionally, look to nature. Natural ecosystem networks and their food webs have large numbers of symbiotic relationships. One species passes its wastes to another as its food. In Kalundborg, similar symbioses are occurring, with one company making good use of the wastes of another.

In fact, a visit to Kalundborg would reveal a large industrial complex with no significant waste lagoons or disposal sites. What might previously have been deposited in such catchments is instead passed along for reuse. For example, the calcium-based sulfur dioxide scrubber effluent from a large oil-fired power plant is piped to a wallboard plant, which now saves on imported hydrated calcium sulfate, the gypsum used in drywall. The biomass effluent from a large pharmaceutical plant is treated sufficiently to be piped or trucked to farmers in the immediate region and used as fertilizer. Waste heat from several plants' hot water and steam is combined and piped to the municipality for commercial and domestic heating.

Growing Urgency

Although Kalundborg grew in an unplanned fashion over decades, today there is a more focused urgency about implementing its symbiotic principles. Industrial ecologists are studying the best ways to develop similar complexes and are working more actively to get them going.

According to the late Edward Cohen-Rosenthal, of the Work and Environment Initiative at Cornell, eco-industrial development (EID) should be viewed not only as promoting sustainability but also as a potential source of good jobs.[4] As he anticipated, attitudes toward waste handling, traditionally an undesirable trade with low wages and uncertain security, have been changing. More people are realizing that recycled wastes have value to industry and agriculture and that keeping wastes out of the environment has a value to communities.

Eco-industrial development could lead to regional economic development. Existing enterprises could save money, as wastes are expensive to haul. New sectors with new jobs could be created. For example, eco-industrial development would be a good use for former Superfund sites and brownfields, which tend to be located in older industrial zones amid low-income neighborhoods that might welcome a more sustainable use. This is not a question of poor neighborhoods getting manufacturing plants no one else wants but of providing completely clean industries with good jobs.

Unfortunately, eco-industrial development is moving slowly in North America. The President's Council for Sustainable Development under President Clinton put together an initiative to develop eco-parks, but it essentially went nowhere.[5] Today, interest has increased in Canada, where EID is a central theme of Burnside, a large industrial complex (1,300 companies) in New Brunswick.[6] Additionally, several small networks centered on the pharmaceutical industry are coming to life in Puerto Rico.[7]

Public Role

High discovery costs—finding partners that have wastes suitable for exchange—are stumbling blocks in the eco-industrial development process. Additionally, constraints and liabilities imposed by hazardous-waste regulations, even if not technically problematic, tend to scare companies away. Moreover, all the success stories have taken a long time to flower, suggesting that patience is essential, and patience is not a typical characteristic of industrial developers.

The impediments point to a possible role for public agencies. For example, government could consider supporting information exchange to lower the discovery costs, it could offer innovative regulatory waivers, or it could create sources of low-cost capital earmarked for EID. The British government set the example recently with a £13 million grant for the development of the National Industrial Symbiosis Program.[8]

Eco-industrial development's potential should spur the private and public sectors to find ways to create partnerships among industries. However, as the Conservation Law Foundation has found, leaving the job primarily to developers' initiatives does not work well, because neighbors often resist plans that have been formulated without their input.[9] It is critical for communities that have suffered from past industrial problems like pollution to get involved early in the process.

Deeply rooted social and political concerns sometimes bring promising brownfield-development processes grinding to a halt. Suspicion about any industrial development, even projects with sustainability objectives, runs deep. Community members need to educate themselves about eco-industrial development and the significant economic and environmental benefits.

Understanding industrial ecology's potential can begin with the recognition that a system in which nothing is wasted already exists, and that system is nature.

John Ehrenfeld *is executive director of the International Society for Industrial Ecology, based in New Haven.*

Endnotes

1 R. Frosch and N. Gallopoulos, "Strategies for Manufacturing," *Scientific American* 261 (1989): 142-55.

2 P.R Ehrlich, and J.P. Holdren, "Impact of Population Growth," *Science* 171 (1971): 1212-1217.

3 E. Von Weizsäcker, A.B. Lovins, et al., *Factor Four: Doubling Wealth: Halving Resource Use* (London: Earthscan Publications, Ltd., 1997).

4 E. Cohen-Rosenthal, "What Is Eco-industrial Development?" in *Eco-industrial Strategies: Unleashing Synergy between Economic Development and the Environment*, eds. E. Cohen-Rosenthal and J. Musnikov (Sheffield, United Kingdom: Greenleaf Publishing, 2003).

5 http://pubs.acs.org/subscribe/journals/esthag-w/2005/jul/business/kb_ecology.html.

6 http://www.uneptie.org/pc/ind-estates/casestudies/Burnside.htm.

7 M.R. Chertow and D.R. Lombardi, "Quantifying Economic and Environmental Benefits of Co-Located Firms," *Environmental Science & Technology* 39, no. 17 (2005): 6535-6541.

8 See http://www.alfed.org/publishor/system/component_view.asp?LogDocId=40644&PhyDocId=33243.

9 James Hamilton, personal communication, June 13, 2006.

By the Numbers

Data and Measurement in Community Economic Development

Highlights of a speech by Federal Reserve Chairman Ben S. Bernanke at the Greenlining Institute's 13th Annual Economic Development Summit in Los Angeles, April 20, 2006

Remarkable strides have been made in developing and analyzing social and economic data at the community level. The information that can be extracted from detailed data profiles of individual communities supports economic development in several distinct ways.

First, by making companies, entrepreneurs, and investors aware of new opportunities and by promoting competition in underserved areas, such information helps put market forces in the service of community development. Second, both government policymakers and community development organizations need the reality check that only hard data can provide. … Third, the increased availability of community-level data facilitates independent research. …

Although government agencies continue to be an important source of data on community development, data collection and data analysis in this area are increasingly becoming the province of the private and nonprofit sectors, notably including community development organizations themselves. …

I will discuss some specific ways data and quantitative measurement have been used in community development. To be clear, I do not believe that all aspects of economic development can or should be quantified. … Still, improving the measurement of inputs and outcomes is critical to better development policy. …

Good data support community growth and development by helping to identify previously unrecognized market opportunities. Free markets can be a powerful source of economic development, but markets work less effectively when information about potential opportunities is absent or costly for private actors to obtain. Several noteworthy initiatives have helped to provide better information.

For example, the Local Initiative Support Corporation's (LISC) MetroEdge initiative seeks to demonstrate the market potential of diverse communities through customized data analyses of each community's demographics and buying power. Such analysis can provide investors with a different perspective. … Similarly, Social Compact's Neighborhood Market DrillDown methodology uses a multilayered research process to provide profiles of the market potential of high-density, lower-income communities. This approach focuses on business indicators—buying power, market size, unmet needs, and market risks—rather than on the deficiency statistics typically used to describe inner-city neighborhoods, such as rates of poverty, crime, and overcrowding. Social Compact, a coalition of business leaders, has applied its DrillDown approach to 101 neighborhoods over the past five years. …

The growth and maturation of community development financial institutions (CDFIs) provide another impetus for data development and analysis at the community level. CDFIs are private-sector financial intermediaries with community development as their primary mission. Like banks and other more conventional financial intermediaries, CDFIs are in the business of attracting funds and putting those funds to work in productive ways. Also like conventional intermediaries, CDFIs depend heavily on the production of accurate information both to guide investment decisions and to provide a basis for attracting new funding. …

To attract more return-oriented investors, including both conventional investors and those with social as well as financial goals, CDFIs must demonstrate financial viability as well as the ability to fulfill the broader development mission. For example, the Opportunity Finance Network's CDFI Assessment and Rating System (CARS) gathers data to evaluate a CDFI's overall creditworthiness and its effectiveness in using its financial resources to achieve its development objectives. …

Although still in its early stages, this initiative, if successful, will have the double benefit of attracting more funds into community development and helping to ensure that those funds are effectively used. More generally, the movement toward quantifying the performance, risk, and community impact of CDFIs is essential to the growth and sustainability of the field, in my view. By demonstrating both financial viability and social impact through hard data, CDFIs are better positioned to obtain the funding necessary to maintain their operations and to respond to emerging needs and opportunities. …

In the community development field, to be sure, financial returns and social returns are not necessarily the same, which is why measurement should include both financial and social indicators. Potential investors, including public-sector and foundation sources of funds, will naturally differ on the weights they put on financial and social returns. To attract the widest range of funding, both types of information should be provided.

Quantitative information plays yet another important role: increasing the effectiveness of policies and programs. The systematic collection and analysis of data on program inputs and outputs is an increasingly important part of learning about what works. For policymakers, data on program results help guide policy development and improve the allocation of scarce public funds.

For community development organizations, participation in broad-based data-gathering serves at least two goals. First, in the long run, their analyses of the activities and the associated outcomes in diverse communities will help them achieve the greatest impact for resources expended. Second, such analyses help community development organizations demonstrate their effectiveness to public and private funders. A number of methods for evaluating community development projects are currently [in use or in development, including the NeighborWorks America's Success Measures Data System and] the Community Investment Impact System developed by the Department of Treasury's CDFI Fund. …

Each of these data-driven initiatives shares the goal of increasing understanding of opaque markets to support investment, policy, and research. The need for data and tools is the driving force behind the Brookings Institution's Urban Markets Initiative. … The think tank is focusing on initiatives that can demonstrate untapped market potential. One such effort is the National Infrastructure for Community Statistics. It will include a central web-based repository that integrates data from federal, state, and local governments and from commercial sources. The ultimate goal of this project, which is under development in collaboration with more than 100 participants from government, nonprofits, and private-sector industries, is to aggregate and to make accessible the data needed to inform decisions about economic development activities. …

The data have a way of challenging our views about what works and what doesn't.

Accountability and feedback, facilitated by data development and quantitative analysis as well as by more-qualitative information, are critical for success. Goals should be modest at first; but knowledge is cumulative, and sometimes good results can be replicated at larger scales. Research, both quantitative and qualitative, furthers learning.

None of this is easy, particularly since the data have a way of challenging our views about what works and what doesn't. But a great deal is at stake both internationally and domestically, and serious empirical analysis has no substitute. The development of more and better data on economically distressed communities, together with sophisticated tools for analyzing those data, is essential for continued progress in community economic development.

Read the entire speech at
www.federalreserve.gov/boarddocs/speeches/2006/20060420/default.htm.

Sharon Conard-Wells

Executive Director, West Elmwood Housing Development Corporation

Responsive Community Development

The abandoned Rau Fastener factory in Providence in 1996.

Sharon Conard-Wells has been a community activist practically from the cradle. She recalls that as a young girl she helped her mother and brother make posters supporting teacher pay during a school strike in the South Bronx. At night, she often guarded the front door while her mother, a door monitor and tenant-association floor captain, went to wake up Sharon's father for his night job. Neighborhood involvement is in her blood.

In 1980, Conard-Wells moved to Providence with her husband, working as a computer scientist and becoming active in the West Elmwood neighborhood. Although she now lives in Warwick, she is identified with West Elmwood for her many initiatives there. One project is perhaps the best known—the project that everyone said was impossible. That was the conversion of the abandoned Rau Fastener factory into mixed-income rental housing. It took years, but the journey demonstrates how responsiveness to a community can lead to miracles.

C&B: Let's start with West Elmwood Housing Corporation's history.

SCW: In the early 1970s, the neighborhood was suffering from neglect. Residents got together, formed the non-profit West Elmwood Housing, and fought for municipal services. They also tapped a federally funded program that provided down payments and closing-cost assistance for first-time homebuyers. After that program lost funding, the group disbanded, but one board member kept the corporation alive, paying fees and doing filings.

C&B: How did you get involved?

SCW: Soon after I moved here, people came around talking about issues, and I started going to meetings. I have a lot of opinions, and I found myself becoming block captain, secretary, treasurer of the West End Coalition. In 1986, business owners offered us neighborhood-improvement money, but we couldn't accept donations without a whole legal process. A priest remembered a parishioner with a corporation on paper and brought everyone to a meeting. Several members of the old group came, and we merged, becoming "West End Coalition doing business as West Elmwood Housing." Our goals were to improve city services, clean up the neighborhood, and influence the disposition of vacant buildings.

When our first director left, the board wanted someone energetic to help the new director. I became the administrative assistant in 1989. When the second director resigned in 1991, I applied.

C&B: What does community organizing mean to you?

SCW: It means "Meet 'Em Where They're At." I ask myself what individuals' needs are. How do I engage senior citizens knowing that they don't like to come out at night for meetings? How do I engage young people? What do parents need?

One Saturday I was in the office, and a local kid came to hang out. Then somebody else came, and before I knew it, I had a group of kids hanging out. A board member stopped by, and we were all sitting around talking. A kid asked about something, and the board member said, "Come back next week, and I'll help you with that."

Our Young Voices program grew from there. The kids were 7 to 16, which was a challenge. We ended up having the older kids come on Tuesday night and help plan for the younger kids. Parents were grateful. One parent asked us to help a younger child who couldn't read. They began to see us as the answer to many things.

2006: The old Rau Fastener factory is now Westfield Lofts, attractive mixed-income rental units.

C&B: You responded to the needs parents brought you?

SCW: We don't try to solve everyone's problems ourselves. But when parents and others come to us saying, "I called the police six times, and they didn't come," we take the time to show them how to help themselves.

We serve three overlapping needs: community development, housing, and economic development. For community development, we get people engaged in block associations. We make calls about stop signs, potholes, etc. We also offer Summer Sweeps, a program for middle school kids. They get a stipend for sweeping in front of businesses, removing graffiti, watering grass, planting trees. They must open bank accounts and deposit a certain amount every week before getting paid. At the end of the summer, they can take some out for school clothes. Rhode Island Housing helped us the first five years, and now Coastway Credit Union supports us, too.

C&B: Those activities address the community part of your mission. What about the housing and economic-development pieces?

SCW: Our loan program relates to both. We offer down-payment and closing-cost assistance and home-repair loans. We make character loans when banks won't.

Our loans can be sold on the secondary market. We service them in partnership with a CPA firm. We provide home-buyer education, one-on-one counseling, credit repair, mortgages, and foreclosure prevention. And we're announcing a program on predatory lending.

Another new program, ClearCorps, clears lead paint from homes in partnership with the city of Providence through a national lead-abatement grant. We train local people and get them certified. They assess, clean, test, and certify that buildings are lead safe. And we're working with Cranston Street merchants to start a business group. The city has offered a program called Neighborhood Markets, and Rhode Island Housing has raised funds for a façade program. So now we can say to neighborhood businesses, "Look, we have funding; tell us what to do with it."

C&B: Let's turn to the project that couldn't be done, the one your colleague in Woonsocket begged you to reconsider.

SCW: I was glad that a friend like Joe Garlick was the first person to give me the "Are you crazy?" look. A neighbor of the abandoned Rau Fastener factory had come to the board and convinced us we had to tackle the factory. So one day when Joe was here, I said, "Let me show you our next project," and we drove over. The look on Joe's face! He said, "Are you crazy? No, Sharon. Please! That project will put you under." I got accustomed to that look from people.

Rau Fastener was an operating factory up until the mid-1990s. It opened in 1892 to make jewelry and snaps. In 1996, the owner abandoned it. A neighbor kept asking me, "What are you going to do about the factory?" and I would say, "We don't do factories." She persisted: "Your job is to fix the neighborhood, and that needs fixing." She gave the board a petition from residents, and we said we'd try to

If we didn't take control of our destiny, we could become a bedroom community of Boston, and we might not be able to stay.

interest someone in the factory. I didn't really know how the game was played, but I knew there was a building, somewhere a business needing a building, and somewhere money. But no one bit.

C&B: What turned the tide?

SCW: Mills became cool. To make a long story short, we bought the factory for $2,500 after an auction where no one made an offer. The board thought deeply about the next step. What if we develop it and fail? What if we don't do it? What if someone is hurt and we're liable?

The board knew it was a great location, two blocks from major bus routes, close to two high schools, two minutes from Route 195, five minutes from downtown, a 20-minute walk to the hospital, with three banks nearby—Sovereign, Citizens, and Bank of Rhode Island. If we didn't take control of our destiny, we could become a bedroom community of Boston, and we might not be able to stay.

The board understood the project could put us out of business. But we were careful. We brought in environmental specialists, historic site experts. We knew we didn't know it all.

C&B: Were past funders supportive?

SCW: Not at first. I got lots of "Sharon, this is no reflection on you, but no no no no no." And then one day, somebody sighed and said OK. All I needed was one. I'd been working with a group of Providence CDCs interested in doing a test project on economic development.

With my first $8,000, I could do a market study. And because mills were popular, there was a market to study. We learned we could get good rents. The Clean Land Fund got money from the Rhode Island Foundation and helped us get an EPA Region I environmental assessment grant. The most contaminated part fortunately did not meet historic standards, so we could tear it down. Without that, the project wouldn't have been feasible. Fleet Bank gave the CDC partnership some predevelopment money. LISC (Local Initiatives Support Corporation) pitched in.

The factory is now Westfield Lofts, mixed-income rental. We have three rental levels: 22 low-income units, units for people whose income is just over the low-income tax-credit guidelines, and market-rate units. Most units are in the affordable range ($750 to $1,000 per month). We're about 70 percent rented since launching in January.

C&B: I understand you're developing five acres in the area.

SCW: Yes, in addition to the mixed-income rentals in stage one, we'll have green space, commercial space, low-income homeownership, and market-rate homeownership.

C&B: And all this started with responding to a neighbor's complaint.

SCW: She convinced us. She said that if it was easy, someone else would have done it but that West Elmwood Housing was supposed to tackle neighborhood improvement. It took us a while, but we did it.

Public Pensions:

The Multiplier Effect

by Doug Hoffer

Pension funds can play an important role not only in ensuring the economic security of a state's retirees, but also in promoting local economic-development goals. Historically, public pension funds' investment policies were narrowly construed, weighing only the rate of return for potential investments. Today, however, many elected officials and trustees recognize that considering secondary effects like local economic growth fulfills both a social responsibility and a fiduciary one.

That is why more trustees are investigating opportunities for "economically targeted investment" (ETI). As financial markets and economic conditions have changed and gaps in traditional sources of credit have appeared, barriers to government goals such as small business development and affordable housing have increased. Officials around the country are learning that pension fund investments, when done properly, can boost economic development without undermining fiduciary responsibility.

What and Why?

California Public Employees' Retirement System defines economically targeted investments as risk-adjusted market rate investments with collateral intent to improve "the economic well-being of the [state], its localities, and residents. Economic stimulation includes job creation, development, and savings; business creation; increases or improvement in the stock of affordable housing; and improvement of the infrastructure."[1]

ETIs are not a separate asset class but a *perspective* that gauges secondary effects as well as good financial returns:

- **Market rate returns.** "ETIs are distinguished from 'benevolent' or 'social' investments. Social investments are made by foundations, government agencies, non profits,and individuals whose primary purpose is to accomplish some social goal. In contrast, ETIs must be organized to yield a market rate of return commensurate with risk, liquidity, and transactional costs."[2]

- **Collateral benefits.** Although most investments yield a return to society, ETIs are distinct because they provide money to underfinanced sectors of the economy and fill "capital gaps."

The societal return from most corporate stocks and bonds is diffuse and may not provide direct social benefit to the state from which the investment originated. ETIs, however, direct both the investment and the social benefit to a defined geographic area. If Vermont pension funds, for example, target investments to Vermont, they can get a good return, help the Vermont economy, and boost the tax base (thereby supporting the security of the state employees they serve).

Because capital markets do not invest equally in all worthy investment vehicles, more pension funds are looking at ways to invest in the local economy without risking a poor return.[3]

Win-Win

Nonfederal public pension plan fiduciaries are bound by rules defined in state statutes, usually a variation of those found in the Employee Retirement Income Security Act (ERISA), the 1974 federal law governing private pension plans. These include cautions about prudence, diversification, and exclusive purpose (fiduciaries must discharge their duties for the *exclusive purpose* of providing benefits to participants and their beneficiaries and defraying reasonable administrative expenses).

The U.S. Department of Labor's most recent interpretive bulletin, July 2002, reiterates that the same fiduciary standards apply to ETIs as to other plan investments, so fund administrators are free to pursue them.

State and local pension plans offer potential for win-win investing. With trillions in assets, they can designate at least a portion to local economic development. The most recent comprehensive survey of public pension plans found at least 29 states have public pension plans with some form of ETI program.[4] Assets invested in ETI programs were estimated at about $55 billion, with residential housing and venture capital the most common ETI programs.[5]

Because mortgage-backed securities are safe and easily traded, public pension funds have made housing an important part of their ETI programs. According to the U.S. General Accounting Office (GAO), almost one-third of those programs are focused on residential housing, with investments in mortgage-backed securities, housing finance agency bonds, investment trusts (for example, AFL-CIO Housing Investment Trust), project financing, and direct financing.

Some pension funds stimulate local development through guaranteed Small Business Administration (SBA) loans, linked certificates of deposit, private placement, and targeted venture capital.

How Are They Doing?

According to the fiduciary standards, it is not enough to have a positive return: a market rate of return for comparable types of investments is required. In 1995, the GAO developed benchmarks for each type of ETI program. Then it surveyed U.S. public pension funds and found that most ETI programs were *outperforming* the benchmarks.

Today the numbers of ETI programs are growing. California's CalPERS and CalSTRS have large ones.[6] Together they have:

- committed $830 million for private equity investment in businesses in underserved areas;
- committed more than $4.3 billion to urban, in-fill real estate ventures, including $695 million for affordable housing;
- purchased $90 million in California home mortgages;

- purchased $260 million in California SBA loans; and
- vastly increased deposits in community lending institutions and credit unions.

In Massachusetts as of March 31, 2006, the market value of the Alternative Investment Portfolio, which includes venture capital and special equity partnerships, was $2.64 billion. The portfolio comprised 6.3 percent of the state's public pension trust funds, although the asset allocation allows up to 10 percent.[7]

As of December 31, 2005, the aggregate investments for all New York City ETI programs since inception amounted to more than $1 billion. The investments went toward renovation, new construction, or financing of more than 30,000 units of affordable housing and many small retail spaces. They "created thousands of construction jobs and financed child-care facilities and senior citizen centers. The five-year overall return on the pension funds' targeted investments was 6.30 percent and the 10-year return was 8.34 percent."[8]

The Texas Growth Fund was established in 1988 and invests in the local economy, too, specializing in "structuring equity and subordinated debt investments that finance buy-and-build strategies, internal expansions, and buyouts of small- to middle-market companies."[9] Through 2004, the Fund has invested more than $400 million in 44 Texas businesses.

And as of December 2005, the Washington State Investment Board had $1.3 billion (2.7 percent of total funds) in Washington-based investments, including public equity, fixed income, real estate, and private equity.[10]

Perceived Barriers

Issues remain. A challenge for funds is that direct investments, including ETIs, are time-consuming. That's why commingled real estate and mortgage accounts are popular. Because they provide liquid, diversified investments with solid returns, they are easier to implement.

A second concern is that complex direct ETIs often have high administrative costs. Mortgages and mortgage-backed securities entail fewer such expenses.

Finally, overzealousness and political interference sometimes cause problems, and fund managers need to be on guard. Connecticut, for example, lost millions in the 1990s by investing in the failing Colt Manufacturing Company to save jobs. Connecticut officials have since learned to give adequate consideration to risk-adjusted returns. In another instance, when oil prices collapsed in 1987, 40 percent of Alaska's in-state mortgages became delinquent or ended in foreclosure. Alaska learned that having 35 percent of its fund assets in mortgages was an unreasonable allocation.

But since the early days of ETIs, pension funds have developed more sophisticated in-house expertise and have hired established professionals to help manage the programs. The number of existing programs (and the billions invested) is evidence that ETI programs can succeed.

Economically targeted investments are prudent if well conceived and managed. Numerous public pension funds have utilized small portions of their assets to fill financing gaps for affordable housing, small business development, and venture capital. The available data suggest that return on investment is reasonable and comparable to similar non-ETI investments.

The primary responsibility of state pension boards is to protect the workers and retirees who depend on the funds' assets. However, with economically targeted investments, they have an opportunity to advance additional goals. To the extent a successful ETI program helps to create a more sustainable economy, it will directly benefit the workers and pensioners the funds represent.

Doug Hoffer *is a policy analyst and consultant in Burlington, Vermont. This article is a shorter version of a report completed for the Vermont State Treasurer.*

Endnotes

1 CalPERS Statement of Investment Policy for Economically Targeted Investment Program, February 14, 2005; see http://www.calpers.ca.gov/eip-docs/investments/policies/other/economically-targeted/eco-target-inv-prg.pdf.

2 R. Ferlauto and J. Clabourn, *Economically Targeted Investments by Statewide Public Pension Funds* (Washington, D.C.: The Center for Policy Alternatives), September 1993, p.4.

3 U.S. Dept. of Labor, Advisory Council on Pension Welfare and Benefit Plans, "Economically Targeted Investments: An ERISA Policy Review," 1992.

4 U.S. General Accounting Office, "Public Pension Plans: Evaluation of Economically Targeted Investment Programs," March 17, 1995.

5 *Economically Targeted Investments: A Reference for Public Pension Funds* (Sacramento, California: Institute for Fiduciary Education), June 1993.

6 See http://www.treasurer.ca.gov/publications/dbl/five_years.pdf.

7 See http://www.mapension.com/InvestmentProgram/CoreDescrip.html#AltInv. The Pension Reserves Investment Trust (PRIT) Fund is a pooled investment fund established to invest the assets of the Massachusetts State Teachers' and Employees' Retirement Systems, and the assets of county, authority, district, and municipal retirement systems that choose to invest in the Fund.

8 See http://www.comptroller.nyc.gov/.

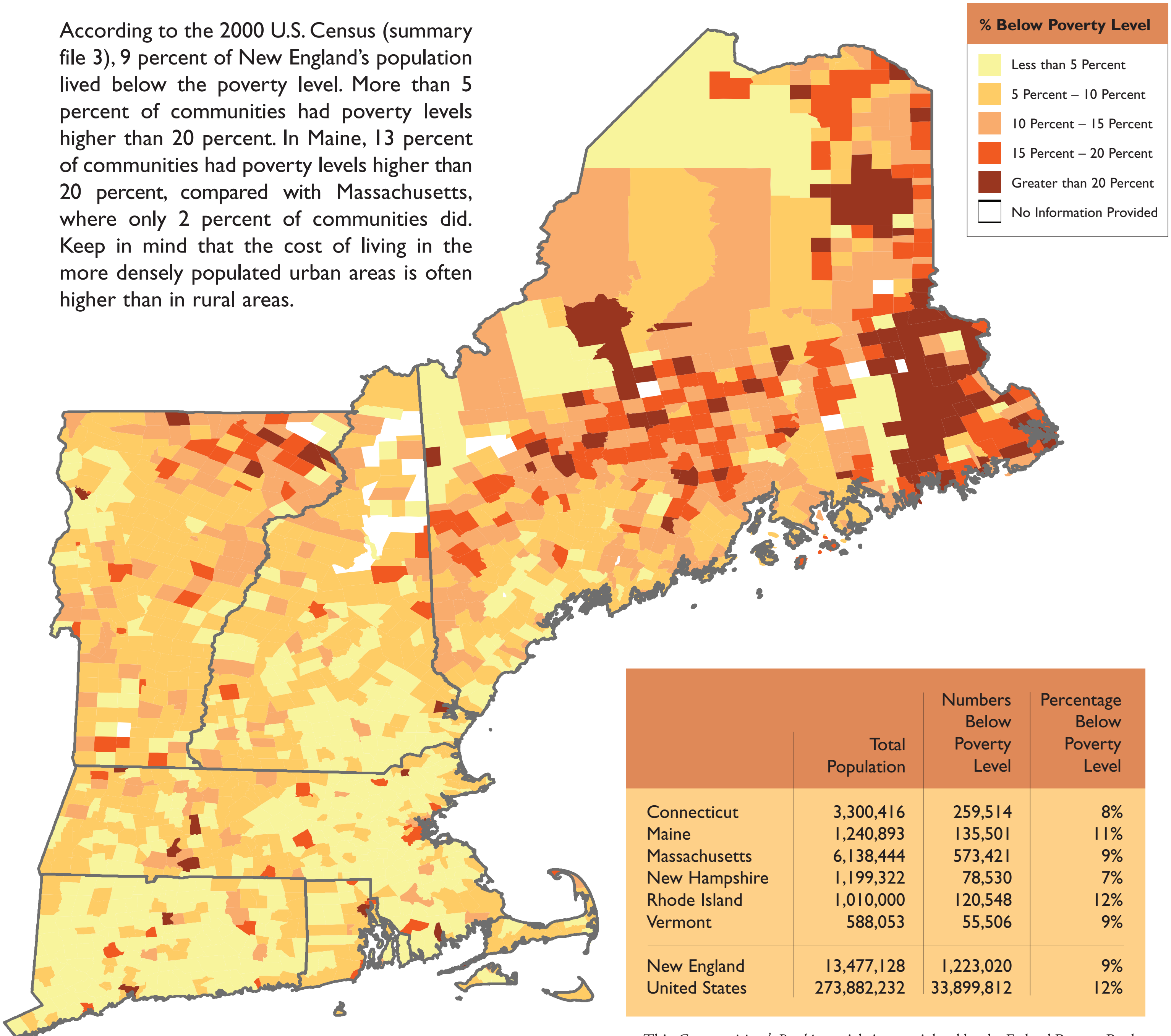
9 See http://www.tgfmanagement.com/investment/i2.html. The Texas Growth Fund "is an equity-oriented investment fund based in Austin. The TGF is backed by the state's four largest public trust funds: the Permanent School Fund (PSF), the Permanent University Fund (PUF), the Teacher Retirement System (TRS) and the Employees Retirement System (ERS). Each of these trust funds, as well as any local government trust fund, is authorized to contribute to TGF 'trusts.' Each of the four major state trust funds is represented on the Texas Growth Fund Board of Trustees."

10 See http://www.sib.wa.gov/financial/pdfs/eti/2005.pdf. "The Washington State Investment Board manages $65 billion in assets for 34 separate state retirement and other trust funds."

Mapping New England

Concentration of Poverty in New England by Cities and Towns

According to the 2000 U.S. Census (summary file 3), 9 percent of New England's population lived below the poverty level. More than 5 percent of communities had poverty levels higher than 20 percent. In Maine, 13 percent of communities had poverty levels higher than 20 percent, compared with Massachusetts, where only 2 percent of communities did. Keep in mind that the cost of living in the more densely populated urban areas is often higher than in rural areas.



	Total Population	Numbers Below Poverty Level	Percentage Below Poverty Level
Connecticut	3,300,416	259,514	8%
Maine	1,240,893	135,501	11%
Massachusetts	6,138,444	573,421	9%
New Hampshire	1,199,322	78,530	7%
Rhode Island	1,010,000	120,548	12%
Vermont	588,053	55,506	9%
New England	13,477,128	1,223,020	9%
United States	273,882,232	33,899,812	12%

Source: 2000 U.S. Census Bureau
Map: Ricardo Borgos, Federal Reserve Bank of Boston

Help for Low-Income Families

Life Insurance for Education

by Lynn Mitchell
Corporate Voices for Working Families

To many working families, life insurance is a luxury. Fortunately, for those who would ordinarily qualify but just can't afford the premium, a corporate member of Washington-based policy group Corporate Voices for Working Families is offering free life insurance as part of its philanthropic outreach—just one of many creative initiatives spearheaded by Corporate Voices members.

At present, 52 companies participate in Corporate Voices for Working Families, a nonprofit, nonpartisan membership organization that brings a private-sector voice into the national policy debate on issues affecting working families. Members collaborate to develop workplace polices conducive to the needs of 21st century families.

Additionally, members often set an example by offering programs to help their own employees. A company might, for example, educate workers about direct deposit of paychecks and its potential boost to saving, or they might offer free assistance with filing for the earned income tax credit and advise workers on saving their refunds.

An Unusual Idea

One Corporate Voices member, insurance company MassMutual, has long been interested in supporting education as part of its community outreach. For example, scholarships that it initially gave out in its home-base cities are now offered nationwide. (The company has home offices in Springfield, Massachusetts, and Enfield, Connecticut, having recently moved from Hartford.)

In 2002, the insurance company took an even bigger step. It decided to tie its educational philanthropy to its area of expertise by offering qualified individuals earning less than $40,000 per year free life insurance to support their children's education. (See the exhibit "MassMutual's LifeBridge Insurance.") The resulting program is called LifeBridge, and it's a good example of the leadership demonstrated by members of Corporate Voices.

Why is it free? First and foremost, LifeBridge is an extension of MassMutual's education-focused community service. It is philanthropy. But the idea for it arose from a discussion about how the company might begin to serve people in the mostly untapped lower-income market. And in fact, the visibility that LifeBridge has provided has benefited the company in a variety of ways.

For example, the program has helped MassMutual agents build relationships with clients. Agents are permitted to market LifeBridge to individuals and may contact the companies where individuals work and see if they want to offer the insurance to eligible employees. In either case, agents are not allowed to solicit additional business from LifeBridge applicants.

As Cindie St. George, the director of LifeBridge Operations, says, "LifeBridge has promoted goodwill and increased recognition for MassMutual and our agents in a number of communities across the country. The word of mouth has been positive." In a couple cases, individuals have even asked to buy additional insurance coverage. So although the primary purpose is charitable, it is charity that has residual benefits for the giver.

"To date, about $2 million in free coverage has been offered to Boston families by my agency," St. Jean says. "I'm hoping to increase that amount over the next year."

Supporting Education

LifeBridge was launched in September 2002 in four states with the support of a handful of nonprofit groups. Agents wrote 1,000 policies in the first full year and 2,000 in the second full year. Today LifeBridge is available in all 50 states and Washington, D.C., dozens of nonprofits have gotten on board, and 5,400 families have been issued policies that amount to more than $270 million in total coverage. The goal is 20,000 policies (or $1 billion in free life insurance coverage) by December 31, 2007, at which time MassMutual will consider what to do with any unused policies and whether to make more policies available.

In April 2006, the "I Have a Dream" Foundation recognized the educational benefits of the program with a Corporate Award. Like MassMutual, the organization believes that the solution to many issues facing low-income communities is education. However, when parents die, the obstacles to their children's schooling are often insurmountable. Free education-oriented life insurance is one answer, and if applicants can pass the screening normally required for life insurance policies, they can help protect their children's future.

If a LifeBridge-insured parent dies (and, sadly, two already have), $50,000 is put directly into a trust fund that is administered by the MassMutual Trust Company, FSB. The trust fund pays for the education-related costs of the surviving child or children. The money

Getty Images


Getty Images

In establishing LifeBridge, MassMutual is leading the way for other corporations to create workforce-friendly initiatives.

may be used for preschools, private schools, trade schools, community colleges, universities, art or music schools, and more. It covers expenses such as books, tuition, fees, and room and board. The child or children have 10 years from the death of the parent or until they reach age 35, whichever is later, to use the money.

"If the money is not used by the children after a parent's death, it is donated to one of five scholarship programs preselected by the parents," writes Washington Post columnist Michelle Singletary.[1] The five programs that the company offers are the United Negro College Fund, the Hispanic Scholarship Fund, the Urban League's National Achievers Society Scholarship Fund, the Achievement Foundation Scholarship Fund, and the Community Foundation of Western Massachusetts.

Cindie St. George says that the program, which has a very small advertising budget and involves pro bono underwriting by MassMutual agents, gets its biggest boost from nonprofit partner organizations. Habitat for Humanity has offered it to its future homeowners, for example. Clients' natural tendency to be suspicious of anything said to be free is alleviated by the support of a familiar nonprofit group. In New England, for example, general agent Richard St. Jean is partnering with The Boston Foundation to help reach out to eligible applicants and increase the amount of free coverage in the Greater Boston area. "To date, about $2 million in free coverage has been offered to Boston families by my agency," he says. "I'm hoping to increase that amount over the next year with the help of my community partners."

In establishing LifeBridge, the company is not only demonstrating that members of Corporate Voices care about working families, it is leading the way for other corporations to create workforce-friendly initiatives. If other companies choose to offer LifeBridge to their employees, so much the better. Businesses that promote the idea of an educated workforce may want to help ensure that their employees' children can go to school no matter what their economic status and no matter what misfortune strikes.

Lynn Mitchell *is policy director of Corporate Voices for Working Families in Washington, D.C.*

Endnote

[1]Michelle Singletary, *Washington Post*, June 16, 2005.

MassMutual's LifeBridge Insurance

MassMutual's free life insurance program extends its educational philanthropy through the work it knows best, insurance. The company aims to provide 20,000 policies to low-income clients by the end of 2007. With services donated from MassMutual agents, the offer is being spread primarily through word of mouth and through nonprofits working with low- and moderate-income families.

The program provides a $50,000 10-year term policy to eligible parents and guardians. MassMutual pays the premiums. There is no cost to the insured or their children. Death benefits go to a trust to be used solely for the education of insureds' eligible children.

Eligible applicants must be:

- aged 19 to 42
- permanent legal residents of the United States
- parents or legal guardians of one or more dependent children under age 18
- currently employed full- or part-time, with a total family income of $10,000 to $40,000 according to their most recent income-tax return
- the only household member who has applied for the program
- in good health as determined by MassMutual's underwriting guidelines

Ineligible applicants:

- have been diagnosed with heart disease, cancer, HIV, or Type 1 diabetes
- currently abuse drugs or have done so within the last 10 years
- are currently on probation

These are Textiles?

Innovations in modern fabric design, manufacture, and use

There's a great new show in the Federal Reserve Bank of Boston's first floor gallery. It's the fourth in our series of changing exhibits since the opening of the New England Economic Adventure in October 2003. In this one we take a solidly New England theme, textiles, to look at some of the familiar, topical, and unusual ways in which modern fabrics are being used and will be used.

Exhibit runs through December • Open to the public • Picture ID required to enter the building
Contact Melita Podesta at (617) 973-3197 for more information

New Hori


Farm field, Grand Isle, Vermont.
Photographs for this article, including back cover, by Julie Weinstein.

zons

by James Putnam, II
First Pioneer Farm Credit

for New England Agriculture

Dramatic changes in farm technology, efficiency, marketing, and farm structure occurred throughout the 20th century and continue at a rapid pace in the New England farm sector. Fifty years ago, a New England farmer's chief competitor was down the road or in a nearby state. Today competition is often global—and almost always with the distant U.S. farm regions of the West.

What agriculture should we sustain in New England? Are we willing to stand on the sidelines and let free market forces take their course? Can farm entrepreneurs be catalysts for development of rural communities? With Congress gearing up to rewrite the Farm Bill in 2007, what are appropriate policy goals for New England?

Does New England Agriculture Matter?

The fact is, less than one percent of New Englanders farm (0.82 percent as of 2002).[1] Viewed another way, $1.98 billion of farm production in 2002 amounted to about 0.35 percent of New England's state gross domestic product (GDP).[2]

The value of sustaining a healthy agricultural economy in our region is clearly not about population numbers or primary economic impact. Agriculture is more significant in terms of local economic impact. For example, farmers account for 4.5 percent of Vermont's population and the gross value of agricultural production is a healthy 2.5 percent of the state's GDP.

There are at least four other reasons why New England agriculture matters:

- **Economic multiplier.** Agriculture has a substantial economic multiplier. For New England, 12.2 percent of our total 2002 employment was farm and farm-related.[3] The U.S. Department of Agriculture defines this statistic to include farmers, those who produce and sell inputs to farmers, those who process and market products using raw materials from farms, and those in wholesale and retail trade of food and fiber products.

- **Land use.** Agriculture plays a big role in New England land use. The *2002 Census of Agriculture* indicates that 10 percent of our land is in farms. Any vision for New England's future land use necessarily involves its farms.

- **Quality of life.** Agriculture affects New England's uniqueness in terms of quality of life for both residents and tourists. Vermont's dairy farms, the Connecticut Valley's tobacco barns, Plymouth County's cranberry bogs, and Downeast Maine's wild blueberry fields help define our region. And thousands of roadside stands, in-city tailgate markets, pick-your-own offerings, bed-and-breakfasts, and corn mazes strengthen New England's tourism industry and provide memorable experiences for local consumers.

- **Environment.** The environmental boon of properly managed land in active farm production is rapidly emerging as a serious benefit of agriculture, and is looming even larger in public policy. Active and well-managed farmland supports diverse wildlife populations and is more benign to watershed hydrology than suburban subdivisions. Crops, pastures, and forests are critical links in our planet's carbon-dioxide ecology.

A Vision on the Horizon

In 2005, the national Farm Credit System (FCS) undertook *Horizons*, a comprehensive research and market-assessment project that examines agriculture and rural America and analyzes trends for the future.[4] Three FCS entities serve New England: First Pioneer Farm Credit, ACA (agricultural credit association); Yankee Farm Credit; and Farm Credit of Maine.

Although New England agriculture differs from other U.S. farming regions in average farm size and other ways, the region is on the same fundamental trajectory for nearly all major American agricultural trends, just more advanced. New England's experience may well be a leading indicator of agriculture's direction. For example, New England has been ahead of most other U.S. regions in diversifying into both niche-farming enterprises and agritourism.

Each of the eight *Horizons* conclusions has meaning for the future of New England agriculture.

Farm windmill on the shore of Lake Champlain, Grand Isle, Vermont.

Heterogeneity

American farmers are not a homogenous group. There is tremendous diversity in farm size, annual revenue, ownership structure, and marketing approaches. To a lesser extent, there is an emerging diversity in the age, ethnicity, and gender of owners and operators. An overwhelming majority of small-scale U.S. farms dominate the food and fiber production system. New England agriculture is even more diverse, and has substantially more niche and direct marketing than major American farming regions. Moreover, new people are entering agriculture: The *2002 Census* found that 11 percent of New England farmers began farming within the previous four years.

Diversification

Relatively few farming-only businesses remain. The majority of farmers, especially small operators, rely on a wide array of nonfarm jobs to stay in agriculture. Even larger farmers diversify their income as a risk-management strategy through agriculture-related or nonfarm investments such as trucking, landscaping, building maintenance, and snowplowing. In New England, 76 percent of farmers earn more than half their income off the farm. Only 11 percent are 100 percent reliant on farming.

Evolution

Business models and farm-ownership structures continue to evolve. Farmers depend on a wide range of businesses for products and services (such as crop-input suppliers, livestock feed dealers, veterinarians, lenders, and crop consultants). The businesses may or may not be owned by farmers or be located in a rural community, but all are essential to the economic viability and quality of life for farmers. In New England, farmers are innovative entrepreneurs, developing businesses that include everything from on-farm bakeries to methane production.

Bright Future

Although the number of farmers, agriculture-related jobs and industries, and agriculture-dependent communities has declined, the future of both U.S. and New England agriculture remains bright. The competitive pressures of globalization and technological advances have resulted in more consolidated, efficient systems for producing food and nonfood products. Nevertheless, small and niche agricultural enterprises have injected local communities with new vitality. Examples include farms with ice cream stands and petting zoos, elaborate corn mazes open to the public, and bed-and-breakfast businesses on farms. Agriculture will increasingly be a source of energy production, feedstocks for industry and medicine, and other value-added products.

Farming in the Shadow of the City

Some rural areas retain few ties to agriculture. Conversely, more agriculture and related businesses are located in suburban areas and near metropolitan centers. It is becoming increasingly difficult to define a rural community solely by population density. Rural communities continue to grow if they are located near growing urban areas or regional economic centers blessed with scenic resources or designated as attractive retirement destinations. According to the *1997 Census of Agriculture*, 47 percent of New England farms were in metro counties and were producing 53 percent of the region's dollar value of production on 34 percent of New England's farmland.[5]

Collaboration

Regional collaboration, public-private partnerships, and coalitions of investors are key to the future of many rural communities. To create new jobs, attract new business, and foster an environment for future economic development, agricultural America must find new ways to reinvest farm real estate equity and to form partnerships among financial institutions, government, universities, rural economic development agencies, and local farm and community leaders. Some states are developing agricultural innovation centers with the objective of bringing together scattered public, private, and industry resources to support entrepreneurial agriculture.

Entrepreneurship

Entrepreneurs remain the lifeblood of American agriculture and rural communities. Historically, the ingenuity of American farmers and ranchers drove U.S. agriculture's productivity growth. Today's rural entrepreneurs, farmers, and ranchers continue to need access to capital, essential infrastructure, and business support services. New entrants to New England agriculture, often with no prior farming background, are a healthy sign of continued entrepreneurial vitality. Public policy that supports entrepreneurial activity and provides access to capital markets will be critical.

Access to Capital

Ongoing access to debt and equity capital is essential for the future prosperity of agriculture and rural communities in New England and across America. Farms, rural businesses, and communities need access to dependable, competitive financial products and services to thrive in this rapidly changing environment. Initiatives such as First Pioneer Farm Credit's FarmStart will provide small working-capital investments for start-up farms in the company's six-state service region. As we celebrate the Farm Credit System's 90th anniversary, we hope the *Horizons* initiative will be embraced by all who seek a bright role for agriculture in the New England economy.

James Putnam, II, *is senior vice president at First Pioneer Farm Credit, ACA, www.FirstPioneer.com, in Enfield, Connecticut.*

Endnotes

[1] See *Statistical Abstract of the United States: 2006*; U.S. Census Bureau, *2002 Census of Agriculture*, and NASS-USDA; http://www.nass.usda.gov/Census_of_Agriculture.

[2] Gross State Product, U.S. Bureau of Economic Analysis, http://www.bea.gov/bea/newsrel/gspnewsrelease.htm.

[3] *State Fact Sheets*, Economic Research Service-USDA, http://www.ers.usda.gov/ StateFacts.

[4] See *21st Century Rural America: New Horizons for U.S. Agriculture*, The Farm Credit Council, Inc., 2006, www.fchorizons.com,.

[5] *1997 Census of Agriculture*, NASS-USDA, http://www.nass.usda.gov/census/index1997.htm. Metro/nonmetro view compiled by the author.

Homeownership in a High-Cost Region

by Esther Schlorholtz

Boston Private Bank

A perfect storm is brewing in the home mortgage industry in eastern Massachusetts. Home prices are among the highest in the nation. Many buyers have borrowed heavily against their homes. When the Federal Reserve began raising rates in July 2004 and the prime rose from 4 percent to 8.25 percent within 24 months, homeowners with variable rates felt it immediately. Moreover, borrowers with adjustable rate mortgages are experiencing substantially higher costs as their rates re-set. Sales of new homes are slowing, and prices are softening.

Meanwhile, mortgage lenders unregulated by the Community Reinvestment Act (CRA) have aggressively marketed high-cost products, often in minority communities. African Americans and Latinos at every income level are five times more likely to get the costly loans than whites, and according to Home Mortgage Disclosure Act (HMDA) data for 2004, Boston's predominately minority neighborhoods were almost eight times more likely to get high-rate loans.

In 2005, both units in this Worcester duplex were purchased for $143,000 with SoftSecond loans. *Photograph by Greig Cranna, courtesy of the Massachusetts Housing Partnership.*

The storm is in its early stages. Foreclosure filings are up. Boston had 24 in 2004 and 60 in 2005. In the first four months of 2006 alone, according to city officials, Boston experienced another 60 foreclosures. The numbers are small compared with the city's nearly 1,700 foreclosures in 1992, but the trend is a concern. It took communities in the early 1990s years to recover from the foreclosures.

Mattapan, Roxbury, Dorchester, and Hyde Park have the highest foreclosure rates. These largely minority Boston neighborhoods also had the most high-cost loans (loans three percentage points or more above the comparable U.S. Treasury security of the same maturity).[1]

The Boston Globe Magazine recently correlated the growing percentage of high-cost loans in these neighborhoods with increasing foreclosures.[2] For example, Roxbury had more than 23 percent high-cost home-purchase loans in 2004, and in 2005 it had foreclosure petitions of 17 per 1,000 homes. Mattapan had almost 34 percent high-cost mortgages in 2004, and in 2005 it had foreclosure petitions of 15 percent.

According to the *Borrowing Trouble? VI* report, high-cost loans accounted for double-digit shares of all home-purchase lending in 17 suburban communities in Greater Boston. That includes Everett with 28 percent, Revere with 25 percent, Marlborough with 21 percent, and Randolph with 20 percent. Beyond Greater Boston, some of the high-cost loan shares were even higher—36 percent in Lawrence, 31 percent in Brockton, and 29 percent in Springfield.

Tackling the Challenge

What should we be doing to minimize the damage? Boston's Mayor Thomas Menino believes in intervening early—for example, by expanding the "Don't Borrow Trouble" campaign initiated by the Massachusetts Community & Banking Council (MCBC). Other municipal leaders are likely to follow suit. Banks are saying they will consider financing at-risk borrowers with fixed-rate products, but many borrowers will need public support.

Legislation has been proposed in Massachusetts that would require mortgage companies (largely headquartered out of state) to bear responsibilities like the ones that banks' assume under the Community Reinvestment Act, but it keeps getting delayed. The Massachusetts Division of Banks is carrying out fair-lending exams to ensure that these mortgage lenders are

In 1999, a Boston school custodian purchased a condominium in this Roslindale development for $135,000 with a SoftSecond loan. *Photograph by Greig Cranna, courtesy of the Massachusetts Housing Partnership.*

Solid, well-performing loans for low- and moderate-income borrowers are the result of good lending products and responsible lenders.

not targeting minority-group populations with high-cost products. Additionally, expanded public-education initiatives are being proposed through MCBC, the Massachusetts Bankers Association, the Massachusetts Mortgage Bankers Association (MMBA), the Massachusetts Mortgage Association, and the Massachusetts Credit Union League. And the Federal Reserve Bank of Boston is coming out with a new consumer brochure, *True or False: Know Before You Go to Get a Mortgage*.[3]

Much more needs to be done, particularly to rein in predatory and fraudulent lending practices and to keep borrowers from taking out loans that they can't repay. Recently, MMBA proposed expanded licensing, monitoring, and education for mortgage brokers, a largely unregulated group, who are usually the first contact with homebuyers and whose fees increase with the size of a loan. Primarily because of a lack of state funding, the proposal was dropped.

Today largely unregulated, out-of-state lenders are the primary source for mortgages in Boston. In 1990, local banks and credit unions controlled nearly 80 percent of the city's home mortgage market, but now they are down to 22 percent.[4] Nevertheless, Massachusetts banks make loans to lower-income and minority groups that outperform out-of-state companies' loans.

Solid, well-performing loans for low- and moderate-income borrowers are the result of good lending products and responsible lenders working with the state, municipalities, and not-for-profit organizations. The loans have predictable, stable monthly payments, and the payments are manageable for borrowers. Almost 40 banks and credit unions now originate loans under the SoftSecond Loan Program, administered by the Massachusetts Housing Partnership.[5]

The Borrower

It is important that borrowers understand the homebuying process and know where to get help if they run into difficulties. Every borrower obtaining financing through the SoftSecond Program must undergo prepurchase counseling and, prior to loan closing, must authorize foreclosure intervention by nonprofit organizations. The program is limited to first-time home buyers earning 100 percent of the area median income or less.[6]

Lenders offering SoftSecond loans issue two loans, one at 75 percent loan-to-value that is a conventional loan but issued at a somewhat below-market rate. The lender also provides a second mortgage at the same below-market rate. The borrower pays no principal on the second mortgage until the 11th year, and public resources may subsidize the interest payment for low-income borrowers. If there is an interest subsidy, it is phased out between years six and 10. Borrowers do not have to pay private mortgage insurance, and although a 3 percent down payment is required, some of that can be a gift or grant.

Since 1990, the SoftSecond Program has helped more than 8,700 low- and moderate-income first-time homebuyers, making it the state's most successful mortgage product for this group. In SoftSecond's 16 years of operation, there have been only 30 foreclosures. Astonishingly, there was only one foreclosure in 2004, three in 2005, and none in the first six months of 2006.

Even a small bank can be successful with SoftSecond loans. Boston Private Bank, which joined the program in 1996, had about $300 million in net assets at that time. Now a $2.2 billion full-service commercial bank, it has originated SoftSecond loans totaling more than $96 million since 2000. It has never experienced any losses with the program, demonstrating that a bank can do well while doing good.

Foreclosure filings are up. Boston had 24 in 2004 and 60 in 2005. In the first four months of 2006 alone, according to city officials, Boston experienced another 60 foreclosures.

For more than 15 years, MCBC has been the forum that has enabled the banks, public officials, and community organizations to collaborate on the credit and financial needs of lower-income people and neighborhoods. It has monitored the success of the SoftSecond Program and has developed improvements to benefit both lenders and borrowers.

Through such partnerships, increased public awareness, and leadership by government officials, nonprofit organizations and lenders will weather this storm. And if the legislature can bring CRA-like responsibilities to all mortgage lenders and can require continuing education and improved monitoring of mortgage brokers, Massachusetts will be way ahead.

Better regulatory oversight in all areas, but especially in fair lending, can ensure that minority-group borrowers and other vulnerable populations are not targeted unfairly by unscrupulous lenders and brokers. Programs to create educated homebuyers and interventions to prevent foreclosures can also help those who are most at risk. Finally, products that promote long-term stability in homeownership—products that work for both the lender and the borrower—will be good for the community overall.

Esther Schlorholtz *is senior vice president of Boston Private Bank and chair of the board of the Massachusetts Community & Banking Council.*

Endnotes

1 These results are reported in an analysis prepared for the Massachusetts Community & Banking Council (MCBC) by Jim Campen of the Gaston Institute at UMass Boston, *Borrowing Trouble? VI: High Cost Mortgage Lending in Greater Boston*, 2004, March 2006.

2 *The Boston Globe Magazine*, April 2, 2006.

3 See www.bos.frb.org/consumer/consumer pubs.htm.

4 Reported in an analysis prepared for MCBC by Jim Campen, *Changing Patterns XII: Mortgage Lending to Traditionally Underserved Borrowers and Neighborhoods in Greater Boston 1990-2004*, January 2006.

5 Jim Campen and Tom Callahan, "SoftSecond Program Celebrates 10 Years," *Communities & Banking*, spring 2001, 15.

6 MassHousing's programs are similarly innovative and can reach higher-income populations, up to 135 percent of the area median income. The programs fill a gap for higher-income minorities (more than $91,000 per year) who find fewer options. For example, in 2004, in spite of high earnings, upper-income African Americans received almost 45 percent of their home-purchase loans as high-cost loans. In contrast, only about 5 percent of upper-income whites did, according to the *Borrowing Trouble? VI* report. Meanwhile, upper-income Latinos received 42 percent of their home-purchase loans as high-cost loans.

Youth Flight

Are Housing Costs the Issue?

Illustration by Kirk Lyttle

by Elizabeth Humstone

A recent *New York Times* article on youth leaving Vermont elicited numerous comments from 18- to 20-somethings in the Green Mountain state. When asked why this once popular state is no longer their home of choice, they pointed to high housing costs, not enough diversity, limited higher-education choices, no nightlife, bad weather, and poor mobile-phone service. Chris Gignoux, a 26-year-old Vermont native, now in graduate school in St. Louis, says he wants to raise a family in his home state but worries he won't be able to afford a home there. An apartment similar to his St. Louis apartment would cost at least twice as much in Burlington.[1]

The Graying of New England

Although bad weather and lack of nightlife are not new, Vermont's population is aging, and that is exacerbating certain trends. According to the U.S. Census, Vermont's birth rate is the lowest in the country. Although Vermont has the highest number of colleges per capita, a disproportionate number of students attend college elsewhere (57 percent), and the percentage of graduates who return is declining.[2] The number of 20- to 34-year-olds in the state has shrunk by 19 percent since 1990, a more substantial decline than in the country as a whole. That could spell trouble for Vermont's higher education institutions, workforce, tax base, economic vitality, and creativity.

Vermont is not alone. As Neal Peirce and Curtis Johnson of the Citistates Group have written for the New England Futures project, "New England is already the nation's oldest region; by 2030 Maine, at 46.9 years median age, will be America's oldest state, and all six states older than the national average."[3] Meanwhile, the Southeast is attracting and retaining a young, skilled population. New England, though a bastion of higher education, had a net gain of 22,000 students (7 percent of total migration) in 2000 while the Southeast had a net gain of 96,000 students (25 percent of migration).[4]

New England's governors, business leaders, and educators are viewing this trend with alarm. What is the region's future without its youth? Where will tomorrow's workforce come from? Who will pay the taxes to support an aging population? Vermont's Governor James Douglas proposed funding for college scholarships with a postgraduate three-year residency requirement.

If New England is to thrive in the 21st century, retaining and attracting youth must be a priority.

In response the Vermont legislature set up a commission to develop a "Next Generation Initiative" with an appropriation of $5 million for scholarships. A program of the Maine Higher Education Consortium, "College for ME," aims to make its residents, including those already at work, the best educated in the country by 2019. The New England Board of Higher Education has initiated the College Ready New England program, designed to improve college attendance and completion rates regionally. And the New England Futures project has proposed strategies for colleges and universities to share resources, curb drop-outs, help immigrants become knowledge workers, and mentor graduates. Certainly, regional collaboration will be needed.

The Housing Issue

Why do so few youth who leave for college fail to return? Among the factors cited are a lack of cultural diversity and career opportunity. Peirce and Johnson also cite prices for home ownership and home rentals. "Soaring housing costs are fueling New England's youth exodus and its ability to attract new workers—white or blue collar," they write. "Massachusetts, Connecticut, Rhode Island, and New Hampshire rank among America's 10 least affordable states for renters." In addition, according to the National Association of Realtors, the median sale price of single-family homes in nine out of 11 of New England's metropolitan areas exceeds the national median by 15 percent to 120 percent. A Rhode Island housing group says that single-family homes are not affordable to families making $50,000 a year. Families making twice that are having trouble finding homes in nearly half the state's cities and towns.[5] Similar statistics are reported throughout New England.

High housing costs can lead to fewer jobs, too, because companies may relocate rather than pay higher salaries, and that further diminishes the opportunity for retaining youth. A 2005 New Hampshire study estimates that 1,300 to 2,800 jobs will be lost annually in the state if the tight housing market continues. The Vermont Housing Finance Agency found that "Vermont employers have come to see the rapid rise in housing costs as an economic concern, particularly in regard to the negative impact these costs have on companies' ability to hire and retain employees—and on employee performance."[6]

New England's elected officials, business leaders, and educators are taking action. In 2004, Massachusetts enacted Chapter 40R of the General Laws to increase the production of housing through financial incentives to

communities. Under 40R, communities designate zoning districts for high density, mixed-use development near town centers and transit stations—with 20 percent of housing units to be affordable. In return, they receive cash payments from the state.

Rhode Island requires communities to explicitly state in their plans how they will meet the housing needs of all income levels. Vermont and Connecticut have laws establishing housing and land-conservation trust funds to provide resources to nonprofits and municipalities to rehabilitate or construct buildings that can become affordable housing. Vermont's 20-year-old law has produced 8,000 perpetually affordable homes—about 3 percent of all year-round housing units.

Numerous models for encouraging affordable housing through regulations abound, but their use has not been widespread. Burlington, Vermont, requires that projects of more than five units make 15 percent affordable. To offset the additional costs to the developer, density bonuses are offered. Many communities are experimenting with smart-growth ordinances that provide high densities in designated growth areas featuring transportation and other services. Cambridge, Massachusetts, amended its zoning ordinance to allow higher density around transit stations.

Despite such efforts, opposition to housing projects still abounds, with neighbors worrying about traffic, loss of views, and possible cost increases for services. To counter this trend, the Vermont Smart Growth Collaborative—and similar organizations in other states—has housing-endorsement programs that provide certificates of endorsement and demonstrations of support at hearings for projects meeting smart-growth criteria. But it is too early to tell how successful they will be in increasing support for mixed-income and high-density housing.

Collaboration Is Key

In a positive development, more businesses are becoming involved. As a report for New Hampshire's Workforce Housing Task Force observes, "Concerned about their continued ability to retain workers and grow in the future, businesses are responding by offering relocation benefits, mortgage and rental assistance, and down-payment plans. They are also organizing in their communities to enact regulatory policies and practices which allow for the development of workforce housing," also called employer-assisted housing.[7]

Addressing the issue of youth flight in New England will take a concerted effort among governments, businesses, housing advocates, and educational institutions, and will require a regional strategy. Rather than tackle the challenges alone, the six states will gain more by sharing skills, tools, and experiences to come up with regional solutions. If New England is to thrive in the 21st century, retaining and attracting youth must be a priority.

Elizabeth Humstone, *a city planner, is a member of the Federal Reserve Bank of Boston's Community Development Advisory Council and Vermont adviser to the National Trust for Historic Preservation.*

Endnotes

[1] Cathy Resmer, "What Do They Want Already? Some Young Vermonters Reveal What It Will Take to Keep Them Here," *Seven Days*, March 15-22, 2006, 26-27A.

[2] Pam Belluck, "Vermont Losing Prized Resource as Young Depart," *The New York Times*, sec. 1, March 4, 2006.

[3] Neal Peirce and Curtis Johnson, "Growth Gamble New England: New Century, New Game" (Montpelier, Vermont: New England Futures, 2006), http://www.newenglandfutures.org/issues/growth/article/.

[4] A.T. Kearney, *Sustainable Prosperity: An Agenda for New England* (Boston: New England Council, 2005), http://www.newenglandcouncil.com/atKearneyReport.php.

[5] Associated Press, "Report: Home Ownership Too Expensive for Most Rhode Island Families," *Providence Journal*, November 17, 2005.

[6] Vermont Housing Finance Agency, "Housing and the Vermont Economy," Issue Paper, Jan. 30, 2006.

[7] Lisa Shapiro, Heidi Kroll, Hannah Kelly, Housing New Hampshire's Workforce, NH Workforce Housing Council, March 28, 2005, p. 3. See also Anna Afshar, "Employer-Assisted Housing," *Community Developments*, issue 1 (Federal Reserve Bank of Boston, 2006).

wanted

Getty Images

Past Authors

of Communities & Banking Magazine

Communities&Banking has been growing and changing since 1989, and it's time to plan a celebration to honor all our authors.

Where are you? Let us know at caroline.ellis@bos.frb.org so we can include you in an upcoming event.

Check out recent and long-ago **C&Bs** at **http://www.bos.frb.org/commdev/c&b/index.htm.**

Communities&Banking
New England's Forum for Low- and Moderate-Income Issues

Inside this issue:

Does Agriculture Matter?

Dairy Farm, Grand Isle, Vermont.

Communities&Banking is a publication of the Federal Reserve Bank of Boston's Public and Community Affairs Department, which covers economic education and exhibitions, consumer protection, and community development. Call (800) 409-1333 with questions. To be notified when the latest issue of *Communities&Banking* and other Bank publications are available on the web, sign up for the Bank's free E-Mail Alert! service at www.bos.frb.org/genpubs/email/index.htm.

FEDERAL RESERVE BANK OF BOSTON™

Communities&Banking

Public and Community Affairs
Federal Reserve Bank of Boston
600 Atlantic Avenue
Boston, MA 02210

Change Service Requested

FIRST CLASS
U.S. Postage Paid
Boston, MA
Permit No.
59702