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Building Nonprofit Developer Capacity Through Equity-Like Capital

Analyzing the effects of providing
PRIs to non-profit developers in the
Window of Opportunity Initiative



Evaluation of WOO Developer PRIs



- Context / Framing
- Summary of Key Findings
- Policy Implications
- Questions for Discussion

Window of Opportunity Initiative (WOO)



- **\$187 million initiative** of the John D. and Catherine T. MacArthur foundation to support rental housing preservation.
- Launched in 2000 and expanded in 2007. Aimed to preserve **300,000 rental units** by 2020.
- Employed a range of strategies, including:
 - Grants for research, policy analysis, and education
 - Program-related investments (PRIs) to non-profit developers, state/local preservation efforts, CDFIs, acquisition funds, and other initiatives
- Prior evaluation by RAND-USC focused on the initiative as a whole.
- This evaluation focused on effects of PRIs to developers.

WOO Developer PRIs



- MacArthur provided **\$42.5 million** in PRI funding to 20 nonprofit developers working in at least 40 states across the U.S.
 - **Unsecured, Entity-level capital, long-term** (10 years) with **low interest rates** (2%)
 - Eligible uses: (a) revolving pre-acquisition/acquisition/bridge capital; and (b) organizational working capital
 - Loan terms commenced in 2002-2009
 - Average PRI per participant: \$2.1 million
- Goal was to **strengthen** the **capacity** of nonprofit developers to engage in rental housing preservation activity at scale.
- Abt Associates and VIVA Consulting conducted this evaluation to study the effects of access to PRI capital on developers' capacity.

Evaluation Questions



1. To what extent and by what means did the WOO PRIs enable borrowers to **expand preservation activities** or **pursue new preservation strategies**? How did this capital aid these borrowers to **leverage other sources of funding** to further their preservation efforts?
2. Did access to entity-level financing influence **borrowers' organizational capacity**?
3. To what extent were the PRIs associated with changes in borrowers' (i) **balance sheet strength or profitability**, (ii) **sources of subsidy** or (iii) **ability to access capital**?
4. To what extent do other large nonprofit affordable housing developers have access to **entity-level financing**? How have they used that financing to support their activities and growth?

Methods



- Mixed-methods approach (qualitative and quantitative)
- Interviews with and a review of financial statements and production history over time from **17 WOO borrowers**
 - Two borrowers are no longer in operation (we prepared case studies on each one).
 - The 20th borrower returned the funds after deciding not to focus on preservation.
- Interviews with and review of financial data from **comparison group of 13 successful nonprofit developers**
- Interviews with **6 industry stakeholders**
- Limitations
 - Not a random-assignment evaluation. No true counter-factual.
 - Comparison developers selected retroactively, rather than at time loans were made.

Summary of key findings



Research Question 1: Effects on Preservation Activities

- Borrowers used PRIs to expand preservation activities. Appreciated flexibility and long-terms. The 17 examined borrowers preserved 50,800 units during life of PRIs.

Research Question 2: Effects on Organizational Capacity

- Borrowers added staff, expertise and systems to facilitate increased preservation.

Research Question 3: Effects on Financial Condition

- All 17 of the examined borrowers ended in a significantly stronger financial position.
- WOO borrowers experienced larger growth in total and net assets than comparison developers. The two groups otherwise had similar financial trajectories

Research Question 4: Access to Equity-Like Capital

- All comparison developers eventually gained access to equity-like capital, though generally later than WOO borrowers.
- WOO PRIs provided a leading role in demonstrating value of entity-level capital.

WOO borrowers expanded their preservation activities



- Those borrowers who had previously focused more on new development expanded their preservation activities.
 - Continued to engage in new development, but built their acquisition and preservation capacity.
- Those borrowers who were already focused primarily on preservation grew their overall businesses.
- Several borrowers were relatively new enterprises; they were able to launch and grow successfully.
- Over time, most groups evolved their preservation/new development balance in response to changing economic conditions and opportunities.
- In total, the 17 examined WOO borrowers report preserving 50,800 units of affordable housing and securing more than \$5.6 billion in capital to support this work.
 - Count includes all units developed by the 17 borrowers in this timeframe, whether or not they used PRI funds.

WOO funds contributed to development of organizational capacity




- Several groups explicitly hired or developed acquisition/preservation teams.
 - Integrated these teams and activities into broader organizational structure over time.
- Organizations built their transactional and financial sophistication as they engaged in more and more varied preservation deals.
- While WOO funds were used as intended for preservation activities, greater liquidity and stronger balance sheets facilitated organizations' expansion into new business lines.
 - New kinds of preservation: RAD, NOAH.
 - Entirely new housing-related enterprises: weatherization training, assisted living/health care.
 - Improvement/preservation of the organizations' owned housing portfolios.

Funds were primarily used on a revolving basis for acquisition and predevelopment



- Repaid in most cases from permanent financing.
 - About 2/3 of the deals were eventually refinanced with LIHTC.
 - WOO funds did not materially enable diversification away from traditional subsidy sources.
- In a small number of deals, funds were used as gap-fillers to allow transactions to proceed.
 - Repaid from other sources: cash flow from other deals, refinancing of other properties.
- 1/3 of units preserved were already owned/controlled by WOO borrowers.
 - Some of these refinancings generated significant additional capital for the borrowers.
- In many cases, MacArthur funds functionally became part of a bigger revolving pool used to seed acquisitions and predevelopment.

Long-term PRIs enabled borrowers to buy and hold properties



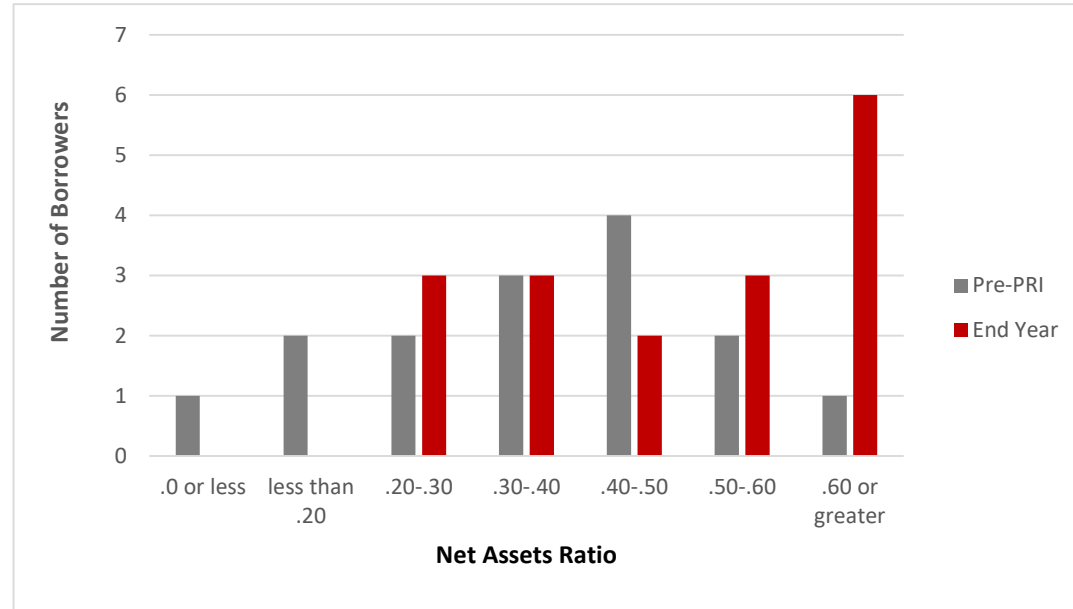
- Developers were able to purchase properties even if the long-term refinance strategy was not immediately at hand.
 - Greater ability to take calculated risks was a primary benefit of the PRIs.
- WOO funds helped borrowers weather recession.
 - Capital markets stalled many deals; long-term PRIs enabled borrowers to hold properties until conditions improved and deals could proceed.
 - With their extra economic strength, some borrowers were able to take advantage of special opportunities during the recession: (a) ARRA and HERA programs, (b) lower acquisition prices.
- WOO funds helped borrowers weather other project obstacles.
 - Zoning challenges, delayed funding awards

WOO loans catalyzed capital accumulation

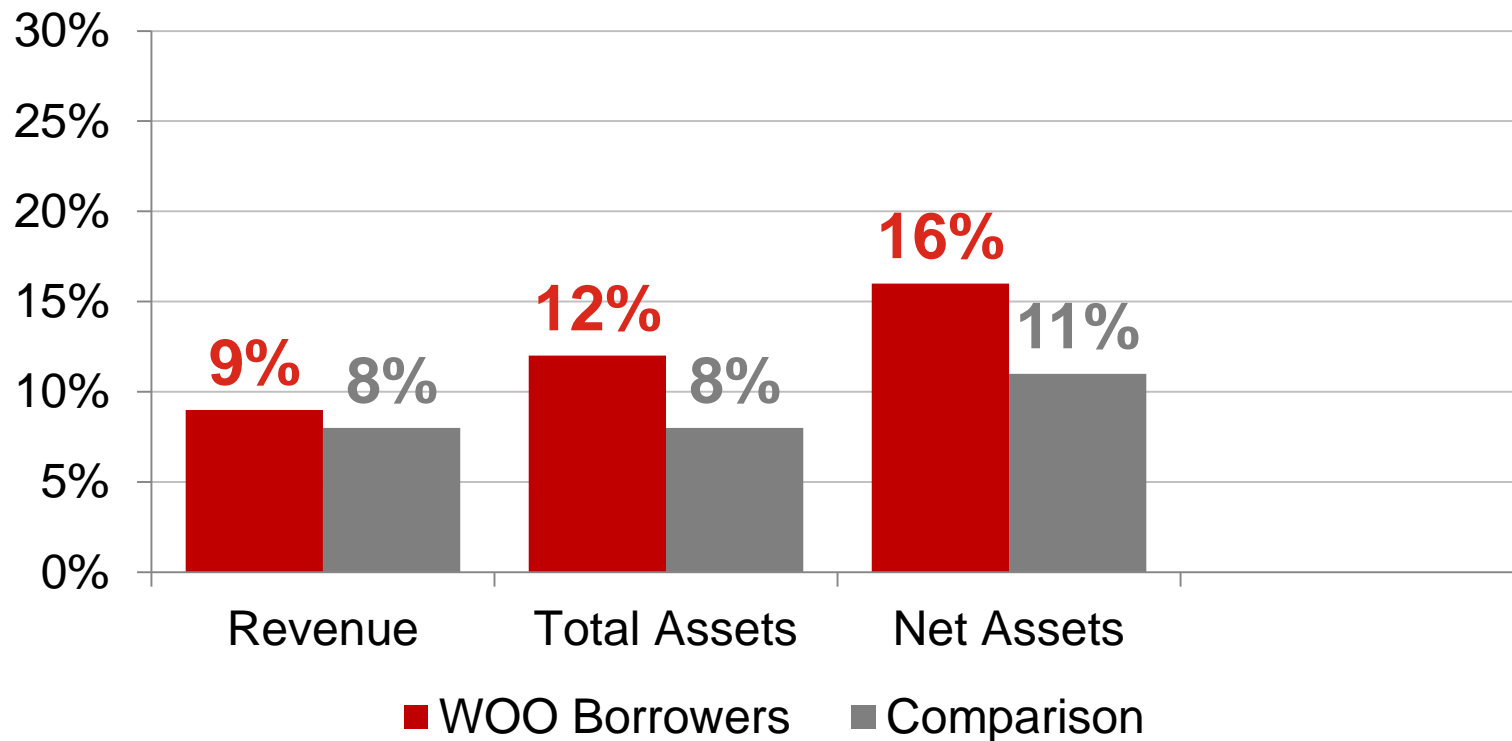
- Changed the way borrowers thought about their financial structure.
 - Expanded staff focus on raising capital (through PRIs, equity programs).
 - Helped organizations build credibility with other lenders.
 - Introduced boards of directors to revolving acquisition/predevelopment funding pools.
- MacArthur program was critical in early industry dialogue about the importance of equity-like capital for nonprofit developers.
- WOO funds were used for activities that were profitable equity-builders for the borrowers.
 - Refinance of portfolio properties

WOO borrowers ended loan terms in a stronger financial position

- All 17 of the WOO borrowers we analyzed ended their loan terms in a stronger financial position
 - Improvement in measures of net worth and liquidity (the current ratio and months of unrestricted cash).
 - Revenues, total assets, and net assets all grew steadily during this period.
 - Exhibit shows growth over time of **net assets ratio**, the ratio of equity (assets – liabilities) to total assets.
 - A new assets ratio of .20 means entity has equity equal to 20% of its total assets.



Average Annualized Growth Rates



Outstanding Questions / Next Steps



- Outstanding Questions
 - Sustainability – To what extent will WOO borrowers continue to be in a strong financial position five or ten years after repaying the PRI?
 - How will borrowers cope with changes in the nature of preservation challenges?
- Next Steps
 - Finalize written report and publish in coming months.
 - Email *Kimberly_Burnett@abtassoc.com* for a copy of the report.

Policy Implications



- Overall, the strategy of investing in non-profit developers appears to have been successful.
 - Can / should this strategy be applied to other contexts?
- Equity and equity-like capital facilitate production / growth.
 - WOO PRIs played a leading role in demonstrating value.
 - Nearly all of the comparison group developers eventually gained access to similarly flexible capital.
 - Regional economic conditions appear to play a role in creating opportunities to harvest equity, leading to regional disparities in access to equity / equity-like capital

Questions for current discussion



- How has the need for equity-like capital changed in the current environment?
 - Is there a different kind of capital that nonprofit developers need now? What kinds of activities could additional, or differently configured, capital open up for nonprofit developers?
- How has the preservation challenge changed, if at all, in the past decade?
- Most interviewees said that the biggest current obstacles to preservation are acquisition and construction pricing.
 - How can nonprofits counter these obstacles?
- How can the philanthropic community best support the nonprofit community in expanding the development and preservation of affordable housing?

Contact

Kimberly Burnett
Senior Associate

Kimberly_Burnett@abtassoc.com



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